STATE BAR OF TEXAS
BANKRUPTCY LAW SECTION
NEWSLETTER

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JUDICIAL PROFILE: THE HONORABLE LEIF M. CLARK OF THE WESTERN DISTRICT OF TEXAS UNITED STATES BANKRUPTCY COURT

By: Debra L. Innocenti, Associate with Oppenheimer Blend Harrison and Tate, Inc. (dinnocenti@obht.com)

Judge Leif M. Clark lit up the blogosphere when he issued an order that denied a defendant's motion "for being incomprehensible" and—here, of course, is the pith—quoted a screwball Adam Sandler film in the process. Clark penned in his now infamous footnote:

> Or, in the words of the competition judge to Adam Sandler's title character in the movie, "Billy Madison," after Billy Madison had responded to a question with an answer that sounded superficially reasonable but lacked any substance,
>
> "Mr. Madison, what you've just said is one of the most insanely idiotic things I've ever heard. At no point in your rambling, incoherent response was there anything that could even be considered a rational thought. Everyone in this room is now dumber for having listened to it. I award you no points, and may God have mercy on your soul."
>
> Deciphering motions like the one presented here wastes valuable chamber staff time, and invites this sort of footnote.

The Sandler citation even earned him the honor of *The Wall Street Journal* Law Blog's first ever "Judge of the Day."

Clark's impatience with lazy thinking was no surprise to the many bankruptcy attorneys who know him well, although we *were* a bit surprised at the choice of reference. Clark has always been the thinking man's judge. Attorneys appearing for the first time before his bench are usually advised that, no matter the subject, Clark will know the law.[1] His bankruptcy students at The University of Texas School of Law—of which I was one—likewise learned quickly that his legal acumen is both broad and deep. Rarely would an esoteric question from the auditorium produce much of a pause.

That reputation has been long in the making. Clark has spent most of his life wrestling with hard questions and what he calls a "coherent" discourse—that is, a rigorous, honest approach to thinking through problems. As a young man, he studied philosophy in preparation for his then-intended post-graduate studies in theology. His favorite reads were Locke and Hume, empiricists who required that theories be tested against observations of the natural world, as well as Kant and Wittgenstein, rigorous thinkers who refused to confine their philosophical constructs to accepted norms. His reading solidified in him a belief that the apparently unanswerable questions are worth pursuing, but that the true reward is often not in the answers, but in the coherence and integrity of the attempt.

After earning his undergraduate degree in 1968, Clark enrolled at Trinity Lutheran Seminary in Columbus, Ohio. There, his penchant for oral argument was honed against classmates of like intellect. "There were no off-limit discussions," Clark reflected. "We made religion face the hard questions."

Although his friends worried about Clark's survival—the headlights of his eight-year-old Dodge were permanently aimed outward from its numerous meetings with the seminary's brick wall—he managed to graduate with all his limbs intact and a Master of Divinity degree to boot. Lee Rupert, his roommate from seminary, would later remark at Clark's swearing in as bankruptcy judge that Clark had accepted a new calling—though this one called for black robes rather than white.

After years of oral argument against "theologians with a capital T," the intellectual rigors of law school were comparatively easy, though the volume of work and the discipline of detail offered its own new challenges. Clark attended the University of Houston Law Center and graduated in 1980 with honors. He started his law career with the San Antonio law firm Cox & Smith, where he hoped he would be practicing tax litigation, but

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REVIEW OF THE 28TH ANNUAL JAY L. WESTBROOK

By: Eric M. Van Horn (Rochelle McCullough LLP—Dallas; evanhorn@romclawyers.com) with contributions from Sonja D. Sims (Law Offices of Sonja D. Sims—San Antonio; sonjasimsesq@yahoo.com) – members of the Young Lawyers Committee[1]

The University of Texas CLE held the 28th Annual Jay L. Westbrook Bankruptcy Conference on November 19-20, 2009 at the Four Seasons Resort & Spa in Austin, Texas. **Berry D. Spears** (Austin), the **Hon. Leif M. Clark** (San Antonio), **Deborah B. Langehennig** (Austin), **Vicki M. Skaggs** (McAllen), served as this year's presiding officers and were guided by the members of the conference's planning committee.[1]

The conference featured speakers from throughout Texas and across the country, and was widely attended by several hundred, including many of our Texas bankruptcy judges and many of our new non-lawyer bankruptcy professionals. With its fantastic line up of speakers, presentations, and networking opportunities, the conference was a great success. For those in the Section who were unable to attend, below (courtesy of members of the Young Lawyers Committee) are summaries and pictures of presentations and events.

PRESENTATION SUMMARIES

Opening Remarks: **Professor Jay L. Westbrook** of The University of Texas School of Law opened the conference with a few humorous remarks about the banking industry and its current state of affairs. Prof. Westbrook explained that his son as a young child would tell people that his dad was a bankruptcy lawyer which meant that he dealt with "exploding banks." Prof. Westbrook acknowledged the near literal truth of that description and then remarked that "for $2 you can buy a share of Citibank." **Berry D. Spears** then welcomed attendees and introduced the first panel.

Recent Developments: The conference began with a survey of important case law developments from around the country moderated by **Prof. Jay L. Westbrook** (Austin), and presented by **R. Bryn (Byrnie) Bass, Jr.** (Lubbock), **Evelyn H. Biery** (Houston), **Deborah B. Langehennig** (Austin), and **Deborah D. Williamson** (San Antonio). The panel highlighted many significant bankruptcy and non-bankruptcy cases that will impact both consumer and business practices including: *In re Dale,* 582 F.3d 568 (5th Cir. 2009); *In re Eastman,*419 B.R. 711 (Bankr. W.D. Tex. 2009); *Matter of ProEducation Int'l Inc.,* 587 F.3d 296 (5th Cir. 2009); *Ogle v. Fidelity & Deposit Co. of Maryland,* 586 F.3d 143(2nd Cir. 2009); and *In re Philadelphia Newspapers, LLC,* 4018 B.R. 548 (E.D. Pa. 2009). The panel previewed the bankruptcy cases to be argued before the Supreme Court (*Espinosa v. United Student Aid Funds, Inc.; Milavetz v. United States;* and *Schwab v. Reilly.* The panel also noted a few cases that only bankruptcy professionals could find interesting or humorous. For example, Prof. Westbrook mentioned a case involving a creditor-trash collector that dumped a 5 feet high and 20 feet long mound of trash on the debtor's property (*In re The Original Barefoot Floors of America, Inc.*, 412 B.R. 769 (Bankr. E.D.Va. 2008). While it was a case about whether the automatic stay was violated (the court held no violation), Prof. Westbrook quipped that it was also a "discharge" case.

Discharge and Dischargeability Update: Manville, Espinosa and Beyond: Sporting a custom made bowling shirt with mountains and the phrase "High on BAPCPA" (see picture in this issue), the always entertaining and informative **Hon. Keith Lundin** (Bankr. M.D. Tenn) reviewed recent developments in discharge and dischargeability litigation including significant appellate decisions involving Sections 727 and 523. Judge Lundin also covered the impact of the Supreme Court's recent *Manville* decision and the anticipated decisions from the Supreme Court in *Espinosa* and *Schwab.*

The Coming Wave of Real Estate Bankruptcies and What You Need to Know about Them (but Either are Too Young to Know or Too Old to Remember): Moderated by **Joseph J. Wielebinski** (Dallas) and presented by panelists **Mark E. Andrews**, the **Hon. Stacey G.C. Jernigan** (Bankr. N.D. Tex. – Dallas), **Clifton R. Jessup, Jr.** (Dallas), and **Michael A. McConnell** (Ft. Worth), this panel discussed key issues in past bankruptcies that might be applicable to the anticipated surge of real estate filings. These issues and cases included the bad faith filing standards under the Fifth Circuit's *Little Creek* decision, identifying single asset real estate debtors, cash collateral and adequate protection, bankruptcy remote entities, and many others.

Geopolitics, Technology, and Prospects for the U.S. Oil and Gas Industries: A.F. Alhajji of NGP Energy Capital Management, LLC (Irving) provided an interesting and informative luncheon presentation about the future of the oil and gas industry in the United States. Mr. Alhajji explained how we got to where we are today, the global surge in demand for oil and gas, and why renewable energy will not be able to fill that demand.

A Practical Guide to Restructuring and Bankruptcy Issues in the Energy Sector – What's Old is New: Seasoned bankruptcy practitioners with significant oil and gas experience **Charles A. Beckham, Jr.** (Houston) and **Harry A. Perrin** (Houston) discussed the lessons they learned from their experiences in the 80's and how those lessons may apply today to executory contracts, avoidance issues, creditor remedies and derivatives.

Federal Rules Update – Highlights for Bankruptcy Practitioners: **Leslie R. Masterson** (Plano), judicial law clerk for the Hon. Brenda T. Rhodes (Bankr. E.D. Texas – Plano) provided an overview of the new time and deadline computation rules and the new Bankruptcy Code time periods that changed effective December 1, 2009. Ms. Masterson highlighted the many changes to the Federal Rules of Bankruptcy Procedure and the Bankruptcy Code, including the rules which changed five-day periods to seven; 10-day periods to 14; 15-day periods to 14; 20-day periods to 21; and 25-day periods to 28. The presentation also covered changes to time periods for summary judgment motions and for amending petitions.

New 502, Evidence and e-Discovery: **Demetra L. Liggins (Houston)** explained the purpose, substance, and effect of the new rule and issues in the bankruptcy context. Ms. Liggins provided a detailed discussion of new Rule 502 to the Federal Rules of Evidence which included remedies and reasonable steps for attorneys who inadvertently disclose a privileged document, as well as how to prevent an opponent from using the document.

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WESTBROOK CONFERENCE PHOTOS

Recent Developments Panel:
Prof. Jay L. Westbrook, Evelyn Biery, Debbie Langehennig, Deborah Williamson, and Byrnie Bass

Discharge and Dis-chargeability Update:
Judge Keith Lundin

Federal Rules Update: Highlights for Bankruptcy Practitioners
Leslie Masterson

Real Estate Wave Panel:
Mark Andrews, Clifton Jessup, Mike McConnell, and Joe Wielebinski

Post-Confirmation Modification of Ch 13 and Ch 11 Individual Plans:
Judge Alan S. Trust

Reorganizations in the Shadow of Chrysler and GM: Bruce Grohsgal and Hugh M. Ray, Jr.

Putting the Judge Back In Charge:
Michael "Buzz" Rochelle, Judge Leif M. Clark, and Judge William M. Schultz

The CRO Unhinged:
A. Mechele Dickerson

Bankruptcy Issues in the Energy Sector: What's Old Is New
Harry Perrin and Charlie Beckham

Westbrook Conference Photos

An Unhappy Union? The Impact of Employment Issues on Chapter 11 Cases: James Landon

Estate and Derivative Litigation: Marty Brimmage, Judith Ross, and Michael Sutherland

363 Sales v. Plans: Judge D. Michael Lynn, Prof. Jay L. Westbrook, and Judge Eugene R. Wedoff

363(k) Credit Bidding Issues: Edward Ripley, Abid Qureshi, Chris Dickerson, and Mark Wege

Ipso Facto Clauses: New and Improved Elizabeth Guffy and Thomas Henderson

Update on the Economy and the Banks: Prof. Sanford J. Leeds III

New 502, Evidence and e-Discovery: Demetra Liggins

Loss Mitigation in Bankruptcy: Debbie Langehennig, James Bailey, and Steve Turner

Ad Valorem Tax Problems in Consumer and Small Business Bankruptcy Cases: Laura Monroe

Conference Reception

Young Lawyers Evening Reception

Young Lawyers Evening Reception

Results From The 2010 Elliott Cup Held in New Orleans February 19-20

On February 19th and 20th, the Annual Fifth Circuit Elliot Cup Moot Court Competition Sponsored by the Texas State Bar Bankruptcy Section - and named in Honor of the Honorable Joseph Elliot, former Chief Bankruptcy Judge for the Western District of Texas - was held at the Fifth Circuit Court of Appeals in New Orleans, Louisiana. Thirteen law school teams from around the Fifth Circuit attended the Elliot Cup. The team of Ms. Kelli Benham and Mr. Rex Mann, from the University of Texas School of Law, was the winning team for this year's Elliot Cup competition, with coaches Ms. Debbie Langehennig, Chapter 13 Trustee, and Mr. Jay Ong of Munsch Hardt Kopf & Harr, P.C. Ms. Benham also garnered the Best Advocate Award at the competition.

The Elliot Cup serves as a run-up to the Annual National Duberstein Bankruptcy Moot Court Competition held at St. John's School of Law in New York in March, and Elliot Cup teams have historically posted excellent results at the national competition. Best of luck to all Elliot Cup teams at this Year's National Duberstein Competition, and many thanks to the numerous judges and attorneys involved in the events for the benefit of aspiring young bankruptcy lawyers.

Congrats to the Winning Team:
Ms. Kelli Benham
and Mr. Rex Mann

FIFTH CIRCUIT CASE LAW UPDATE

VIOLATING THE COURT'S ORAL INJUNCION… NOT A WISE MOVE IN THE FIFTH CIRCUIT

By: Misty Escobedo, Judicial Extern to the Honorable Harlin D. Hale and recent graduate of the SMU's Dedman School of Law (mreeder@smu.edu)

Good Day Mr(s) ____________. Your mission, should you choose to accept it, is to dispose of property belonging to the bankruptcy estate. The court has issued an oral injunction prohibiting the disposal of the estate's assets held in Trust. Your window of opportunity is short. You must complete your mission before the Court's written order is entered into the record. If you are caught you will pay the piper. This message will self-destruct in 10… 9…8…

If only this was really how bankruptcy worked. In *Ingalls v. Thompson*, (*In re Bradley*), 588 F.3d 254 (5th Cir. 2009), the court determined that a party who fails to comply with an oral injunction order of a bankruptcy court is eligible for civil contempt sanctions. Sadly, one man had to learn the hard way that a bankruptcy court's oral injunction does not need to be memorialized in a formal written order to be both powerful and binding. This is his story…

MISSION LOG

Gary Bradley declared bankruptcy in July 2002. Sometime thereafter the court found that the transfer of assets Bradley had made to the Lazarus Exempt Trust before filing bankruptcy was part of a fraudulent scheme and enjoined the trustee, Bradley Beutel, from removing assets from the Trust. *Id* at 258. However, that injunction expired with the conclusion of the trial on the merits in the bankruptcy court. *Id*.

Almost immediately following the trial Beutel began making preparations to sell significant portions of the Trust assets while the court's decision on the adversary proceeding was pending. *Id*. at 258. Ronald Ingalls, Chapter 7 Trustee, together with the United States and FDIC as creditors filed a motion to maintain the injunction pending the court's ruling on the adversary proceeding. *Id*. Mr. Beutel did not attend the hearing on the motion but his attorney testified that there were plans to sell part of the Trust assets. *Id*. The court issued an oral injunction and instructed Mr. Beutel's attorney to draft the order. *Id*. at 259. It took another month for the court's ruling to be memorialized in a written order. *Id*. Within weeks of the court issuing its oral injunction Beutel had finalized the sale of several of the Trust assets. *Id*.

Beginning September 9, 2004, Beutel began to disperse funds received from the sale to various entities controlled by the trust, himself, and Bradley. The next day, Beutel filed a Motion to Approve Disbursements, seeking permission to make certain transfers contrary to the injunction previously announced. It was not until September 20, 2004, that the bankruptcy court issued its ultimate written injunction, with terms essentially corresponding to those it had announced at the hearing. *Id*. 259.

The next month, Ingalls, FDIC, and the United States filed a motion for contempt. *Id*. Several years passed before the bankruptcy court found Beutel in contempt both personally, and in his capacity as trustee, for "transferring Trust property and failing to retain the consideration received in the entities that sold the property." *Id*. at 260. Sanctions were imposed. *Id* at 259-61. Beutel eventually settled with Ingalls, personally, but Tommy Thompson, successor trustee, appealed the contempt order and sanctions in his capacity as trustee. *Id*. at 261.

Thompson made three arguments on appeal. *Id*. Most significantly was his assertion that without a written order he was under no compulsion to comply with the court's oral injunction. *Id*. Relying on authority from the Seventh Circuit, he challenged the court to either break with the Seventh Circuit's ruling or overturn his contempt conviction. *Id* at 262. The Fifth Circuit declined to take either road. *Id*.

CIVIL OR CRIMINAL CONTEMPT: WHAT'S THE DIFFERENCE?

The court started its analysis by determining whether or not the contempt was civil or criminal. *Id* at 263. Civil and criminal contempt are defined by their purpose. *Id*. (quoting *Lamar Fin. Corp. v. Adams,* 918 F.2d 564, 566 (5th Cir. 1990)). Civil contempt is used to coerce compliance with the court's orders or to compensate others for the party's violation. *Id*. No special safeguards are required, i.e. establishing the *mens rea* or proving the case beyond a reasonable doubt. *Id*. On the other hand, criminal contempt is a means to punish the non-compliant party and vindicate the power of the court. *Id*. In either instance a failure to comply with the court's order can lead to jail time or monetary damages. *Id*. In the case of civil contempt, the prison sentence must be conditional and coercive; monetary damages accrue over time. *Id*. Conversely, prison terms for criminal contempt are meant to punish past conduct and are unconditional; monetary damages are enforced as a lump sum. *Id*.

By issuing a contempt order that required Thompson to repay the bankruptcy estate the money he had divested, the court found him guilty of civil contempt, specifically compensatory or remedial contempt. *Id*. This kind of contempt, like criminal contempt, is backward looking; however, its intent is not to punish but to compensate the violated party for the contemptuous actions. *Id*. This kind of contempt order survives the underlying litigation and can be enforced even after the litigation has concluded. *See Id*. at n 8.

DOES THE BANKRUPTCY COURT HAVE THE POWER?

But does the bankruptcy court have the power to enforce its orders by contempt? Criminal contempt is governed by 18 U.S.C. § 401. However, the power of 18 U.S.C. § 401 is limited and for the most part unavailable to bankruptcy courts. *Id* at 265-66. Bankruptcy courts only have the power to enforce criminal contempt if the contemptuous act occurs in the court's presence. *Id*. On the other hand, civil contempt is an inherent power of the federal courts. *Id* at 265. More particularly, the Fifth Circuit has determined that the bankruptcy court's civil contempt power derives from 11 U.S.C. § 105. *Id* at 266.

ESTABLISHING THE ELEMENTS: WHEN IS THE COURT'S ORDER *IN EFFECT?*

Thus having established that the contempt was civil and the court had the power to enforce its orders by civil contempt, the next question becomes whether or not the elements of civil contempt were met. There are three elements of civil contempt "(1) that a court order was *in effect*, (2) that the order required certain conduct by the respondent, and (3) that the respondent failed to comply with the court's order." *Id* at 264. This case essentially turns on the first element. Thompson argued that the court's order was not *in effect* because the oral injunction had not yet been reduced to writing. To

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Fifth Circuit Case Law Update II - *Kennedy v. Mindprint*: A Not-So-Irrebuttable Presumption — The Fifth Circuit Narrows the Imputed Conflicts Rule

By: Caleb D. Trotter, Judicial Extern to the Honorable Harlin D. Hale, third-year student at SMU's Dedman School of Law and joining Munsch Hardt Kopf & Harr, P.C. in 2010 (ctrotter@smu.edu)

Introduction

Attorneys are on the move more than ever before. Since the early 1980's, the number of attorneys changing law firms has risen sharply. Lateral hiring at most law firms now significantly outpaces entry-level hiring. With large percentages of both associates and partners moving from firm to firm, the number of complex conflicts of interest issues has become a very real issue in today's legal marketplace. One of these issues arises when an attorney leaves one large law firm and goes to another. Texas courts have always been hesitant to impute any conflict of interest from the transferring attorney onto the members of the new law firm. However, what has been less clear is whether transferring attorneys carry with them a duty not only to *their* former clients at the old firm, but also the clients of all of his former associates, regardless of any actual relationship or exchange of confidential information. The Fifth Circuit in 1971, and again in 1981, described this latter type of duty in terms of an "irrebuttable presumption": it was to be presumed, no matter the facts of the situation, that all confidences received by one attorney are imputed to all associates and employees of that attorney. Thus, when an attorney moved from one firm to another, he carried with him duties to all clients of his former firm, regardless of whether that attorney gained any actual knowledge of, or confidential information about, those clients. The Texas Supreme Court has never addressed this particular situation, but in 2009 the Fifth Circuit re-evaluated its position on the issue in *Kennedy v. MindPrint (In re ProEducation Int'l, Inc.)*, 587 F.3d 296 (5th Cir. 2009). The Circuit's conclusion may have a far-reaching impact on the modern legal community.

Factual Background

In an adversary proceeding to *In re ProEducation International, Inc.*, the bankruptcy court disqualified an attorney, Kirk A. Kennedy, representing judgment creditor Dr. Mark Andrea. Kennedy worked in the Houston offices of Jackson Walker, L.L.P., from February 2003 through November 2004. While working at Jackson Walker, Kennedy's office was located down the hallway from another bankruptcy attorney, Lionel Schooler. Mr. Schooler had been representing MindPrint since 1999, in a state court case against ProEducation.

Dr. Andrea was one of several ProEducation shareholders who had taken a position adverse to MindPrint in that same state court action in 1999. ProEducation filed for Chapter 7 bankruptcy in November of 2000, and the state court case was removed to bankruptcy court as an adversary proceeding. Schooler continued to represent MindPrint throughout the adversary proceeding and all matters pertaining to the ProEducation bankruptcy. These services provided by Schooler coincided with the period during which Kennedy worked in the same office of Jackson Walker. The bankruptcy court proceedings entered judgment in favor of MindPrint and the group of shareholders against ProEducation. MindPrint subsequently filed a motion for sanctions against the group, which was denied. MindPrint appealed the denial of sanctions, and that motion was heard in November of 2005.

When Kennedy left Jackson Walker in November of 2004, he took a position as the general counsel of Gulf Coast Cancer Center, where Dr. Andrea worked as the medical director. The attorney who had been representing Dr. Andrea in the adversary proceeding withdrew from the case in November of 2005, before the appeal on the motion for sanctions. Kennedy subsequently became Dr. Andrea's counsel, and MindPrint immediately objected because of Kennedy's former association with Jackson Walker. While Kennedy did not formally enter an appearance, he did contribute to a brief filed on Dr. Andrea's behalf. Kennedy continued to work on the appeal of the adversary proceeding, including taking discovery and collection efforts from the judgment. Kennedy ultimately filed a motion to appear on behalf of Dr. Andrea.

Procedural Background

MindPrint again objected to Kennedy's representation of Dr. Andrea, and filed a motion to disqualify him on grounds of an imputed conflict of interest. The bankruptcy court granted the motion, finding that Jackson Walker's attorneys' knowledge of MindPrints' confidential information "extends to former employees." The court concluded that confidential information had been given to the attorney actually doing work for the client, Mr. Schooler, and that confidences obtained by an individual attorney are shared with other members of the firm. The bankruptcy court's ruling was affirmed on appeal by the United States District Court for the Southern District of Texas. Kennedy appealed to the Fifth Circuit.

The Rules of Professional Conduct

The issue for the Fifth Circuit on appeal was whether a concurrent conflict should be imputed to a former associate who had no actual knowledge of the case or client involved. As it had done in the past, the Firth Circuit considered both the Texas Rules of Professional Conduct and the ABA Model Rules of Professional Conduct in reviewing the issue. Texas Rule 1.09 and Model Rule 1.9 both cover attorney's duties to former clients, and both lay out the circumstances for when conflicts are imputed to current and former associates. As such, both Texas Rule 1.09(b) and Model Rule 1.9(b) impute the personal conflicts of one attorney to all other members of a firm. The Court paid special attention to the Comments of both Rules. Comment 7 to Texas Rule 1.09, added in 1990, states that the imputation can be removed when an attorney leaves a firm, so long as the departing attorney never personally represented the former client. Likewise, Comment 6 to Model Rule 1.9 states that imputation to a former associate will depend on the "situation's particular facts", and places the burden of proof upon the attorney whose disqualification is under review. The Court concluded that both Rules, despite linguistic differences, require that a departing attorney must have either personally acquired confidential information about the client, or personally represented the client to remain under imputed disqualification.

Should the Presumption be "Irrebuttable"?

This construction by the Fifth Circuit differs from several of the Circuit's prior rulings, in that it seems to allow an attorney, formerly associated with a firm, to offer evidence showing that they never personally represented a former client, and never actually acquired confidential information about that client, and thus there should be

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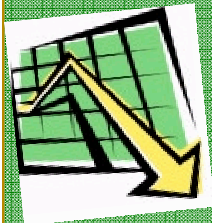

Chapter 11 practice: Post-Confirmation Claims in a Post-Modern World: *In re Texas Wyoming Drilling, Inc.* and Its Impact on Preservation of Claims

By Evan R. Baker, (evan.r.baker@gamil.com), Judicial Extern to The Honorable Stacey G.C. Jernigan and Incoming Judicial Law Clerk for the Honorable Lewis M. Killian, Jr. of the Northern District of Florida

Under the Code, a debtor, trustee, or representative of the debtor estate may include in a plan the right to retain or enforce any claim or interest of the estate. 11 U.S.C. § 1123(b)(3)(B); *see also In re United Operating,* 540 F.3d 351, 355 (5th Cir. 2008). Thus, the way a debtor may preserve its standing to pursue a post-confirmation claim is "if the plan of reorganization expressly provides for the claim's 'retention and enforcement by the debtor.'" *In re United Operating*, 540 F.3d at 355 (quoting 11 U.S.C. § 1123(b)(3)(B)). In order to preserve such post-confirmation claims, the debtor must have first established the claim with a reservation that is "specific and unequivocal." *Id.* (citing *Harstad v. First American Bank*, 39 F.3d 898, 901 (8th Cir. 1994)). If a "blanket reservation" of "any and all claims" is insufficient under *In re United Operating*, how specific should a reorganization plan be to preserve a debtor's post-confirmation claim? *See In re Texas Wyoming Drilling, Inc.*, 2010 WL 276653 at *7 (Bankr. N.D. Tex Jan. 20, 2010).

A recent opinion in the Fort Worth Division of the Northern District of Texas sheds light on the application of *In re United Operating* and other cases dealing with the standing issues created by post-confirmation claims. In a joint opinion of *In re Texas Wyoming Drilling, Inc.* and *In re Lori Lyn Ranzino-Renda*, Judge Lynn ruled that *In re United Operating* should not be applied in "so draconian a fashion as to disserve the interests of creditors and frustrate pursuit of claims which may have merit." *Id.* at *6.

Facts

In re Texas Wyoming Drilling, Inc.

Texas Wyoming Drilling, Inc. ("TWD") filed for chapter 11 protection in April of 2007 and a plan of reorganization was confirmed in October of 2008. After confirmation of the TWD Plan, TWD brought an adversary proceeding against multiple defendants claiming that dividend payments distributed prior to the Petition Date were made while TWD was insolvent, and thus were avoidable fraudulent transfers under section 548 of the Code.

The TWD Defendants responded to the complaint by asserting TWD lacked standing to pursue its claims because it "failed to preserve such as to the TWD Claims with adequate language in the TWD Plan." *Id*. at *2. The TWD Defendants also asserted that TWD was judicially estopped from pursuing claims, which were also *res judicata*.

The relevant part of TWD's Plan of Reorganization stated, "the Reorganized Debtor shall retain all rights, claims, defenses, and causes of action including, but not limited to, the Estate Actions." The Plan defined "Estate Actions" as:

> any and all claims, causes of action and enforceable rights of the Debtor against third parties, or assertable by the Debtor on behalf of creditors, its estate, or itself…for recovery or avoidance of obligations, transfers of property or interests in property…recoverable or avoidable pursuant to Chapter 5 or other sections of the Bankruptcy Code or any applicable law.

See Id. at *3.

TWD was found to have been in material default under the terms of its Plan, whereupon the case was converted to chapter 7, which resulted in the substitution of the chapter 7 trustee as the Plaintiff in the adversary case.

In re Lori Lyn Ranzino-Renda

Lori Lyn Ranzino-Renda sought protection under chapter 13 of the Bankruptcy Code in September of 2006, and her case was converted to a chapter 11 case several months thereafter. Upon the confirmation of her Plan of Reorganization in October of 2007, Ranzino-Renda filed a complaint against the "Cook Defendants," alleging a malpractice claim, among various other allegations. *Id.* at *3.

Similar to the TWD Defendants in *Texas Wyoming Drilling,* the Cook Defendants asserted lack of jurisdiction over the Ranzino-Renda adversary because Ranzino-Renda failed to preserve her standing to pursue those claims post-confirmation.

Ranzino-Renda's Plan stated "all real and personal property of the estate…including but not limited to all causes of action…and any avoidance actions…shall vest in [Ranzino-Renda]." *Id*. Additionally, Ranzino-Renda's Disclosure Statement identified specific litigation claims that she had previously listed in her Schedule B. Moreover, the Disclosure Statement contained specific language evidencing Ranzino-Renda's intent to pursue a number of post-confirmation claims against the Cook Defendants. Although the Plan did not contain any language regarding the Cook Defendants, Ranzino-Renda's Disclosure Statement specifically described them as potential litigation claims.

Issues

The court, in this opinion, faced similar issues in two very different cases. For instance, did TWD or Ranzino-Renda preserve their standing to pursue post-confirmation claims by using "appropriate language" in the Plan or in the Disclosure Statement? Moreover, did the fact that the TWD case was converted from chapter 11 to chapter 7 raise another issue of whether the Trustee had standing to bring these claims even if the Plan language was insufficient? If so, was the trustee judicially estopped from bringing these claims or were they barred by *res judicata? See id.* at *4.

Analysis

After a thorough analysis of the language of the Plans involved in these two cases, the Code, and relevant case law, the Court ruled that both TWD and Ranzino-Renda had standing to pursue their adversary claims, and further, that the language utilized in the Plans and Disclosure Statements was sufficient to preserve and retain the

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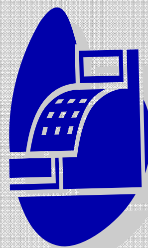

Consumer Corner: Fifth Circuit Case Update III: making Sense of Collateral Attacks and Plan Finality in the Fifth Circuit –In re Chesnut

By: Caleb D. Trotter, Judicial Extern to the Honorable Harlin D. Hale, third-year student at SMU's Dedman School of Law and joining Munsch Hardt Kopf & Harr, P.C. in 2010 (ctrotter@smu.edu)

Introduction

A three-judge panel for the Fifth Circuit, consisting of Judges King, Garza, and Haynes, recently released an unpublished opinion in the matter of Vance Chesnut. *In re Chesnut*, No. 09-101145, 2009 WL 4885018 (5th Cir. Dec. 17, 2009). While the court determined that the opinion should not be published and is not precedent, it does perhaps cast some light on where the Fifth Circuit stands on an issue currently before the Supreme Court. The Supreme Court recently heard arguments on an appeal of the Ninth Circuit's decision in *Espinosa v. United Student Aid Funds, Inc.*, 553 F.3d 1193 (9th Cir. 2009). *Espinosa* affirmed the Ninth Circuit's prior opinion in *In re Pardee*, which held that a discharge of a student loan in a Chapter 13 plan is a final judgment which cannot be set aside or ignored regardless of whether the plan contains illegal provisions. *See In re Pardee*, 193 F.3d 1083, 1086 (9th Cir. 1999). The plans in those Ninth Circuit cases granted discharge of student loan debts, despite the fact that the debtors failed to initiate an adversary proceeding to prove undue hardship, as required by section 523(a)(8) of the Code and Rule 7001(6). The opinions, at their core, place a higher value on the finality of plan confirmations and discharge orders than the requirement of an adversary proceeding under the Code. According to the Ninth Circuit, the requirements of an adversary proceeding only apply while the case is pending before the bankruptcy court; once the plan is confirmed, it is a final judgment that cannot be set aside simply because it was the result of an error.

The *Chesnut* court dealt with similar legal questions, and while the panel did not have to decide between the legal and final natures of a confirmed plan, its language affirmed Fifth Circuit precedent that arguably conflicts with *Espinosa's* holding.

Factual and Procedural Background of *Chesnut*

Vance Chesnut filed a voluntary petition for relief under Chapter 13 of the Bankruptcy Code in early 2003. In his petition, Mr. Chesnut claimed that Templeton Mortgage Corp. was a secured creditor. Templeton was the holder of a promissory note made by Mr. Chesnut's wife. Mr. Chesnut filed his Chapter 13 petition soon after Templeton had accelerated the debt and posted the property for foreclosure. Templeton ignored the bankruptcy case and proceeded with the foreclosure sale. Chesnut responded several months later by filing an adversary proceeding against Templeton for willfully violating the automatic stay provisions. The bankruptcy court agreed that Templeton had violated the automatic stay, noting that Templeton had notice that Chesnut was claiming an interest in his wife's property. The bankruptcy court's decision was overturned on appeal to the district court, but affirmed by the Fifth Circuit in *Brown v. Chesnut*, 422 F.3d 298, 306 (5th Cir. 2005) ("*Chesnut I*").

During the appeal process of *Chesnut I*, Chesnut filed a proof of claim on Templeton's behalf. Templeton received notice of this proof of claim but did not file any objection. Chesnut's plan ultimately listed Templeton's claims among those of the other secured creditors, and proposed that all such creditors would release their liens upon completion of the plan payments. Templeton again did not object, and the plan was confirmed. Templeton did not appeal the confirmation order. Once payment under the plan was complete, Chesnut sought release of Templeton's lien on the property. Templeton refused to the release the lien, despite accepting payments from the Chapter 13 Trustee. Templeton claimed that the property was Mrs. Chesnut's separate property, that no proceeding had ever determined that it was property of the estate, and that the confirmed plan had no effect on the validity of its original lien. The bankruptcy court disagreed, and ordered the lien released, stating that *res judicata* barred all collateral attacks on the confirmed plan. The district court affirmed, and Templeton timely appealed to the Fifth Circuit.

Application of *Res Judicata* to the Confirmed Plan

The Fifth Circuit compressed Templeton's claims into two main issues: (1) whether *res judicata* applied to the plan and required release of the lien, and (2) whether Templeton had adequate notice of the effects of the plan's provisions. Templeton challenged the bankruptcy court's subject matter jurisdiction over the confirmation proceedings. Because the property was not part of Chesnut's bankruptcy estate, Templeton argued, the bankruptcy court had no jurisdiction to order release of its lien after plan payments. The Fifth Circuit summarily dismissed this attack, stating that the issue of a bankruptcy court's subject matter jurisdiction may be raised on direct appeal, but that a party to the original proceeding may not raise the issue in a collateral attack. The panel in *Chesnut* cited the Supreme Court's recent decision in *Travelers Indemnity Co. v. Bailey*, which declared that once confirmation orders become final, they become *res judicata* to the parties, whether or not the orders were proper exercises of bankruptcy court jurisdiction. 129 S. Ct. 2195, 2205 (2009). The *Travelers* decision specifically stated that once orders become final on direct review, they become *res judicata* not only to each matter offered and received to support or challenge the claims, but also to "any other admissible matter which might have been offered for that purpose." *Id.* at 2205.

Despite this broad stroke painted by the Supreme Court, the *Chesnut* panel made it clear that Templeton had received actual notice of both the proof of claim filed on its behalf and the Chapter 13 Plan. Because Templeton could have raised the issue of subject matter jurisdiction to the bankruptcy court several times prior to plan finality, the Fifth Circuit ruled that the issue was "insulated" from collateral attack. *Chesnut*, 2009 WL 4885018, at *3.

The panel was careful to distinguish Templeton's claims from those of creditors who had challenged subject matter jurisdiction in similar cases. *See In re McCloy*, 296 F.3d 370, 374 (5th Cir. 2002). In *McCloy*, the creditors questioned subject matter jurisdiction in a timely fashion, where Templeton's argument came after the time for appeal had passed. Therefore, declared the Fifth Circuit panel, Templeton's arguments came "far too late in the proceedings" to unsettle a confirmed and completed plan. The panel went on to emphasize the importance of the finality provision of the Code, in section 1327(a).

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SPECIAL FEATURE: STATE CASE LAW REVIEW

WINNING ONE "FOR THE GIPPER": RECENT OPINIONS MAKE GOOD LAW (OR CLARIFY EXISTING LAW) FOR BANKRUPTCY TRUSTEES

By: Erin E. Jones, a partner with Jones Morris, LLP, Houston, Texas (erin@jonesmorris.com)

In the past year there have been many excellent decisions out of the federal courts and Texas state courts clarifying the application of the doctrine of judicial estoppel in bankruptcy related litigation. These cases, discussed in more detail herein, are critical in further empowering trustees to prosecute claims on behalf of bankruptcy estates. The purpose of this article is to provide an overview of recent cases regarding the application of judicial estoppel to bankruptcy trustees and also to highlight a recent state court of appeals decision regarding the applicability of Bankruptcy Code § 108 to claims arising under state law.

In 2005 married debtors (the "Debtors") filed for chapter 7, failing to schedule medical malpractice claims[1] as an asset prior to receiving their discharge.[2] At no time during the pendency of the bankruptcy case did the appointed chapter 7 trustee (the "Trustee") have knowledge of the existence of the Debtors' claims. It follows that if the Trustee did not know that the malpractice claims existed, he certainly could not have administered the asset, including abandoning the medical malpractice claims to the Debtors.[3]

The Debtors initiated a lawsuit in state district court prior to receiving a discharge and did not notify the Trustee of the pending lawsuit. The Defendants in that case eventually discovered the Debtors' bankruptcy case and their failure to schedule the medical malpractice claims and filed a motion for summary judgment against the Debtors on the grounds of judicial estoppel. Debtors' litigation counsel then contacted the Trustee who moved to reopen the bankruptcy case on an emergency basis and intervened as the proper party plaintiff in the pending lawsuit in the state district court.

Relying on *In re Superior Crewboats,* 374 F. 3d. 330 (5th Cir. 2004), the state District Court Judge granted the motion for summary judgment as to the Debtors and held that the Debtors' failure to schedule the medical malpractice claims prior to receiving a discharge was sufficient to judicially estop them from prosecuting their claims. Defendants then insisted that the Fifth Circuit's opinion in *Superior Crewboats* required the District Court Judge to impute the Debtors' conduct to the Trustee and to find that the Trustee was judicially estopped as well. At the Court's request, the Trustee provided ample authority rejecting Defendants' argument that the Trustee was judicially estopped by virtue of the Debtors' conduct.[4] After substantial briefing and oral argument, the District Court Judge ruled in favor of the Defendants finding that the Trustee was judicially estopped because he found that the Trustee "stepped into the shoes" of the Debtors who were judicially estopped from pursuing the claims.

But it gets even more complicated – at the summary judgment hearing, Defendants claimed that the malpractice claims were barred by the statute of limitations because, as they argued, Bankruptcy Code section 108(a) could not extend the "absolute" two-year statute of limitations set forth in the Texas Medical Liability Act. TMLA section 74.251(a). After significant briefing regarding federal supremacy and preemption, the District Court Judge also held that the two-year statute of limitations under the Texas Medical Liability Act was "absolute" and could not be extended by Bankruptcy Code section 108(a).

The Trustee appealed the District Court's decision and nearly two and a half years later the First Court of Appeals, applying federal law, reversed and remanded the case back to the trial court.[5]

FEDERAL SUPREMACY IS ALIVE AND WELL – AT LEAST AS TO THE TEXAS MEDICAL LIABILITY ACT

Defendants argued that the statute of limitations contained in the Texas Medical Liability Act (TMLA section 74.251(a)) is an "absolute" statute of limitations and that as a matter of law Bankruptcy Code section 108(a) could not have extended that statute of limitations. Defendants relied on the following language from the TMLA in support of their position:

> NOTWITHSTANDING ANY OTHER LAW and subject to subsection (b), no health care liability claim may be commenced unless the action is filed within two years from the occurrence of the breach or tort or from the date the medical or health care treatment that is the subject of the claim or the hospitalization for which the claim is made is completed (emphasis added).

Not surprisingly, the Trustee argued that Bankruptcy Code section 108(a) operated to extend the TMLA statute of limitations because the Supremacy Clause of the United States Constitution dictates that when a state law is contrary to federal bankruptcy law, federal law prevails. The District Court Judge *sua sponte* determined that TMLA section 74.251(a) is a statute of repose and not a statute of limitations and therefore federal preemption does not operate to trump this so-called "absolute" limitations period. TMLA section 74.251(a) is not a statute of repose, however, the First Court of Appeals did not have to reach this issue because recently, in *Stanley v. Trinchard*, 579 F.3d 515 (5th Cir. 2009),the Fifth Circuit held that Bankruptcy Code section 108(a) is intended to supersede all time limitations under state laws even if such limitations are deemed to be substantive rights such as a statute of repose. The Fifth Circuit stated that "Because Congress expressed an overriding unqualified interest in allowing bankruptcy trustees sufficient time to discover causes of action on behalf of their estates, we hold that section 108 (a) of the Bankruptcy Code, 11 U.S.C. § 108(a), extended Louisiana's legal malpractice preemption period." *Id.* at 516. Of particular importance to bankruptcy litigators is the following passage from the *Trinchard* case:

> The subject of bankruptcy falls within the express constitutional powers of Congress, and bankruptcy law therefore takes precedence over state laws under the Supremacy Clause. U.S. Const., art. VI. Section 108(a) is written broadly to extend any "period [fixed inter alia by 'applicable nonbankruptcy law'] within which the debtor may commence an action." The statute's clear purpose is to afford bankruptcy trustees extra time to assess and pursue potential assets of the debtor's estate. Congress drew no distinction among the state law vehicles that govern time limits for filing suit, whether statutes of limitations or prescription, repose or preemption. The language of Section 108(a) compels the conclusion that Congress expressly

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Business Case Law Update - Substantial Sanctions for Violating Discharge Injunction: *McClure v. Bank of America*

By: Jessica Voyce, Judicail Extern to the Honorable Harlin D. Hale and third-year student at SMU's Dedman School of Law (jvoyce@smu.edu)

A November 2009 bankruptcy court decision may influence businesses to heighten their efforts to avoid discharge injunction violations. In *McClure v. Bank of America*, the Fort Worth Division of the U.S. Bankruptcy Court for the Northern District of Texas sanctioned both parties that, the Court ruled, violated the 11 U.S.C. § 524(a)(2) discharge injunction. *McClure v. Bank of America* (*In re McClure*), Ch. 7 Case No. 07-43036, Adv. No. 08-04000, 420 B.R. 655 (Bankr. N.D. Tex. 2009). Payment of the sanctions hinged on whether the businesses set in place new procedures to ensure that such knowing violations would be avoided in the future, giving creditors an incentive to get it right the first time.

Background

Qualico, Inc., substantially owned by Danny and Kimberly McClure (the "McClures"), filed for Chapter 7 relief in July 2007. The McClures concurrently filed for Chapter 7 relief personally. At the time, the McClures owed both personal debts and debts related to their guaranteeing Qualico, Inc. debts to creditor Bank of America. These debts were discharged in the McClures' November 2007 section 727 discharge.

Still, Bank of America proceeded to refer two credit card accounts (cards issued to Qualico, Inc. and personally guaranteed by the McClures, referred to as Accounts "One" and "Two") to Creditor's Financial Group ("CFG") for collection. CFG then assigned the accounts to two of its collectors, Craig Osborne ("Osborne") and Peter Rebelo ("Rebelo"), who then attempted to collect from McClures.

Violation of the Discharge

The McClures alleged that Bank of America, CFG, and Rebelo each "willfully and intentionally violated the discharge injunction" and sought an order both holding each party in civil contempt of court and awarding damages. *See Piggly Wiggly Clarksville, Inc. v. Mrs. Baird's Bakeries*, 177 F.3d 380, 382 (5th Cir. 1999). By attempting to collect on the discharged debt, each of the defendants did violate the discharge, so the issue to be decided became whether the parties did so knowingly. *See Faust v. Texaco Refining and Marketing Inc.* (*In re* Faust), 270 B.R. 310 (Bankr M.D. Ga. 1998).

Bank of America Violation

The Bank of America portfolio officer that forwarded the accounts to CFG for collection testified that Bank of America was aware the McClures had been discharged of their personal guarantees on both of the Qualico, Inc. accounts. Because Bank of America had knowledge of the discharge and attempted to collect anyway, the Court held that Bank of America knowingly violated the discharge injunction and was liable for civil contempt.

CFG Violation

In considering a fact scenario warranting more in-depth analysis, the Court reviewed CFG's computerized data system and information transmission protocol to determine whether CFG knowingly violated the discharge injunction. The account information was electronically transmitted from Bank of America to CFG. CFG's computerized data system categorizes the information as to type: name, address, phone number, social security number ("SSN"), etc. In this case, the numbers categorized as the SSN were in fact Qualico, Inc.'s tax ID numbers in the SSN format. Thus, when CFG used those numbers to perform its automatic bankruptcy checks, it found neither Qualico Inc.'s bankruptcy nor the McClures' bankruptcy.

Neither CFG's act of receiving the two accounts from Bank of America nor its handling of Account One were in violation of the discharge injunction. Account One was assigned to Osborne for collection, without a phone number and without any notation that Danny McClure ("McClure") was a co-obligor on the account. In order to find out this information, Osborne obtained an external debtor location report, which listed McClure as the owner of Qualico, Inc. and gave his personal information—including phone number and SSN.

Osborne did not use this SSN to conduct a bankruptcy check on McClure, but he did use the phone number to call McClure numerous times, eventually making contact with him. After a few aggressive remarks from Osborne, McClure notified Osborne of both his personal bankruptcy and Qualico, Inc.'s bankruptcy. This contact did not amount to violation of the discharge injunction because neither Osborne nor CFG were aware of the bankruptcy at the time of this contact.

Learning of the bankruptcy, Osborne put Account One on protective status, to prevent CFG employees from contacting McClure about the debt. However, CFG's computer system did not link this protective status to Account Two, assigned to Rebelo, even though there was no question that the two accounts concerned the same entity. Though the information is stored on the same server, CFG's computer system did not automatically provide a collector with information other collectors had entered on related accounts.

It was CFG's handling of Account Two that resulted in a violation of the discharge injunction. McClure was already listed as a co-obligor on the collection information that Rebelo received, yet Rebelo made no attempt to run a second bankruptcy check. A few days after Osborne learned about the bankruptcy from McClure, Rebelo sent a collection letter to the McClures and attempted phone contact. Because Rebelo had no personal knowledge of the McClures' bankruptcy, the Court eventually found that he did not knowingly violate the discharge, even though he inadequately investigated the account. The issue then was whether Osborne's knowledge was sufficient notice to CFG for Rebelo's contact to amount to a violation of the discharge injunction.

The Court found that there was sufficient notice to CFG, and the fact that CFG's computer system was not set up to transfer protected status to related accounts or share collector information between accounts did not excuse it from violating the injunction. "Creditors are obligated to maintain procedures to ensure that they do not violate section 524." 4 Collier on Bankruptcy ¶ 524.02[2][b] (15th ed. rev. 2009). CFG's procedures were inadequate to do so. Because CFG had already received *actual* notice of the bankruptcies at the time Rebelo contacted McClure, CFG did violate the discharge

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Young Lawyers Committee

The Young Lawyers Committee for the Bankruptcy Section is a group of motivated young attorneys from across the State who have volunteered their time and talent. The purpose of the Committee is to increase the involvement of and integrate young lawyers on a State-wide basis into the Section at all levels, promote participation of young lawyers in seminars and events at all stages, and raise the visibility of our young lawyers by assisting them in professional networking and promoting professional development on a State wide basis. The Committee holds monthly conference calls on the second Wednesday of each month, and has a variety of exciting opportunities for young bankruptcy professionals to be involved. If you are interested in joining, please contact one of the Committee's new officers below.

The Committee's leadership has recently changed, and will be led by Brian Rogers of Victoria as Chair (brogers@rogersdavis.com); Joshua Searcy of Longview as Vice-Chair (joshsearcy@jrsearcylaw.com); and Layla Milligan of Austin as Secretary (layla@ch13austin.com).

The Committee's new Liaisons to the respective Section's Vice-Presidents are:

Liaison - Public Education - Omar Alaniz (Dallas)

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CALL FOR ARTICLES AND ANNOUNCEMENTS

The **State Bar of Texas Bankruptcy Law Section** is dedicated to providing Texas practitioners, judges, and academics with comprehensive, reliable, and practical coverage of the evolving field of bankruptcy law. We are constantly reviewing articles for upcoming publications. We welcome your submissions for potential publication. In addition, please send us any information regarding upcoming bankruptcy-related meetings and/or CLE events for inclusion in the newsletter calendar, as well as any items for our "Troop Movements" section (changes in practices).

If you are interested in submitting an article to be considered for publication or to calendar an event, please either e-mail your submission to a member of the Editorial Staff at tmillion@munsch.com, evanhorn@romclawyers.com or eborrego@whc.net or send your submission by regular mail (addresses on page 12).

Please format your submission in Microsoft Word. Citations should conform to the most recent version of the Bluebook, the Texas Rules of Form, and the Manual on Usage, Style & Editing.

Should you have any questions, please visit our website at http://txbankruptcylawsection.com.

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UPCOMING EVENTS

April 1-2, 2010	Fifth Circuit Bench-Bar Bankruptcy Conference, The Center for American and International Law, Dallas Metroplex (Plano)
April 29 – May 2, 2010	ABI 28th Annual Spring Meeting, Gaylord National Resort & Convention Center, National Harbor, Maryland: Information available at http://www.abiworld.org/ASM10/
May14, 2010	Northern District of Texas Bankruptcy Bench-Bar Conference, Dallas Infomart
June 2-4, 2010	State Bar Advanced Business Bankruptcy, Advanced Consumer Bankruptcy Conference, Bankruptcy Law 101 Conference, Hilton Dallas Lincoln Center, Dallas
June 3, 2010	2010 Annual Meeting Bankruptcy Law Section (during Advanced Business and Consumer Courses), Hilton Dallas Lincoln Center, Dallas Texas
June 10-11, 2010	State Bar of Texas Annual Meeting, Fort Worth, Texas at the Fort Worth Convention Center: Information available at http://www.texasbar.com
June 23-25, 2010	Western District of Texas Bench/Bar Conference, JW Marriott San Antonio Hill Country Resort & Spa, San Antonio Texas

LOCAL EVENTS

Dallas:
The Dallas Bar Association Bankruptcy and Commercial Law Section normally meets the first Wednesday of each month at the Belo Mansion. Social begins at 5 p.m. with program beginning at 5:30 p.m.

Fort Worth - Tarrant County:
Bankruptcy Section - monthly CLE luncheon meetings on the third Monday of each month to its members. Contact - Marilyn Garner at (817) 462-4075 or marilyndgarner@flashwave.com. Meetings are normally held at the Ft. Worth Petroleum Club.

San Antonio:
The San Antonio Bankruptcy Bar Association meets on the 4th Tuesday of every month at the San Antonio Country Club. Social begins at 5 p.m. with program beginning at 5:30 p.m. Participants receive 1 hour CLE .

A Brown Bag lunch with Judge Clark, Judge King, the Bankruptcy Clerk, and members of the Bankruptcy Bar is held quarterly at the Adrian Spears Judicial Training Center.

Houston:
The last Friday of each month from 7:30 to 9:00 Judge Bohm and the Moller/Folts Inn of Court present the Issues in Chapter 11 Program in Judge Bohm's Courtroom. The program is available to all lawyers (Inn membership is not required). CLE credit and donuts provided. For more information or to RSVP, please contact Liz Freeman (efreeman@porterhedges.com).

Members of HAYBL are invited for monthly "Chamber Chats" with Judge Bohm and a special guest. Eight monthly spaces available and HAYBL membership required. For more information, contact Allison Byman (Allison.Byman@tklaw.com).

Members of HACBA are invited for monthly "Chamber Chats" with Judge Bohm and a special guest. Eight monthly spaces available and HACBA membership required. For more information, contact Pam Stewart (plsatty@swbell.net).

TROOP MOVEMENT

Houston

Elizabeth Freeman (formerly of Locke Lord Bissell & Liddell LLP) joined Porter & Hedges LLP as Partner.

Berry Spears has moved from the Austin to the Houston offices of Fulbright & Jaworski L.L.P.

(Continued from page 1)

ended up doing bankruptcy, more or less by accident. While working on a litigation problem in the firm library, he says, a senior partner needing someone to help on a project asked, "Are you busy?" Clark was told the project had a short fuse and involved a bankruptcy case. This was not a selling point. There was little or no bankruptcy work back then, Clark explains, and the practice was mostly housed in boutique firms and known as something "lesser lawyers" did. The particular project involved an action under the old (pre-1978) bankruptcy statute. The partner needed legal support for an Appellee's brief to the Fifth Circuit seeking remand of an action to the trial court. Clark prepared the research, and the partner succeeded in obtaining the remand. Clark was invited to stay on with the project.

The bankruptcy case was Commonwealth Oil Refinery Company, then the largest chapter 11 case pending in the nation, and the lawyers he worked with were "the best [he] had ever seen." He was sold on the practice. Soon, he found himself handling bankruptcy matters for other firm clients, under the then new Bankruptcy Code. The bankruptcy boom had begun, and many young lawyers jumped into the practice. Because the law was new, young lawyers willing to work hard could excel, and Clark was one of those young Turks.

By the mid-1980s, bankruptcy was exploding. Case filings were through the roof all over the state. There were then only two bankruptcy judges in the Western District of Texas. But two were not enough. The Western District of Texas covered Midland, Waco, El Paso, San Antonio, and Austin—an area larger than many states. Congress authorized a third judge, and Clark was appointed. Later a fourth was created, a position that Frank Monroe filled.

It was almost an anomaly that a bankruptcy practitioner was appointed to the position at all. The new bankruptcy law included an attempt to break the bankruptcy "ring" of the 1960s and 70s, where attorneys and judges practiced in such small circles, they were sometimes beholden to each other. The new law changed how judicial appointments were made and lengthened terms from six to fourteen years. Instead of the district court, the circuit court appointed the bankruptcy judges. Some circuits, in their ardent attempts to stem the perceived corruption, appointed judges outside of the practice, resulting in some unfortunate choices.

Judge Sam Johnson, the Fifth Circuit judge who chaired the merit selection panel for choosing judges in the Western District of Texas, took a different view of the process, Clark said. He believed it was actually better to pick bankruptcy practitioners so long as one was careful to investigate the applicant's integrity. His judgment had been confirmed by his selection panel's first two choices, Glen Ayers and Larry Kelly, and Johnson continued that course when he sought out candidates for the third position.

Johnson made a good choice. Clark has authored over 200 published decisions, including *In re Greystone III Joint Venture*, 102 B.R. 560 (Bankr. W.D. Tex. 1989) (addressing classification and unfair discrimination in a cramdown confirmation); *In re Applegate Property, Ltd.,* 133 B.R. 827 (Bankr. W.D. Tex. 1991) (addressing insider's acquisition of unsecured claims and bad-faith vote against plan); *In re Simmons,* 205 B.R. 834 (Bankr. W.D. Tex. 1997) (analyzing Section 1334 "arising in" jurisdiction); *In re Sullivan,* 195 B.R. 649 (Bankr. W.D. Tex. 1996) (addressing unfair discrimination in the context of debtor's more favorable treatment to student loan debt); *In re Landing Associates, Ltd.,* 157 B.R. 791 (Bankr. W.D. Tex. 1993) (analyzing bad faith bar to confirmation); *In re El Paso Refinery, L.P.,* 257 B.R. 809 (Bankr.W.D.Tex. Apr 15, 2000) (offering a detailed analysis of Fifth Circuit law on reasonableness of attorneys' fees and fee enhancement). Clark's opinions have proven especially helpful to practitioners looking for a thorough analysis of sometimes difficult legal issues.

Not all the cases that have come before him have been as nuanced and notable as *Greystone.* Some have taken a turn for the comical—at least in retrospect. Clark remembers a hotly-contested consumer case that concerned the exemption of the debtor's numerous and extensive firearms. The case was filed before metal-detectors had become a standard feature in the building that houses the bankruptcy courts in San Antonio. "The debtor sat at the counsel table," Clark describes, "and when he set down his large gym bag, the entire courtroom heard a distinct metal clank." Thankfully, a pointed glance at the court security officer and a brief examination of the bag's contents–no guns– substantially reduced the tension level.

During his tenure on the bench, Clark has tried to maintain a balanced approach to the cases before him. A judge "can't be too laissez faire," Clark said. "Otherwise, he surrenders control to whoever makes the most noise. At the same time, the judge isn't a lawyer in the case."

Clark advises young bankruptcy practitioners—and, indeed, all lawyers that come before him—to know what the law is. "The judge should not be the only one in the courtroom to know the letter of the law." He also counsels that "zealous advocacy doesn't mean endless advocacy." A lawyer should make her argument but not continue to push and push when that argument becomes untenable.

Clark's judicial mentors advised him to make the most of the opportunities the position provides. "As a judge, you're presumed to have something to say, and since you have more opportunities to be heard, you can make a difference." He's found one of the most rewarding and challenging opportunities to be his participation in the National Bankruptcy Conference. The membership includes some of the "sharpest people you'll ever meet, and they're not shy about sharing what they think – or telling you what they think of what you have to say." The high caliber of the scholarship and the speed at which it is produced is "unparalleled," Clark said.

Clark has been a frequent speaker at bankruptcy seminars, from local bar association presentations to recent presentations at the National Conference of Bankruptcy Judges' Annual Meeting and the quadrennial session of INSOL International. He is also an adjunct professor at The University of Texas School of Law, teaching bankruptcy courses. For sixteen years, he also taught a short course on American constitutional law to foreign students in Salzburg, Austria, as part of the International Law program of McGeorge School of Law.

"The beauty of the courtroom," Clark explains, "is that in a proceeding before the court, instead of yelling, we make the best case to a third-party neutral, who listens, understands, and reaches a conclusion that has coherence." To Clark, this coherence is "the thing itself," absent in political discourse, what is now the domain of infotainment and talk radio shows, where there is no room for dialogue, "only monologues screamed across the room." Coherence is more than applying logic. It is an effort at balancing equity and public policy. It is an effort at clarity and integrity. Ultimately, it is an effort at intellectual honesty.

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A devotion to such a discourse has taken on even more importance for Clark, as he reflects on the society that his children will inherit. He married Rochel Lemler in 2002, and now is a proud father of son Harrison and daughter Carson Renee.

So here we come full circle to the Order Denying Motion for Incomprehensibility. It is no surprise that incoherent thought—for Clark, one of the worst sins in the judicial sanctum sanctorum—would drive him to the point of quoting, yes, Adam Sandler.

[1] Incidentally, attorneys and witnesses are also advised not to swing the gate to the bar.

CHAPTER 11 PRACTICE — *IN RE TEXAS WYOMING DRILLING, INC.*

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claims.

To arrive at its conclusion, the court's decision had to meet the standard enunciated by *In re United Operating* requiring a plan to be "specific and unequivocal" in retaining a debtor's post-confirmation right to pursue claims. *See In re United Operating,* 540 F.3d at 355; *see also* 11 U.S.C. § 1123(b)(3)(B). The court's reasoning in applying the "specific and unequivocal" standard rests upon the Fifth Circuit's determination that "such language in a plan is essential to put creditors on notice of any claim that the debtor wishes to pursue after confirmation." *In re Texas Wyoming Drilling, Inc*., 2010 WL 276653 at *7 (analyzing *In re United Operating*, 540 F.3d at 355). Thus, the court, in this case, read *United Operating* as necessitating the inclusion of "specific and unequivocal" language so that creditors could be properly informed when voting on whether to confirm a proposed plan.

In its consideration of the TWD motion, the court ruled that *United Operating* does not require a Plan to "include identification of specific claims against specific defendants." *Id.* at *8. Instead, the court found that a categorical reservation of claims would be sufficient to meet the *United Operating* standard. *Id.*; *see also In re Manchester*, 2009 WL 2243592 (Bankr. N.D. Tex July 16, 2009). Nor did the court find that the requirement of "specific and unequivocal" inclusion of claims in a Plan was intended to place future defendants on notice, but rather, to enable creditors to make an informed decision when voting on the plan. Accordingly, the court held that TWD satisfied the requirements of *United Operating* by sufficiently placing creditors on notice of their intent to preserve all possible avoidance actions, even though no specific defendants were named. *In re Texas Wyoming Drilling, Inc.*, 2010 WL 276653 at *9.

The court found otherwise with regard to the Ranzino-Renda Plan, ruling that it failed to satisfy the requirements of *United Operating. Id.* at *10. Instead, the language contained in the Ranzino-Renda Plan was "a clear example of a blanket reservation that was deemed in *United Operating* to be insufficient to preserve [post-confirmation claims]." *Id.* Nevertheless, the failure of the Ranzino-Renda's Plan to specifically retain claims did not bar the pursuit of her claims against the Cook Defendants.

Even though, on its face, Ranzino-Renda's Plan failed to adequately preserve her claims, the court applied contract law to construe the Plan, finding that the Disclosure Statement, in concert with the Plan, was adequate to specifically and unequivocally preserve Ranzino-Renda's claims against the Cook Defendants. *Id.* at *10-11. Because the specific language in Ranzino-Renda's Disclosure Statement demonstrated her intent to pursue claims against the Cook Defendants, the court found the Disclosure Statement sufficient to justify Ranzino-Renda's preservation of her standing to pursue these claims, stating that "looking at a plan and disclosure statement together is in line with the general contract principle that documents forming part of the same transaction are to be read together." *Id.* (citing *This Is Me, Inc. v. Taylor*, 157 F.3d 139, 143 (2d. Cir. 1998)).

After deciding that both TWD and Ranzino-Renda had sufficiently preserved their standing to pursue their respective claims, the court addressed the issue of whether TWD's chapter 7 Trustee had standing to pursue claims. *Id.* at *12. The court's creative and thorough discussion of the inner workings of the Code led it to conclude that TWD's chapter 7 Trustee had standing, even if TWD failed to otherwise preserve its claims, post-confirmation.

The first step in the court's analysis was to determine whether the claims against the TWD Defendants belonged to the bankruptcy estate or to TWD. *Id.* at *12; *see also* 11 U.S.C. §§ 541, 548, and 550. The court reasoned that section 1112 of the Code gives bankruptcy courts the ability to convert a post-confirmation chapter 11 case to a chapter 7 case instead of dismissing the case outright. *Id.* at *13. As the case had been properly converted to chapter 7, the court further found that any undisposed property in the post-confirmation estate would constitute a part of the bankruptcy estate under chapter 7. *Id.* Since the post-confirmation estate never disposed of its claims against the TWD Defendants prior to conversion, then those claims were the property of the chapter 7 estate and could be enforced by the chapter 7 Trustee. Thus, the court concluded that the Trustee was permitted to "enforce the TWD Claims on behalf of the estate for the benefit of unsecured creditors even if the language of the TWD Plan is insufficient to meet the 'specific and unequivocal' requirement of *United Operating*." *Id.*

IMPACT OF *IN RE TEXAS WYOMING DRILLING, INC.*

Even though a "blanket reservation" of future claims is insufficient under the *United Operating* standard, it remains unclear what "specific and unequivocal" may actually mean with respect to language contained in plans of reorganization. *In re Texas Wyoming Drilling* sheds light in this area, demonstrating that reservations of claims need not be specific to individuals. Moreover, even if a plan's express language is insufficient, the disclosure statement still may suffice in preserving future, post-confirmation claims under contract theories.

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BUSINESS TRACK PRESENTATIONS

The New World of Reorganizations was the topic for these presentations and the Hon. Leif M. Clark (Bankr. W.D. Texas – San Antonio) presided over the sessions and moderated two of the panels. These sessions explored several of the big changes occurring in Chapter 11 and also revisited how reorganizations were once done.

Who's Really in Charge Here? Reorganizations in the Shadow of Chrysler and GM: **Bruce Grohsgal** (Wilmington) and **Hugh M. Ray, Jr.** (Houston) had a "spirited" discussion moderated (read: refereed) by Judge Clark about how the Chapter 11 landscaped has evolved from being about Debtors-in-Possession to being about Secured-Creditors-in-Possession and whether, after Chrysler and GM, we now have a Buyer-in-Possession. Messrs. Gorhsgal and Ray also debated the merits of the recent *Philadelphia Newspapers* decision on credit bidding under Section 363(k).

Who's Really in Charge Here? The CRO Unhinged: University of Texas School of Law **Professor A. Mechele Dickerson** (Austin) discussed how the Chief Restructuring Officer has become an easy replacement for existing management and important issues relating to the rise of the CRO. Such issues include (i) to whom the CRO answers when the board of directors is inactive, moribund, or nonexistent; (ii) who is the company hiring (the CRO or the CRO's entire firm); and (iii) whether a CRO is an adequate substitute for an examiner or trustee.

Who's Really in Charge Here? Putting the Judge Bank in Charge: Judge Clark moderated a discussion between **Michael "Buzz" R. Rochelle** (Dallas) and the **Honorable William M. Schultz** (Houston, retired Bankr. S.D. Tex. – Houston) regarding the appropriate level of a bankruptcy judge's involvement in cases and how a judge's level of involvement has changed over the years. The panel discussed how judges, before the Code, used to be very involved in cases by presiding over 341 meetings and requiring DIPs to make monthly reports directly to them. The panel discussed the drawbacks to keeping a judge so far removed from a case and whether monthly status conferences with the debtor reporting to the judge would be a helpful middle ground approach.

CONSUMER TRACK PRESENTATIONS

A Consumer Bankruptcy Attorney's Guide to Assisting Small Businesses in Trouble: **John Akard, Jr.** (Houston) explained approaches to helping a small business owner in financial distress and available options when Chapter 11 is too expensive. These approaches include closing the business and counseling the small business owner when the business is no longer viable. The sale of business assets pre-bankruptcy often brings a better price. Mr. Akard stressed the necessity of developing a game plan and confirming its viability by researching the risk involved.

Post-Confirmation Modification of Chapter 13 and Individual Chapter 11 Plans: **The Honorable Alan S. Trust** (Bankr. E.D.N.Y. – Central Islip) discussed issues regarding whether and when a confirmed Chapter 13 plan and/or an individual Chapter 11 plan can or should be modified post-confirmation. Judge Trust explained how any such modifications might be impacted by changes in the debtor's disposable income. Judge Trust also highlighted the four permissible postconfirmation modifications under section 1329(a): increase or reduce payments on claims of a class provided for by the plan; extend or reduce the time for such payments; alter the amount of distribution to a creditor included in the plan to account for payment of claim other than by the plan; and reduce payments by the amount paid for health insurance for debtors and dependants.

Loss Mitigation in Bankruptcy: **James E. Bailey, III** (San Antonio) and **Steve P. Turner** (Austin) discussed the options and programs available to debtors for modifying loans. Messrs. Bailey and Turner specifically discussed the advantages of federal programs such as the Making Home Affordable Program (MHA) and Home Affordable Modification Program (HAMP). Traditional loss mitigation options are still available if a debtor does not qualify for federal programs. Borrowers are encouraged to make use of housing counselors like The Department of Housing and Urban Development (HUD) and the Texas Foreclosure Prevention Task Force (TFPTF) for current information about negotiating with lenders.

Ad Valorem Tax Problems in Consumer and Small Business Bankruptcy Cases: **Laura J. Monroe** (Lubbock) provided an overview of state property tax issues in bankruptcy and the best practices for addressing them. Ms. Monroe also explained that consumer attorneys should be sure to explain to their clients that some taxes are not dischargeable. Post-petition taxes must be paid or the debtor risks dismissal or lift of stay. Watch for situations when the debtor is not named as the property owner as the entity who owns the property on January 1st is the only party liable for taxes.

FRIDAY PRESENTATIONS

What a Chapter 13 Lawyer Can Teach a Chapter 11 Practitioner: **The Honorable Eugene R. Wedoff** (Bankr. N.D. Ill. – Chicago) explained ways in which Chapter 13 and Chapter 11 interact and what business practitioners can learn from Chapter 13. Judge Wedoff demonstrated the interaction between the two by discussing how consumer-oriented bankruptcy Supreme Court cases relate to Chapter 11, specifically, *Rash, Till, Maramma,* and the forthcoming decision in *Espinosa.*

An Unhappy Union? The Impact of Employment Issues on Chapter 11 Cases: **C. James Landon** (Austin) discussed a variety of employment issues and concerns that result from a bankruptcy filing, including issues related to the WARN Act, collective bargaining agreements, COBRA, the American Recovery and Reinvestment Act, and retention and severance plans in bankruptcy (KERPs).

Estate and Derivative Litigation: Gold Mine or Shaft? **Marty L. Brimmage, Jr.** (Dallas), **Judith L. Weaver Ross** (Dallas), and **J. Michael Sutherland** (Dallas) discussed the implications of several recent cases involving bankruptcy estate litigation including *Highland Capital Management v. Chesapeake Energy Corp. (In re Seven Seas Petroleum Inc.), Wooley v. Faulkner (In re SI Restructuring, Inc.), Torch Liquidating Trust v. Stockstill; Dynasty Oil & Gas, LLC v. Citizen Bank (United Operating, LLC)*, the Supreme Court's *Ashcroft v. Iqbal*, and many others. The issues covered included recent case law involving *in pari delicto*, equitable subordination, preserving causes of action, damages, defenses, and standing.

363 Sales vs. Plans: What's Happening. What's Fair? The University of Texas School of Law **Professor Jay L. Westbrook** (Austin), the **Honorable D. Michael Lynn** (Bankr. N.D. Tex. – Ft. Worth), and the **Honorable Eugene R. Wedoff** (Bankr. N.D. Ill. – Chicago) discussed whether the future of Chapter 11 will be in plans of reorganization or in sales, which it should be, and how Chrysler and GM impact these issues. The panel also covered ways in which judges might influence or give certainty to the 363 sales process by issuing guidelines, and

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addressed related issues including evaluating irreparable harm and valuations.

Section 363(k) Credit Bidding Issues: Moderator **Mark W. Wege** (Houston) and panelists **Chris L. Dickerson** (Chicago), **Abid Qureshi** (New York City), and **Edward L. Ripley** (Houston) discussed issues involving the use of credit bids by secured creditors in 363 sales. The panel discussed practical case examples, recent cases (including *Philadelphia Newspapers, Scotia Pacific,* and *SubMicron*), and how the process is complicated by new financial innovations like loan syndication.

Ipso Facto Clauses – New and Improved? **Elizabeth M. Guffy** (Houston) and **Thomas S. Henderson, III** (Houston) discussed the newest trends in structured financial arrangements and how they are unsettling what was thought to be a settled area of the effect of *ipso facto* clauses in bankruptcy. The panel focused on the recent *General Growth Properties* decision and the weakness in that company's transactional documents which allowed the bankruptcy court to pull several "bankruptcy remote" entities into the Chapter 11.

Update on the Economy and the Banks: The University of Texas McCombs School of Business Professor **Sanford J. Leeds, III** explained the most important economic developments and the health of the nation's banks. Prof. Leeds covered issues relating to the underfunding of social security, risk taking by banks, enforcing federal banking regulations, and the lack of personal liability by banking executives. Prof. Leeds also predicted a "muddling economy" for the next few years and explained how a long recession is exponentially worse than a short one.

EVENTS

In addition to Thursday evening's reception after the presentations and the conference's speaker's dinner, the Bankruptcy Section's Young Lawyers' Committee hosted its third annual evening reception and invited all attendees to the Lanai Rooftop Lounge – a trendy bar in Austin's Warehouse District where young and experienced practitioners and non-lawyers mingled into the night. Special thanks to the events sponsors: the **Bankruptcy Section; Conway MacKenzie, Inc.; Harney Management Partners, LLC; and Lain, Faulkner & Co., P.C.**

[1] To view the members of the conference faculty, planning committee, the many generous sponsors, and entire course program, please see the conference brochure on UTCLE's website: http://www.utcle.org/conference_overview.php?conferenceid=862.

BUSINESS CASE LAW UPDATE — *MCCLURE V. BANK OF AMERICA*

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injunction and was liable for civil contempt. Additionally, the Court, by clear and convincing evidence, found that both Bank of America and CFG *willfully* violated the discharge because both entities intended to perform the actions that constituted the violation. Thus, the Court found both entities in civil contempt.

DAMAGES & SANCTIONS

The Court then evaluated the McClures' requests for actual damages and attorney's fees. In awarding $2,500 in damages for the "substantial time and effort" the McClures put into this case, the Court stated that such damages both reward debtors for pursuing suits for violation of the discharge injunction and provide an incentive for creditors to avoid violations altogether. The Court did not, however, award any amount to compensate for emotional distress, finding only a tenuous correlation between CFG's actions in contacting McClure and McClure's "severe emotional distress and sleeplessness."

As for attorney's fees, Bank of America and CFG argued against the high amount of the attorney's fees requested by the McClures, for which the two entities would be jointly and severally liable. Again the Court pointed to the importance of providing a disincentive to violation of the discharge injunction as well as the two entities' own part in increasing those fees by stretching out the proceedings. The Court then awarded the portion of the requested attorney's fees it found reasonable, which totaled slightly less than $80,000.

Most notably, the Court then imposed sanctions on both Bank of America and CFG for their "lack of concern for the law" evidenced by their "failing to adopt measures sufficient to prevent violations of the discharge injunction and then willfully violating the discharge injunction." Because the discharge is "at the heart of bankruptcy protection" and provides the fresh start for debtors that Congress intended, the Court stated that it had a duty to "act promptly and firmly" both to stop the conduct violating the discharge injunction and to prevent further breach. *In re McClure*, 420 B.R. at 664 (citing *Marrama v. Citizens Bank*, 549 U.S. 365, 376 (2007)).This duty became all the more important when the violators deal with "millions of customers, many of whom will be in bankruptcy cases."

Having reviewed these considerations, the Court concluded that it was both reasonable and necessary to sanction Bank of America in the amount of $100,000 and CFG in the amount of $50,000, both amounts payable to the registry of the court. *See* 11 U.S.C. § 105(a). In keeping with the above reasons for applying sanctions, the Court made each of these payments contingent upon each entity's adoption of new procedures to prevent future violations. If within ninety days of the opinion's entry the President or General Counsel of either company presents, by affidavit, a description of such new procedures, that company's sanction need not be paid.

IMPACT

Considering how such sanctions can add up and how they may even be larger than the respective discharged debts, creditors may think twice before collecting debts without doing their homework. Perhaps companies will implement new protocol to both acquire and circulate debtor information, now knowing that the "my left hand did not know what my right had was doing" argument does not hold water.

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THE REQUIREMENT OF AN ADVERSARY PROCEEDING

The panel next addressed Templeton's second argument, that the plan itself violated Code because no adversary proceeding had been initiated by Chesnut to establish his rights in the property. Templeton claimed that Rule 7001(2) of the Federal Rules requires an adversary proceeding whenever a debtor must determine the "validity, priority, or extent of a line or other interest in property." Because an adversary proceeding was required, but never initiated by the debtor, Templeton argued there could be no *res judicata* effect from the confirmation order. However, the panel never reached the question of the effect of the requirement of an adversary proceeding on *res judicata* because they declared that Rule 7001(2) did not apply to the case at bar. Because the confirmed plan did not challenge the validity, priority, or extent of Templeton's lien, but rather acknowledged the lien and provided for release after full payment, Rule 7001(2) was inapplicable, and *res judicata* applied fully to Templeton's collateral attack.

NOTICE

Templeton claimed as part of its statement of issues that it had insufficient notice of Chesnut's intention to require the release of the lien, which was clearly stated in the plan. The panel waived this entire argument because it was absent from the body of Templeton's brief. The panel did state in *dicta*, however, that because Templeton was properly served with "all relevant filings", and actively participated in Chesnut's bankruptcy proceeding, Templeton was bound by the *res judicata* effect of the confirmation order. What the Fifth Circuit did not have to address, because of its decision that an adversary proceeding was not required under the Code, was whether failing to initiate such a proceeding was tantamount to a lack of notice. In *Espinosa*, the Ninth Circuit stated that when a proceeding is required by the Code and Rules (i.e., initiating an adversary proceeding to show undue hardship for discharging student loan debt), but the bankruptcy court confirms the plan nonetheless, the confirmation order has a *res judicata* effect on all collateral attacks. One of the central arguments of the *Espinosa* opinion, and what will most likely be a critical issue for the Supreme Court on review, is whether a failure to abide by the statutory requirements for initiating a proceeding is equivalent to depriving the party expecting such a proceeding of their Constitutional right to due process under the Fifth Amendment. The panel in *Chesnut* never reached this issue.

FIFTH CIRCUIT PRECEDENT

The *Chesnut* opinion is further limited because of the panel's holding that nothing in the plan violated provisions of the Code or Rules. The Fifth Circuit has, however, dealt with cases in which the creditor's rights under the Code were compromised by the confirmed plan. Two cases highlight the Circuit's willingness to carve out an exception to the general rule that a confirmed plan is *res judicata* to all parties who participated in the confirmation process. The first of those cases is *In re Simmons*. 765 F.2d 547 (5th Cir. 1985). In that case, a creditor who had filed a secured claim on its own behalf was incorrectly listed in the debtor's plan as an unsecured creditor. The creditor approved the plan on condition that the mistake be corrected. The debtor failed to correct the plan, and the bankruptcy court granted confirmation despite the fact that the debtor never objected to the creditor's secured claim. The Fifth Circuit overruled the bankruptcy court's decision, stating that once a creditor has filed a proof of claim, the Code and Rules place the burden on the debtor to object. Thus, in the Fifth Circuit, a secured creditor is not bound by a plan which reduces its claim where no objection has been filed by the debtor. The court reasoned that without such an objection being filed by the debtor, the creditor is never placed "on notice" that full participation in the confirmation proceedings in required.

The Fifth Circuit reaffirmed the *Simmons* exception seven years later in *In re Howard*. 972 F.2d 639 (5th Cir. 1992). In *Howard*, the court again held that confirmation of a plan that reduces or eliminates the claim of a creditor is *res judicata* to that creditor only if the debtor properly objects to the claim under the Code. The creditor in *Howard* had timely filed a proof of claim for $5,000. The debtor never objected to that proof of claim, but nevertheless reduced it to $500 in its final plan. The court held that this reduction was a violation of section 501, which states that a claim is allowed unless a party in interest objects. Because the debtor never objected, but rather reduced the claim in the plan, the plan itself was flawed. The creditor was never served with a copy of the final plan, and did not participate in the confirmation proceedings. The court declined to hold that *any* flaw in the provisions of a plan may be objected to after confirmation. In *Howard*, the court specifically stated that a plan may change the terms of payment and otherwise modify the terms of the debt underlying liens, and that creditors are put on notice of "the possibility" of these changes by notice of the filing of a bankruptcy proceeding and must object to the confirmation of a plan in order to prevent their effect. However, the court also stated that these types of changes are final as to creditors only because they do not conflict with other provisions of the bankruptcy Code. Thus, under *Howard* and *Simmons*, it appears that the Fifth Circuit will not apply *res judicata* to plans that conflict with provisions of the Code.

One case that many have cited for the proposition that a confirmed plan is always *res judicata* to all parties is *Republic Supply Co. v. Shoaf*. 815 F.2d 1046 (5th Cir. 1987). The bankruptcy court in that case included a provision in a Chapter 11 plan that invalidated a guaranty by a third party in favor of one of the creditors. That creditor failed to object to the plan at the final confirmation hearing. The Fifth Circuit ruled that, despite the fact that the bankruptcy court was without statutory authority to release the guaranty in the plan, the plan confirmation was *res judicata* on that issue. One distinction between *Shoaf* and *Simmons* seems to be that nothing in the *Shoaf* plan itself actually violated the Code. Rather, the court stated that the bankruptcy court "lacked the authority" to release the guaranty. In *Simmons*, however, the debtor had actually failed to take a procedure required by the Code, and had thus failed to place the creditor on notice as to its objection. Thus, it appears that one key issue for the Fifth Circuit in deciding when to apply *res judicata* effect to a confirmed plan is whether or not something in the plan violates the Code or Rules, and whether that violation has the additional effect of depriving a party of notice. While this distinction may seem subtle, the circuit's opinion in *Shoaf* was limited by *Howard*. In the *Howard* opinion, the court stated that "[t]o the extent [*Shoaf* and *Simmons*] might be in conflict, we would be bound to follow *Simmons* as the earlier decision of this court on the subject." *Howard*, 972 F.2d at 641. The court in *Howard* continued thus: "[T]he general applicability of *res judicata* to bankruptcy plan confirmations must give way . . . to the interest of the secured creditor . . . ." *Id.*

With this understanding of Fifth Circuit precedent in mind, it is readily apparent why the panel's ruling against the need for an adversary proceeding in *Chesnut* is so important to the holding. Because an adversary proceeding was not required to determine the validity of Templeton's lien, there was no violation of the Code or Rules in the confirmed plan. Thus, the confirmed plan was *res judicata* to all parties. The panel in *Chesnut* states plainly that the holdings of *Howard* and *Simmons* stand for the proposition that a plan must be consistent with the provisions of the Code, citing section 1322(b)(11). Because an adversary proceeding was not necessary to determine the nature of Templeton's lien, the absence of such a proceeding did not affect the general rule that *res judicata* bars

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FIFTH CIRCUIT CASE LAW UPDATE III — *IN RE CHESNUT*

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collateral challenges to confirmed plans.

WOULD THE FIFTH CIRCUIT AGREE WITH *ESPINOZA*?

The Ninth Circuit opinion in *Espinosa* stands for the reasonably unique proposition that the finality of a confirmation order and violations of the Code and Rules need not conflict. The court stated that the Code's finality provision, section 1327(a), and those provisions requiring an adversary proceeding can both operate fully and without conflict, "within their proper spheres." *Espinosa*, 553 F.3d at 1198. According to the Ninth Circuit, provisions giving creditors rights to special procedures only come into play when the case is pending before the bankruptcy court. This effectively places the burden on the creditor to read each proposed plan fully before confirmation, and object to the plan until the debtor initiates the special proceeding required by the Code. No articulation of this policy was more blunt than that in *Pardee*, which states that the Ninth Circuit recognizes the "finality of confirmation orders even if the confirmed bankruptcy plan contains *illegal provisions*." *In re Pardee*, 193 F.3d at 1086 (emphasis added). This blanket approach to the finality of plan confirmations is defended by the Ninth Circuit based on the concept that all creditors are put on "full and fair" notice as soon as they are served with the proposed plan. Thus, in the Ninth Circuit creditors are expected to review each proposed plan and search for objectionable provisions, or else the plan will become *res judicata* upon confirmation and any future objections or collateral attacks will be barred, regardless of the legality of the plan.

Espinosa may not run counter to the Fifth Circuit's decision in *Howard*, because in that case the creditor in question had never been served with notice of the final plan. However, it is reasonable to assume that the Fifth Circuit would reach a different outcome in a case with facts similar to those in *Espinosa*. The Fifth Circuit, unlike the Ninth, does in fact see a conflict between the finality provision and those requiring special proceedings of parties in a bankruptcy case. *See Howard*, 972 F.2d at 641 (stating that *Simmons* represents an exception to the rule of *res judicata* in *Shoaf* "based upon the competing concerns expressed in the bankruptcy code."). The Fifth Circuit made it clear in *Simmons* and again in *Chesnut* that a bankruptcy plan must be consistent with the provisions of the Code. The Code and Rules provide debtors with specific mechanisms for objecting to proofs of claim, as the Fifth Circuit noted in both *Howard* and *Simmons*. In those cases, the debtors failed to use those mechanisms and both courts stated that *res judicata* would not apply. In *Chesnut*, no adversary proceeding was necessary, and thus the debtor's failure to initiate such a proceeding had no bearing on the *res judicata* effect of the confirmation. Because the Code and Rules also provide a specific mechanism for discharging student loan debts, it is logical to assume that the Fifth Circuit would not apply *res judicata* to a confirmed plan purporting to discharge student loan debt without using those mechanisms (also known as "discharge-by-declaration"). This should assuage the fears of some that the Fifth Circuit under *Shoaf* would allow the use of so-called "ambush" tactics.

CONCLUSION

The *res judicata* effect of a confirmed plan containing provisions inconsistent with the Code and Rules is an issue of vital importance to the everyday practice of bankruptcy attorneys nationwide. The Fifth Circuit has shown a willingness to waive the *res judicata* effect when a confirmed plan deprives creditors of notice they expect under the Code. The Ninth Circuit, on the other hand, has declared that once a plan is confirmed, it is final regardless of whether it contains "illegal" provisions. While the *Chesnut* decision does not fully address all of the issues in *Espinosa*, it does reaffirm the Fifth Circuit's rule that bankruptcy plans must be consistent with the provisions of the Code. What remains to be seen, is whether the Supreme Court agrees.

FIFTH CIRCUIT CASE LAW UPDATE — *INGALLS V. THOMPSON*

(Continued from page 6)

support his theory Thompson relied on two cases from the Seventh Circuit.

The Seventh Circuit has issued two opinions, *Bates v. Johnson,* 901 F.2d 1424 (7th Cir. 1990) and *Hispanics United of DuPage County v. Village of Addison*, 248 F.3d 617 (7th Cir. 2001), which both "stand for the proposition that an injunction not reduced to writing is not a valid, appealable injunction under the Federal Rules of Civil Procedure." *Id* at 261-62. However, the Fifth Circuit chose to distinguish between the holding in those cases and the necessity of a written injunction for the court's order to be in effect such that an actor with notice of the injunction who violated the court's oral decree could be held in civil contempt. It found that the court's civil contempt power was "broad and pragmatic, reaching where it must." *Id* at 265. The court further noted that it had already determined that an actor could be held in criminal contempt for failing to obey a bankruptcy court's oral decree. *Id* at 264. Thus, by correlation, since Beutel's conduct "could support a criminal contempt conviction" the Fifth Circuit saw no reason that civil contempt could not also reach it. *Id* at 265.

PRESCRIBING A REMEDY

Finally, the court determined that the damages prescribed by the bankruptcy court for Beutel's violation were appropriate. "[T]he contempt finding made Beutel liable to the opposing party rather than imposing a fine payable to the court." *Id* at 265-66. The court "consider[ed] a contempt order restoring diverted property to be necessary and appropriate to implement the bankruptcy court's ultimate injunction, and to prevent abuse of process." *Id* at 267.

FINAL SCORE: JUDGE 1…TRUSTEE 0: TIME TO PAY THE PIPER

The appeals court affirmed the district court's ruling that the bankruptcy court was within its discretion to hold Beutel, as trustee, in contempt. However, the court suggested that to avoid similar situations in the future the lower courts should consider drafting at least some of their own orders to insure that they are entered in a timely fashion.

From the facts outlined in *In re Bradley*, it is not hard to imagine that Beutel was operating under a theory not too far removed from that presented in the "mission" statement at the beginning of this article. But his mission was misguided…his window of opportunity was not short, it was non-existent. For failing to obey the court's oral injunction Thompson, as successor trustee, ultimately had to pay compensatory sanctions totaling $317,953.53.

Beutel fought the law, but the law won.

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> extended the time for pursuing any action that would otherwise be time-barred under state law.

Id. at 519.

In the *Consunji* case which is the subject of this article, the First Court of Appeals acknowledged and applied the Fifth Circuit's holding in *Trinchard* and stated the following:

> Section 108(a)'s purpose is self evident: it is to provide the trustee with additional time to evaluate and to prosecute the debtor's potential claims as assets of the bankruptcy estate. Equally as clear, as noted by the Fifth Circuit, is that section 108(a)'s application is without qualification.[6]

The First Court of Appeals held that to the extent that the TMLA shortens the time frame provided by Bankruptcy Code section 108(a) it is in direct conflict with the Bankruptcy Code and it is preempted by federal law. The First Court of Appeals' opinion in *Consunji* provides very clear guidance for state courts in future cases as to the applicability of Bankruptcy Code section 108 (a) to the extension of state law statutes of limitations, statutes of repose and/or other prescriptive periods.

THE FIRST AND FOURTEENTH COURTS OF APPEAL ACKNOWLEDGE APPLICABILITY OF FIFTH CIRCUIT'S KANE DECISION IN STATE COURT MATTERS

It is true that a bankruptcy trustee "steps into the shoes of the debtor" and that a bankruptcy trustee is subject to whatever defenses a debtor has – but only *as of the petition date.* A bankruptcy trustee is not, *however,* bound by nor does he step into the shoes of the debtor with regard to a debtor's post-petition conduct (such as failing to schedule an asset). The duty to disclose assets is continuing during a bankruptcy case and thus failing to schedule and/or disclose the existence of an asset during the pendency of a bankruptcy case is post-petition conduct that cannot be imputed to the trustee.

As set forth in *Kane,* it is asking too much of *Superior Crewboats* and *In re Coastal Plains* to conclude that a trustee is judicially estopped based solely upon the conduct of a debtor. It is important to note that the *Kane* case does not overrule *Superior Crewboats* or *In re Coastal Plains* because each of those cases is in harmony with *Kane*. The purpose of the *Kane* opinion is to warn litigants and courts not to read so much into those cases, which were decided on the specific and narrow facts of those cases.

Only a few months before the First Court of Appeals issued its opinion in the *Consunji* case, the Fourteenth Court of Appeals addressed the identical question in another case. In *Bailey v. Barnhart*, 287 S.W.3d 906 (Tex.App.-Houston [14th Dist] June 16, 2009), the Fourteenth Court of Appeals held that a bankruptcy trustee who has no knowledge of the existence of a claim and has not abandoned the claim under bankruptcy procedures is not judicially estopped from pursuing claims belonging to a debtor who failed to disclose such claims prior to receiving a bankruptcy discharge.

Relying on the *Kane* decision, the First Court of Appeals in the *Consunji* case determined that a bankruptcy trustee cannot be bound by a debtor's post-petition conduct and that a trustee is not automatically estopped just because the debtor was judicially estopped.

There can be no doubt that a debtor's non-disclosure of litigation claims causes harm to its creditors. But, as other courts have pointed out, allowing the same non-disclosure to prevent an impartial and objective bankruptcy trustee from pursuing the claims for the benefit of creditors is like a double whammy for those creditors. Using an *equitable doctrine* like judicial estoppel to further harm legitimate creditors is not an equitable result – especially in a case like the *Consunji* case wherein the creditors are those who provided for the medical treatment of Mr. Consunji as a result of the injuries caused by the Defendants.

The *Kane* case provides the ultimate guidance on the issue of judicial estoppel of bankruptcy trustees. However, the First and Fourteenth Court of Appeals' decisions in *Consunji* and *Bailey v. Barnhart* are excellent references for future state court litigants.

For additional information regarding these cases and/or authorities cited in briefing, please feel free to contact the author of this article.

[1] During the course of the chiropractic treatment of the debtor, the defendant chiropractor negligently manipulated the cervical spine of Mr. Consunji resulting in hundreds of thousands of dollars in medical care and potential claims for the bankruptcy estate.

[2] *See In re Consunji,* Case No. 05-93516, United States Bankruptcy Court Southern District of Texas, Houston Division. The Trustee, Rodney Tow, was represented by Ms. Jones as general bankruptcy counsel and Toby Fullmer of Matthews & Fullmer as special litigation counsel.

[3] Given the size of the claims, the Trustee certainly would have prosecuted them had he known about them.

[4] At the time, the District Court Judge did not have the benefit of *Kane v. National Union Fire Ins. Co.*, 535 F.3d 380 (5th Cir. 2008), which we now know plainly rejects such a broad interpretation of *Superior Crewboats.* However, the Trustee did point to many other cases from lower courts within the Fifth Circuit and nationally that reach the same conclusion as the Fifth Circuit in the *Kane* case.

[5] *See* Case No. 01-07-00464, *Rodney Tow as chapter 7 trustee of the bankruptcy estate of Bernardino and Erwina Consunji* v. *Scott K. Pagano and Campbell Chiropractic Clinic P.C. d/b/a Campbell Chiropractic Wellness Center,* in the Court of Appeals for the First District of Texas. The November 5, 2009 opinion available at http://www.1stcoa.courts.state.tx.us/opinions/HTMLopinion.asp?OpinionID=87210.

[6] Opinion available at http://www.1stcoa.courts.state.tx.us/opinions/HTMLopinion.asp?OpinionID=87210.

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no conflict. Prior to this ruling, the Fifth Circuit had stated that there was an *irrebuttable* presumption that all confidences obtained by one member of a firm are shared with the other members of the firm. This was the exact presumption that the bankruptcy court applied in declining to consider Kennedy's evidence, relying on *In re American Airlines, Inc.*, 972 F.2d 605, 614 & n. 1 (5th Cir. 1992). However, the Fifth Circuit in *Kennedy* noted that the language describing the presumption as "irrebuttable" was never applied to the facts in *American Airlines*, and thus was *dicta*. Also, the court in *American Airlines* relied on two prior Fifth Circuit rulings, *American Can Co. v. Citrus Feed Co.*, 436 F.2d 1125, 1129 (5th Cir. 1971) and *In re Corrugated Container Antitrust Litigation*, 659 F.2d 1341, 1346-47 (5th Cir. 1981), in support of its irrebuttable presumption rule, and both of those cases applied an older version of the Texas Rules that did not contain Comment 7. Furthermore, the Court agreed with several legal commentators in describing the irrebuttable presumption as "both unfair and unworkable" when applied to these facts.

After rejecting the irrebuttable presumption, the Fifth Circuit looked to Kennedy's evidence that he never represented MindPrint while at Jackson Walker, and that he never even knew of its existence. Kennedy had testified that he had no knowledge whatsoever of MindPrint at the evidentiary hearing before the bankruptcy court, and MindPrint never presented any evidence to contradict his testimony. Even Schooler admitted that he had no knowledge or recollection that Kennedy had ever worked for MindPrint while at Jackson Walker. In determining that Kennedy's evidence was sufficient to demonstrate a lack of conflict, the Circuit affirmed that attorneys should have the opportunity to present evidence that they never obtained confidential information regarding the client in question. Because the evidence was uncontradicted, Kennedy could successfully demonstrate that any imputed conflict ended as soon as he left Jackson Walker.

CONCLUSION AND APPLICATION TO TEXAS ATTORNEYS

The Fifth Circuit's re-evaluation of the presumption of imputed conflicts may have a great impact not only on attorneys' ability to move laterally from one firm to another, but also on law firms' internal screening procedures. The Circuit did not affirmatively replace the "irrebuttable presumption" with a rebuttable one, nor did it declare that no presumption remains at all. What is clear, however, is that when uncontroverted evidence is presented that an attorney was never involved with the representation of a former client, such evidence will suffice to remove the imputed conflict of interest. In today's tumultuous economy and legal market, attorneys have enough to worry about when considering a lateral move. The Fifth Circuit's opinion in *Kennedy* seems to remove at least one of those potential concerns.