

COLORADO BANKRUPTCY COURT OPINIONS
October 2001 through December 2001

***Leonard v. McMorris*, 272 F.3d 1295 (10th Cir. 2001).** This is the appeal from *Leonard v. McMorris*, 106 F. Supp. 2d 1098 (D. Colo. 2000), in which certain officers of Nations Way Transport were held liable for the earned but unpaid wages and benefits of employees of the debtor-company which were unpaid when the company filed bankruptcy. Since that ruling, Nations Way confirmed its Chapter 11 plan and the plaintiffs' wage claims were paid. The plaintiffs continue to seek accrued vacation pay, sick leave pay, holiday pay, and other non-wage compensation, plus attorneys' fees and the 50% penalty provided under the Colorado Wage Claim Act. Citing a lack of Colorado precedent, the Tenth Circuit certified two questions to the Colorado Supreme Court: (1) Are officers of a now-bankrupt corporation individually liable for the wages of the corporation's former employees under the Colorado Wage Claim Act, Colo. Rev. Stat. Section 8-4-101, *et seq.*, and (2) if so, are all officers individually liable due to mere status as officers or must the officers have been high ranking or active decision-makers? **Query:** What if the non-payment of employees' wage claims is the result of a lender seizing the company's accounts?

***In re Western Pacific Airlines, Inc.*, 2001 U.S. App. LEXIS 26599 (10th Cir. 2001).** This appeal gives us the opportunity to review a little tax law. Here, the Chapter 7 Trustee joined the county taxing authorities of Denver and El Paso in asserting a tax lien for state personal property tax (under Colo. Rev. Stat. §§ 39-10-113 and 39-10-111(11)) against the lessor's *title* to the aircraft leased to the debtor, Western Pacific Airlines, as opposed to the lessee-taxpayer's *leasehold interest* in the aircraft. Of course, the trustee was hoping to treat the property subject to the tax lien under Bankruptcy Code § 724(b). The Bankruptcy Court ruled in favor of the lessors, holding that the counties' personal property tax liens did not attached to a lessor's *title* to the leased property, here, several 737 commercial aircraft. The District Court affirmed and this appeal follow. The Tenth Circuit affirmed. After examining the applicable statutes, the Court concluded that the language of the statutes did not authorize the seizure of a lessor's property to pay the unpaid personal property taxes of the lessee-taxpayer. In contrast, other Colorado statutes and ordinances authorize taxing authorities to subject the lessor's title interest in leased goods to the payment of the unpaid taxes of the lessee-taxpayer, such as the Colorado sales, use and wage and withholding tax statutes. These statutes are constitutional because people conducting business in Colorado have notice of the tax risk and can take advantage of the safe harbor provided under the applicable statutes and ordinances.

***Hill v. Kinzler (In re Forster)*, 2001 U.S. App. LEXIS 27194 (10th Cir. 2001).** The debtor operated several ponzi schemes. The funds obtained by the debtor's fraud were commingled in a common bank account. During the gap period between the commencement of an involuntary petition and the entry of the order for relief, the debtor engaged in a series of transfers to a person fraudulently induced to invest in one of the schemes. The Chapter 7 trustee then sought to recover the funds transferred under § 549(a). The dispute centered on whether the funds transferred were property of the estate. The bankruptcy court held that the funds were subject to a constructive trust and, therefore, were not property of the estate, *ergo*, no unauthorized post-petition transfer occurred. The District Court affirmed but the Tenth Circuit reversed. Two

elements must be established to impose the equitable remedy of a constructive trust: (1) a showing of fraud or mistake in the debtor's acquisition of the property, and (2) the claimant must be able to trace the wrongfully held property. The first element was not in dispute; the second element was. The Bankruptcy Court applied the so-called lowest intermediate balance rule to trace the funds invested by this particular victim into the debtor's commingled bank account. On appeal, the trustee contended that the Bankruptcy Court should have considered whether use of this tracing fiction was equitable in this case. The Tenth Circuit agreed. The lowest intermediate balance rule is an equitable remedy that should not be applied where equity does not warrant the result. The funds in the debtor's account were all from the debtor's fraudulent schemes. To apply the lowest intermediate balance rule to impose a constructive trust in favor of one of the debtor's victims had the result of merely elevating the claim of this victim above all the other victims who sat in the same position. In bankruptcy, the bankruptcy court must weigh the claims of the remaining creditors before employing an equitable remedy such as the lowest intermediate balance rule. **Query:** Can a debtor use the theories of constructive trust or equitable lien to bring property into the estate?

Sladek v. Zeman (In re Sladek), 269 B.R. 229 (D. Colo. 2001) (J. Kane). Debtors filed Chapter 7 and then converted to Chapter 13 after the order of discharge was entered. The Chapter 13 trustee objected to certain exemptions claimed by the debtors, objected to confirmation of the Chapter 13 plan for lack of good faith and moved to reconvert the Chapter 13 to Chapter 7. The Bankruptcy Court ruled in favor of the Chapter 13 Trustee on all issues and this appeal followed. On appeal, the debtors argued that the property was incorrectly claimed as exempt and that the debtors meant to not include it all. The property consisted of certain malpractice claims, which were not exempt under state law. The Court affirmed the denial of the exemption. Second, the Court affirmed the Bankruptcy Court's finding of lack of good faith and the conversion. The Court considered the totality of the circumstances to find the lower court's ruling proper, which consisted of conversion after entry of discharge, significant errors of omission in the schedules, and the debtors' resistance to the efforts of the Chapter 7 and 13 trustees to administer the assets of the estate.

Manion v. Providian National Bank, 269 B.R. 232 (D. Colo. 2001) (J. Kane). Everyone should take a few minutes to read this case. Judge Kane proves himself to be quite a storyteller. The case involves redemption rights, the effect of Bankruptcy Code § 1327(b) and § 549(a). This case itself has quite a complicated set of facts. The debtor's Chapter 13 plan provided that a parcel of real property would be surrendered. Prior to confirmation, the first lender obtained stay relief and proceeded with foreclosure. Shortly before the owner's redemption expired, the owner without bankruptcy court authorization granted three deeds of trust on the property to an apparent third party. The debtor did not surrender the property as required under the Chapter 13 plan and redemption was made by the holder of the three deeds of trust, who obtained a public trustee's deed to the property and sold it at a profit. Adversary proceedings were commenced. The court held that the grant of the deeds of trust were unauthorized post-petition transfers and that these deeds of trust further were invalid under § 1327(b) and the Chapter 13 plan. The court affirmed the bankruptcy court's award of damages.

***Ketel Thorstenson, L.L.P. v. Swanson (In re Swanson)*, 2001 U.S. App. LEXIS 27606 (BAP 10th Cir. 2001) (also appearing at 2001 Bankr. LEXIS 1645).** Debtor had embezzled money from his employer and filed Chapter 13. The employer sued the debtor's supervisor (an outside third party) for failure to monitor the debtor's work activities properly and to review the transactions of the debtor. The third-party supervisor then sought stay relief to join the debtor as a party to the litigation to establish his percentage responsibility for the employer's losses but specifically did not seek to recover damages from the debtor. At the stay relief hearing, the debtor argued that he was unable to defend the lawsuit because all of his excess income was being paid under his confirmed Chapter 13 plan. The bankruptcy court denied the stay relief motion but allowed the movant to depose the debtor. This appeal followed. The BAP affirmed. The movant had failed to provide to the Court a transcript of the bankruptcy judge's oral ruling and, therefore, movant had failed to provide an adequate record for the appeal. **Query:** Why did the debtor care?

***Zubrod v. Kelsey (In re Kelsey)*, 270 B.R. 776 (B.A.P. 10th Cir. 2001).** Husband and wife maintained a joint checking account. Both spouses had unrestricted access to all funds in the account. The husband worked outside the home; the wife did not. A couple of days after entry of an arbitration award against the husband, the husband withdrew all the funds in the joint checking account and made two mortgage payments, paid the attorney in the arbitration action and his bankruptcy counsel and gave one-half of the cash to his wife. The debtor then filed Chapter 7. Thereafter, the wife re-deposited the funds into the checking account. The trustee sought to recover the funds transferred to the wife as a fraudulent conveyance under Bankruptcy Code § 548, claiming the transfer was for less than reasonably equivalent value. The Bankruptcy Court entered judgment in favor of the trustee and this appeal followed. On appeal, the wife argued that one-half of the funds in the account was her property and that, in any event, she gave "value" for the transfer on account of *past* and future support and love. As to the **first** contention, the Court ruled that once the debtor-husband withdrew the funds from the joint checking account, title to all the cash passed to him; at that point, the cash was his property which he could dispose of as he pleased. When he transferred part of the withdrawn cash to his wife, that transfer constituted a transfer of the debtor's property for § 548 purposes. As to the **second** contention, the Court held that intra-family support and love do not constitute "value" under § 548(d)(2)(A) which must be "quantifiable," concluding that the transfer was not supported by reasonably equivalent value. Next, the Court considered whether the transfer constituted an actual fraudulent conveyance under § 548(a)(1)(A). Reviewing the traditional factors of fraud, the Court concluded that the transfer satisfied the actual fraud standard. The transfer was to an insider, made while the debtor was insolvent, for no consideration and made in contemplation of the bankruptcy filing. The Bankruptcy Court's decision was affirmed.

***Skehen v. Miranda (In re Miranda)*, 2001 Bankr. LEXIS 1549 (B.A.P. 10th Cir. 2001).** This appeal involved 9 cases in which the Chapter 13 trustee sought the 10% fee under 28 U.S.C § 586 from payments to the Chapter 13 trustee in cases either dismissed or converted prior to confirmation of the Chapter 13 plans. In each of the 9 cases, the Bankruptcy Court denied the Chapter 13 trustee's request for fees. Reviewing the relevant statutory provisions, the Court affirmed. The Court concluded that Chapter 13 trustees are entitled to payment of the 10% fee only upon confirmation of a Chapter 13 plan and that the Chapter 13 trustee is not entitled to an

administrative expense claim under Bankruptcy Code § 503. In reaching this conclusion, the Court noted the difference between Chapter 12 and Chapter 13, where under Chapter 12, the trustee is expressly entitled to the fee prior to returning any funds to the debtor following dismissal or conversion of a Chapter 12 case. The Court was sympathetic to the Chapter 13 trustee's position, but concluded that the statute was clear and the remedy had to be sought with Congress.

***In re Patterson*, Case No. 99-25093 SBB (01-10-02; Docket No. 52).** This case concerns adequacy of Chapter 13 debtor's counsel's fee disclosure and propriety of a "fee reserve" in a Chapter 13 plan. Court rules that the § 329 disclosure made on Local Form 102.1, while "legally sufficient," is not adequate under the circumstances. The ruling requires, prospectively, that after February 1, 2002, where a fee agreement materially varies from the "baseline" scheme of legal services set forth in General Order 2001-1, the disclosure statement must either detail that variation or attach the fee agreement. The Court rules that although use of a fee reserve in a Chapter 13 plan is not improper, it is ripe for abuse if not utilized when the debtor needs post-petition legal services.

***In re Gorodess*, Case No. 01-17854 MSK (12-31-01).** The Chapter 7 trustee sought to sell the debtor's Avalanche season tickets. The debtor argued that transfer restrictions caused these not to be property of the estate or of inconsequential value to the estate and thus not subject to sale by the trustee. Judge Krieger found that the debtor's interest in Avalanche season tickets and renewal privileges constituted property of the estate, although controlled by Colorado state law. The Court ordered the debtor to pay the trustee the purchase price of all games already played in the current season and turn over tickets for games not yet played. In addition, the Court authorized the trustee to sell the unused tickets for the current season at a price not to exceed the face amount of the ticket, plus tax. Lastly, the Court ruled that the trustee could not sell season renewal rights without the consent of the Colorado Avalanche, but such rights could be relinquished to the Avalanche in consideration of payment for tickets for games not yet played.

***Baroway & Dawson, P.C. v. Euell (In re Euell)*, Case No. 01-13050 DEC, Adversary No. 01-1237 EEB (01-02-02).** The Court found that the law firm which served as the *guardian ad litem* for the debtor's children during her divorce did not have standing to assert a claim against the debtor under 11 U.S.C. § 523(a)(15) because the legislative history indicates that such an action belongs solely to an ex-spouse.

QUESTION: Could this claim have been successfully prosecuted under 11 U.S.C. § 523(a)(5)?

***Munaf v. Turner (In re Turner)*, Case No. 00-24966 MSK, Adversary No. 01-1095 ABC (11-08-01).** The Court found nondischargeable under § 523(a)(5) attorney fees that had been awarded against the debtor in a state court dependency and neglect proceeding to the lawyer for the person other than the parents of the minor children in whose interest the state court proceeding was brought and who was awarded permanent parental responsibility.

In re Alling*, Case No. 01-18412 ABC (12-18-01).** The Court confirmed a Chapter 13 plan, over the Chapter 13 trustee's objection (withdrawn in the course of the hearing), which provided for payment of child support arrearages over 35 months by direct payments to the nondebtor ex-spouse under an order to the debtor's employer. This case dispensed with the requirement of written consent of the nondebtor ex-spouse in such circumstances previously imposed by ***In re Davidson, 72 B.R. 384 (Bankr. D. Colo. 1987).

***In re Fickinger*, Case No. 01-10591 ABC (07-27-01).** The Court sustained a creditor's objection to confirmation of a Chapter 13 plan based on § 1325(a)(3), finding on the particular evidence presented that the plan had not been proposed in good faith.

***In re Murphy*, Case No. 02-16366 ABC (01-09-02).** Relying on the plain language of section 326(a) and the absence of legislative intent to the contrary, the Court denied the Chapter 7 trustee's application for an administrative expense claim for reasonable compensation for his Chapter 7 services in the Chapter 13 to which the case had been converted prior to any distributions in the Chapter 7.

Wilson v. Deselms (In re Deselms)*, Case No. 00-20898 DEC, Adversary No. 00-1595 ABC (12-03-01).** The Court declined to approve a settlement of an adversary proceeding involving challenges both to dischargeability of the debt to the plaintiff **and** to the debtor's discharge, finding that the specific terms of the proposed settlement included the debtor's giving the plaintiff consideration for dropping the challenge to the debtor's overall discharge. The Court severed the dischargeability and discharge claims and required the plaintiff to proceed with adjudication or settlement of the former before prosecuting or dismissing the latter. ***See Pennwell Printing Co. v. Stout (In re Stout), Case No. 00-14884 MSK, Adversary No. 00-1351 ABC (05-17-01).

***Professional Home Health Care, Inc. v. U.S. Department of Health and Human Services, Health Care Financing Administration, et al. (In re Professional Home Health Care, Inc.)*, Case No. 01-12254 ABC, Adversary No. 01-1217 ABC (07-31-01).** The Court denied a T.R.O. seeking to enjoin, under the section 362(a) automatic stay, efforts to terminate a Chapter 11 debtor-in-possession's Medicare service agreement on a finding, following an evidentiary hearing, that the respondents' efforts were a bona fide exercise of police and regulatory power, excepted from section 362(a) by section 362(b)(4), as opposed to an effort by regulators to pursue their own pecuniary interests. The case was on remand from the United States District Court following Judge Kane's reversal of an initial similar determination that had been made by the Bankruptcy Court, based on affidavits and argument, without the opportunity for an evidentiary hearing.

King v. Barree (In re Coury)*, Case No. 99-17396 SBB, Adversary No. 01-1051 ABC (06-08-01);** Motion for Reconsideration denied (06-29-01) (pending appeal*** to U.S. District Court, Case No. 01-AP-1286). Pursuant to 28 U.S.C. § 1334(c)(1), the Court abstained from adjudicating a Chapter 7 trustee's claim against the personal representative in a pending state court probate proceeding. The Chapter 7 trustee, under section 541(a)(5), succeeded to the debtor's inheritance when the debtor's father died within 180 days following the filing of the bankruptcy.

The personal representative in the probate proceeding sought, under state probate law, to offset a debt owed the decedent by the debtor in the course of calculating the amount of the inheritance due the bankruptcy estate. The Court also dismissed for failure to state a claim under 11 U.S.C. § 549(a) the Chapter 7 trustee's claim against the debtor's ex-husband who had been paid \$48,257.25 by the probate estate on a debt of the decedent as guarantor of the debtor. The Court found section 549(a) inapplicable because the payment had not been made with "property of the [bankruptcy] estate," but instead with property of the probate estate.

In re Moreno, Case No. 01-10587 ABC; In re Hotel Frisco, L.L.C., Case No. 10588 (jointly administered), Docket No. 105 (01-17-02). The Court declined to approve a stipulation for limited stay relief in Chapter 7 under which operating control of the estate's assets would pass from the trustee under section 721 to a mortgagee-in-possession pending the trustee's efforts to sell the debtor's hotel assets as an operating concern. In disapproving the stipulation, the Court ruled that it sought an improper delegation of the trustee's limited Section 721 operating authority, as well as de facto appointment of a receiver contrary to the prohibition of Section 105(b).