BANKRUPTCY LAW NEWSLETTER

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TENANCY BY THE ENTIRETIES - THE FINAL CHAPTER? *

The U.S. Sixth Circuit Court of Appeals released its decision in Craft v. United States on April 1, 1998 reversing the District Court judgment and indicating once again that a tax lien for one spouse does not attach to tenancy by the entireties ownership of real property in the State of Michigan. The Sixth Circuit held that state real property law determines what property rights exist, and then federal law determines what consequences such as tax lien attachment result from those property rights.

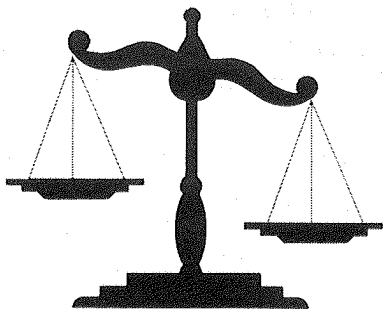
The Court traced the history of the tenancy by the entireties issue through its previous decisions in Cole v. Cardoza and Leroy Lane I and II. The Court reiterated that a tax lien for one spouse does not attach to tenancy by the entireties as it is defined by Michigan real property law.

The Court then next examined the argument of the government that when both spouses signed a Quit Claim Deed, that for some transitory moment the entireties estate was terminated and Don Craft owned an undivided one-half interest in the property which the lien could then attach to. The Court disagreed and indicated that it was unaware of any precedent that reflected an intermediary step when tenancy by the entireties property is conveyed by Quit Claim. The panel then examined whether or not under federal law the IRS lien could attach to any future

interest that the tax-payer held in the real property and once again indicated that the Court was bound to define any future interest in the property by Michigan real property law. Relying on the 1918 case of Sanford v. Bertrau, the Court indicated that Don Craft did not possess any separate future interest, therefore the federal tax lien could not attach to some future interest which did not exist under Michigan law.

The Court closed by remanding the case back to the District Court to determine whether or not the conveyance to Sandra Craft constituted a fraudulent conveyance against the IRS, an issue that was never ruled upon by the District Court during the first trial.

* Case summarized by Jeff Moyer of Donovan, Love & Twinney who briefed and argued the case before the Sixth Circuit last September.



OTHER RECENT OPINIONS

Eastern District of Michigan

Failure to Timely Serve Complaint does not Warrant Dismissal of Adversary Proceeding. Bankruptcy Rule 7004(a).

The Debtor had set fire to his office, and plead guilty to arson. Later he filed for Chapter 7 Bankruptcy relief. The insurance companies filed an action under §523(a)(6) objecting to the dischargeability of the arson damages. The insurance companies timely filed the adversary proceeding, but failed to serve process within 120 days. The Debtor Defendant filed a motion to dismiss.

The Court analyzed Federal Rule of Civil Procedure 4(m), incorporated by Bankruptcy Rule 7004 (a), particularly the 1993 amendments. The rule, as amended provides "If service of the summons and complaint is not made upon a defendant within 120 days after the filing of the complaint, the court, upon motion or on its own initiative after notice to the plaintiff, shall dismiss the action without prejudice as to that defendant or direct that service be effected within a specified time; provided that if the plaintiff shows good cause for the failure, the court shall extend the time for service for an appropriate period. Based upon the amendment, the Court found that the plaintiff did not have to show good cause why service was not made.

The Advisory Committee on the Civil Rules specifically authorizes the Court to relieve a plaintiff of a potential dismissal, even if no good cause is shown. The court noted the change in the rule was to allow the Court to avoid draconian penalties for technical mistakes. Here, if the adversary proceeding had been dismissed, a subsequent action would be time barred by Bankruptcy Rule 4007(c). The Court found additional factual support for its

finding in the fact that the Debtor's attorney had been aware of the Complaint, had engaged in settlement negotiations, and had not challenged the sufficiency of process in the motion.

In re: Madar Case No. 97-30342
Westfield Insurance Companies, et al v. Madar.
Adversary Proceeding No. 97-3030; March 19, 1998
Honorable Arthur J. Spector

Eastern District of Michigan

Creditors May Not Use Attorney Discipline Process to Collect Dischargeable Debt.
-Section 524 (a)

An attorney was retained to handle a personal injury action. The attorney failed to file the complaint, a legal malpractice action was commenced. The attorney and his former client accepted a mediation award of $27,500. The attorney then filed Chapter 7 and listed the debt to his former client. The former client did not object to the discharge of the debt, and the Debtor's discharge was granted.

The former client retained new counsel and filed a request for investigation with the Attorney Grievance Commission. The basis for the request was the malpractice. The Debtor submitted several Stipulated Orders of Discipline to the Commission providing for a reprimand, a period of supervised probation and payment of costs. The former client objected to each Stipulated Order because they failed to provide for payment of the discharged debt. The Debtor filed a motion with the Bankruptcy Court asserting that the former client and his new counsel are violating the permanent injunction set forth in §524(a) by attempting to have the discharged debt paid as part of the grievance procedure.
The Court found the former client's efforts and those of his attorney violated the provisions of §524(a)(2). The Court found the persistent and unrelenting attempts to secure payment of the discharged debt as part of the grievance procedure are a clear violation of that section. The Court noted that the Attorney Discipline Board would be in violation of § 525(a) if it ordered the Debtor to re-pay the discharged debt.

With regard to damages, which §524 has no express authorization, the Court found authority to award them based on the inherent contempt power of the Court. Further, the Court noted that in cases involving "malevolent intent", punitive damages could be awarded. Here, no punitive damages were ordered since the Court found the parties to be acting more out of ignorance than a clear disregard and disrespect of the bankruptcy laws.

In re: Borowski; Case No. 93-53927-R
Eastern District of Michigan - Honorable Steven W. Rhodes
United States Bankruptcy Judge.
February 27, 1998

Ninth Circuit

Chapter 7 Debtor Can Keep Automobile Despite Failure to Surrender, Redeem or Reaffirm.

The Ninth Circuit Court of Appeals recently ruled that a Chapter 7 Debtor

may retain an automobile and continue to make the payments, without electing whether to redeem the property or reaffirm the debt. The Circuits are split on this issue with the Second, Fourth and Tenth Circuits, and now Ninth allowing the Debtor to retain property without following one of the intentions set forth in §521(2)(A). The Fifth, Seventh and Eleventh Circuits take the view that once a debtor decides to retain property, he or she is restricted to the options of claiming an exemption and redeeming or reaffirming the debt.

McClellan Federal C.U. v. Parker
Ninth Circuit, No. 96-15784, March 17, 1998

U.S. Supreme Court

Punitive Damages Awarded on Account of Fraud are Non-Dischargeable.

A unanimous Supreme Court held that a Chapter 7 Debtor's liability for treble damages, plus attorneys fees and costs, arising from over-charging tenants in violation of a city rent control ordinance are non-dischargeable in accordance with §523(a)(2)(A). The Court concluded that 523(a)(2)(A) is best read and understood to prohibit the discharge of a liability arising from a debtor's fraudulent acquisition of money, property or services, including an award of treble damages for fraud. The court rejected arguments that only the portion of liability representing a restitutimony recovery should be non-dischargeable indicating that had Congress wanted to do so, they would have made that intent clear.

Cohen v. De La Cruz
U.S. Supreme Court No. 96-1923
Opinion by Sandra Day O'Connor
March 24, 1998

FEDERAL BAR ASSOCIATION BANKRUPTCY SECTION STEERING COMMITTEE MINUTES. MARCH 20, 1998.

Present: D. Andersen; T. Curtin; P. Mears; H. Nelson; S. Rayman; E. Richards; B. Rodgers; T. Sarb; T. Schouten; P. Teholiz; R. Wardrop; R. Wright; M. Van Allsburg; T. VanHattum.

I. REPORT ON SUMMER SEMINAR

Peter Teholiz reported to the Steering Committee that the plans are well underway for the FBA Summer Seminar which will be held at the Park Place Hotel in Traverse City, Michigan, on July 30, 31 and August 1, 1998. the seminar will include panel discussions regarding the following topics as they relate to bankruptcy law: tax issues and dealing with the IRS; family law and marital issues; religious contributions; retirement plans; dealing with the Chapter 13 Trustee's office; and HMO insolvencies.

II. REPORT FROM THE TECHNOLOGY SUBCOMMITTEE

Robert Wright delivered a report from the Technology Subcommittee regarding a proposal to distribute bankruptcy court opinions on CD-ROM. The Technology Subcommittee has concluded that it would be simpler, more efficient and more cost effective for the bankruptcy court to make the bankruptcy judges' past opinions available on the court's website which

would allow practitioners to access the opinions via the Internet. The Technology Subcommittee will seek to obtain the court's approval and cooperation in this project.

III. PROPOSED LOCAL RULE 7.03 - IMPLEMENTATION OF SECTION 521(2)

Tom VanHattum presented a proposal from the Consumer Bankruptcy Coalition to amend the Local Rules of the Unites States Bankruptcy Court for the Western District of Michigan. The proposed rule concerns the implementation of Section 521(2) regarding the statement of consumer debtor's intentions with respect to the retention or surrender of secured property with notice, but without seeking a lift of stay, where the debtor has previously reaffirmed a secured debt, but has failed to make the required payments. The proposed rule is patterned after a similar rule (L.B.R. 7.03) which is in effect in the Bankruptcy Court for the Eastern District of Michigan. Any comments concerning the proposed rule should be directed to Robert Wright as chair of the Local Rules Committee.

IV. JUDGE HOWARD'S RETIREMENT

It was recently announced that Judge Laurence E. Howard will be stepping down from the bench effective March 1, 1999. Judge Howard has also relinquished his duties as Chief Judge, and Judge Gregg has been appointed to assume the role of Chief Judge, effective immediately.

The Steering Committee discussed various proposals to express the bankruptcy bar's admiration and respect for Judge Howard on the occasion of his retirement following a long a distinguished career as a lawyer and a jurist. The Steering Committee has previously obtained approval from the Federal Bar Association for the commissioning of a portrait of Judge Howard. The Committee has also discussed various proposals to honor Judge Howard and recognize his accomplishments on the Bench. The Steering Committee welcomes any suggestions regarding appropriate tributes to Judge Howard.

Further discussion was held regarding the process for selecting a replacement for Judge Howard. The United States Court of Appeals for the Sixth Circuit will appoint a selection committee to interview candidates and make recommendations which are then submitted to the Sixth Circuit for the final appointment. The Bankruptcy Steering Committee will recommend that the Federal Bar Association request that the selection committee include bankruptcy practitioners.

V. NEW BUSINESS

Patrick Mears noted that the Federal Bar Association annual meeting will be a social event held at the Meijer Gardens on October 8, 1998.

There being no further business, the meeting was adjourned.

SUMMER BANKRUPTCY SEMINAR

In addition to the Michigan FBA Bankruptcy Section Seminar, which will take place on July 30 to August 1, 1998 at the Park Place Hotel in Traverse City, Michigan (which every attorney should seek to attend), there is another seminar that FBA Bankruptcy Section members may wish to attend this summer. The 16th Annual Norton Institute Seminar will again take place at the Jackson Lake Lodge, Jackson Hole, Wyoming, on July 2-5, 1998.

Judge Gregg will be speaking on "Individuals in Chapter 11" and "Chapter 11 Post-Confirmation Matters". Consumer law issues will be addressed by Judge Lundin and Judge Waldron.

The geography and surroundings are spectacular! It includes the Grand Tetons, Yellowstone National Park (wildlife and geyser basins), and the Snake River (as well as other rivers and fishing streams).

Judge Gregg is planning a white water rafting trip on the Snake River on Sunday afternoon, July 5, immediately after the conclusion of the seminar. **All FBA Bankruptcy Section members are invited to join this outing!** Telephone Linda Lane at (616) 456-2264 for information. Persons interested in the white water trip must sign up by June 1, 1998 through Judge Gregg's office.

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LOCAL BANKRUPTCY STATISTICS

CHAPTER	MARCH - 1998	YTD - 1998
Chapter 7	830	2,116
Chapter 11	5	11
Chapter 12	1	3
Chapter 13	256	720
TOTALS	1,092	2,850

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