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PROGRAM SUMMARY 6-12-21

By: Gary R. Wallace-Program Summary Committee Chair

CDCBAA Holds Sixth Meeting and MCLE Program of 2021: "The Fight Against an Alarming Trend: Section 706(b) Motions, and State Court Comes to Bankruptcy Court"

On June 12, 2021, the CDCBAA held its sixth members meeting and MCLE program of the year. To help mitigate the spread of COVID-19, the meeting and program were conducted as a live webinar via Zoom video. The program topic was: " **The Fight Against an Alarming Trend: Section 706(b) Motions, and State Court Comes to Bankruptcy Court**." The distinguished panel featured local practitioners Nicholas Gebelt, Esq., James Selth, Esq., and Robert Aaronson, Esq. CDCBAA President Hale Antico moderated.

As our learned speakers explained, the trend which is causing concern for individual debtors and their counsel is the filing of motions (usually by trustees) pursuant to 11 U.S.C. section 706(b) to *convert* individual Chapter 7 cases to Chapter 11. Section 706(b) states: "On request of a party in interest and after notice and a hearing, the court may convert a case under this chapter to a case under chapter 11 of this title at any time. These conversion motions are being filed as to individual debtors whose debts are not primarily consumer in nature (i.e., primarily business debt), and typically only when such debtor's income substantially exceeds his/her expenses. While it is true that section 707(b) contains its own dismissal provisions when an individual debtor's income exceeds his/her expenses, section 707 is *expressly limited to individuals with primarily consumer debt*. So, the critical distinction to keep in mind is this: just because an individual with primarily business debt is exempt from section 707(b)'s mean's test (and thereby also exempt from the dismissal language contained therein), that same debtor (with primarily business debt) may find himself/herself the subject of a conversion motion under section 706(b).

Another driving force behind section 706(b) motions is the inability to utilize the "for cause" and "including" language contained in section 707(a) to obtain dismissal in business debt individual cases. While case law is a bit thin on this issue, at least one court in the 9th Circuit has determined that an "ability to repay" is not a sufficient basis for dismissal under 707(a) in non-primarily consumer debt cases. See *In re Motaharnia*, 215 B.R. 63 (Bankr. C.D. Cal. 1997)("there is no evidence that Congress intended for [ability to pay] to be considered cause under section 707(a)").

The speakers suggested several ideas for opposing a section 706(b) motion (or at least reducing the chances that one will be filed). First, it was noted that, because such motions will not likely be granted after a discharge has been entered, counsel should be very reluctant to agree to extend the time for entry of a discharge. Second, there are several decisions which the speakers noted (and which are contained in their handout) which have found that these motions are an unauthorized end-run around the limitations of section 707(b), and that section 706(b) was never intended to permit such a strategy. Other decisions discussed by the speakers have observed that section 706(b) cannot be used to force an individual debtor into a repayment plan. Still other cases have found that the debtor's interests (including his/her right to obtain a "fresh start") are at least relevant factors in deciding whether such a motion should be granted. It was

further noted that such motions rarely have traction in court unless the income/expense disparity is extreme. Constitutional arguments arising from the Thirteenth Amendment's prohibition against involuntary servitude may also help, since they are analogous to the concerns and restrictions applicable to Chapter 13 case conversions.

Our speakers also discussed which debts are "consumer" and which are "business" for filing purposes. Involuntary debts are not consumer debts. Thus, tax debts are not consumer debts. See *Westberry*, 215 F.3d 589 (6th Cir. 2000). It is possible that certain medical debts (normally considered consumer debts) may qualify as nonconsumer debt when they arise from an emergency. See, e.g., *In re Sijan*, 611 B.R. 850 (Bankr. S.D. Ohio 2020). Student loan debts are more complicated, with the litmus test being the "primary purpose" for which the debt was incurred. Under the same approach, a personal home loan for the debtor's residence is normally a consumer debt. See *In re Kelly*, 841 F.2d 908 (9th Cir. 1988); but see *In re Cherrett*, 873 F.3d 1060 (9th Cir. 2017)(business reason predominated in purchase of temporary second home).

A valuable 49-page outline, containing many case citations and summaries, was presented to all registered participants.

The next CDCBAA members meeting and Zoom MCLE program will be held on July 10, 2021. The topic will be "Non-Attorney Professionals in Bankruptcy." We hope you will join us.

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