

## BANKRUPTCY—CREDITORS' RIGHTS

### DEBTOR'S STATE AND FEDERAL TAX REFUNDS ARE EXEMPT FROM THE BANKRUPTCY ESTATE

In re Charles Benn, Jr. 340 B.R. 905 (2006).

**FACTS:** Mr. Charles Benn, Jr. filed a petition under Chapter 7 on December 31, 2003. In his third amended schedules, he claimed an exemption in all possible 2003 tax refunds under Mo.Rev.Stat. § 513.427, 26 U.S.C. § 6402, and 31 U.S.C. §3727. The trustee filed an objection to the claimed exemption. Prior to an order being entered concerning the claim of exemption, the debtor received a refund of the 2003 federal income tax withholding in the amount of \$1502. He also received a refund of the 2003 state income tax withholding in the amount of \$36. After the debtor received the refund checks, the Trustee filed a motion for turnover of the refunds to which the debtor objected. The Eastern District of Missouri overruled debtors' exemption claims and ordered turnover of refunds, and debtors appealed.

**HOLDING:** Reversed and Remanded

**REASONING:** The Court reasoned that, on the date that Chapter 7 petitions were filed, prior to the end of tax year to which refunds related, debtors had only contingent right to refunds. This interest was not subject to attachment under Missouri law, and could thus be claimed as exempt by debtors.

In making its decision, the court looked to a 1970 Missouri Court of Appeal's case, which cited an 1876 Missouri Supreme Court case, for the proposition that "[t]he debt for which an attachment may issue must possess an actual character and not be merely possible, and dependent upon a contingency which may never happen." *State Gov't Employees Ins. Co. v. Lasky*, 454 S.W.2d 942, 950 (Mo.App.1970). The court in *Lasky* noted that "[b]y an unbroken line of decision since that time our Courts have held that to be the subject of a garnishment the debt must be certain and not contingent." *Lasky*, 454 S.W.2d at 950.

The court in the instant case reasoned that the tax returns are contingent because the tax refunds that the trustee argues are not exempt did not exist in fact on the petition dates. Both petition dates precede the end of the tax year. The refunds, if any, could not be determined by the Internal Revenue Service or anyone else on the petition date, because of income that could have been earned following the filing of the petition, and because of deductions or credits for which the debtors/taxpayers may have been eligible following the petition date. Therefore, the "refunds" in question were contingent and not certain on the petition date. Under the *Lasky* analysis, such contingent interest could not be attached under Missouri law by any creditor.

The court held that Benn's tax refunds were not subject to attachment under Missouri law because Benn filed the Chapter 7 petitions prior to the end of the tax year to which the refunds related. As a result, Benn had only a contingent right to the refunds, and could thus be claimed as exempt.

### TAKING OF PLAINTIFF'S HOUSE FOR TAX LIEN VIOLATES CONSTITUTION

Jones v. Flowers, 126 S. Ct. 1708 (2006).

**FACTS:** In 1967, Gary Jones purchased a house in Little Rock, Arkansas. He lived in the house with his wife until they separated in 1993. He moved out while his wife continued living in the house. Jones paid the mortgage each month for 30 years, and the mortgage company paid Jones' property taxes. After Jones paid off his mortgage in 1997, the property taxes went unpaid and his property was certified as delinquent. In April 2000, the Commissioner of State Lands attempted to notify Jones of his tax delinquency and his right to redeem the property by mailing a certified letter to Jones at the North Bryan Street address. The letter stated that unless Jones redeemed the property, it would be subject to public sale in two years. No one was home to sign for the letter, and it remained unclaimed in the post office for fifteen days until it was returned to the Commissioner.

Two years later, in April 2002, the Commissioner published a notice of public sale, and a few months later, Linda Flowers submitted a purchase offer. The Commissioner mailed Jones another certified letter to the same address notifying him that the property would be sold unless he paid the taxes. This letter was also returned unclaimed, and Flowers completed the purchase. Immediately after the thirty-day period for post-sale redemption, Flowers had an unlawful detainer notice delivered to the property. ARK. CODE ANN. § 26-37-202(e). The notice was served on Jones' daughter, who notified him about the tax sale.

Jones filed a lawsuit in Arkansas state court against the Commissioner and Flowers, alleging that the Commissioner's failure to provide notice of the tax sale and of Jones' right to redeem resulted in the taking of his property without due process. The trial court granted summary judgment in favor of the Commissioner and Flowers, holding that the notice procedure followed by the Commissioner complied with the constitutional due process requirement. Jones appealed, and the Arkansas Supreme Court affirmed the trial court's judgment. The court held that attempting to provide notice by certified mail satisfied due process in the circumstances presented. Jones then appealed to the Supreme Court of the United States.

**HOLDING:** Reversed.

**REASONING:** The government may hold citizens accountable for tax delinquency by taking their property. Before doing so, however, due process requires the government provide adequate notice of the impending taking. U.S. CONST. amend. XIV. The Supreme Court granted certiorari to resolve a conflict among the circuits and the state supreme courts concerning whether the Due Process Clause requires the government to take additional reasonable steps to notify a property owner when notice of a tax sale is returned undelivered.

**Due process does not require a property owner receive actual notice before the government may take his property.**

# RECENT DEVELOPMENTS

In *Dusenbery v. United States*, 534 U.S. 161 (2002), the Court held that due process does not require a property owner receive actual notice before the government may take his property, but requires the government to provide “notice reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections. *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306 (1956). The Commissioner argued that once the State provided notice reasonably calculated to inform Jones of his impending tax sale via mailing a certified letter, due process was satisfied. However, the courts of appeals and the state supreme courts have frequently addressed this issue and held that when the government learns its attempt at notice has failed, due process requires the government to do something more before real property may be sold in a tax sale.

The Commissioner relied strongly on Arkansas law for providing notice by certified mail to an address that the property owner is responsible for keeping up to date. ARK. CODE ANN. § 26-35-705. However, the Court held that the government must consider unique information about an intended recipient regardless of whether a statutory scheme is reasonably calculated to provide notice. Knowledge that notice was ineffective is one of the peculiarities of this case and should be taken into account in assessing the adequacy of the notice. When the Commissioner received the returned certified letter unclaimed, he had good reason to suspect that Jones was in no better position than if it had not been sent at all. Thus, the Commissioner’s effort to provide notice to Jones of an impending tax sale of his house was insufficient to satisfy due process given the circumstances of this case. The judgment of the Arkansas Supreme Court was reversed, and the case was remanded for proceedings consistent with this opinion.

## SANCTIONS AGAINST ATTORNEY ARE NONDISCHARGEABLE IN BANKRUPTCY

Ball v. A.O. Smith Corp., 451 F.3d 66 (2nd. Cir. 2006).

**FACTS:** Debtor-attorney James Jay Ball, Esq. acted for many years as counsel for the Gautreaus in lawsuits arising out of the sale of Harvestore farm silos manufactured by creditor-appellee A.O. Smith Corporation (“A.O. Smith”). With Ball as their counsel, the Gautreaus had filed a complaint against A.O. Smith alleging Racketeer Influenced and Corrupt Organizations Act (“RICO”) and state-law fraud claims in connection with their 1977 purchase of a used Harvestore silo. In August 2000, Judge Melancon granted summary judgment for A.O. Smith and dismissed the action with prejudice. Judge Melancon found that the plaintiffs’ claims were clearly time-barred under the one-year period for the state-law claims and the four-year statute of limitations for the RICO claims.

A.O. Smith sought sanctions against Ball for his role in bringing the suit. At the conclusion of an evidentiary hearing, Judge Melancon determined that “[t]here was not a colorable claim when the lawsuit was filed” and that the plaintiffs’ claims “were so obviously [barred] that under the circumstances it was unreasonable to bring the suit in the first place.” Judge Melancon found that Ball violated both Rule 11 and Section 1927.

In February 2002, Ball filed for bankruptcy. A.O. Smith

filed an adversary proceeding in the bankruptcy court requesting that the sanctions judgment imposed against Ball in the Gautreau proceeding be declared nondischargeable. The court agreed with A.O. Smith that Ball’s actions were willful and malicious, and the debt was, therefore, exempt from discharge. On Ball’s appeal, the Second Circuit Court of Appeals held that his “conduct is properly characterized as ‘willful and malicious,’” and affirmed the bankruptcy court’s holding.

**HOLDING:** Affirmed.

**REASONING:** The court found that Judge Melancon made specific factual findings that satisfied the Bankruptcy Code’s malice requirement. Although Judge Melancon’s opinion did not use the terms “malicious” or “malice,” his decision to award sanctions under Section 1927 was affirmed by the fifth circuit, which adopted standards for such an award requiring findings that are the equivalent to findings of malice. The court held that the actions encompassed the concept of malice because the action was undertaken without just cause or excuse.

## BANKRUPTCY LAWYER’S CONFLICT REQUIRES DISGORGEMENT OF FEES

In re James Gregory, 340 B.R. 915 B.A.P. 8th Cir. 2006).

**FACTS:** In June of 2002, attorney Ross Briggs filed a Chapter 13 bankruptcy petition on behalf of his client. Pursuant to local rules, Briggs elected to receive a flat fee of \$1,700 for all services related to the bankruptcy petition including, but not limited to, representation of the debtor on motions to incur debt. From October 2003 to April 2005, the debtor in this case repeatedly failed to make payments according to the repayment plan ordered by the court so the Trustee filed several motions to dismiss the case. Because the debtor was able to cure the arrearage each time, the motions were withdrawn.

During this time, the debtor’s attorney became employed as a mortgage consultant with Wells Fargo Bank. While the attorney stated he did not file any additional consumer bankruptcies after becoming a mortgage consultant, he continued to represent his existing clients, including the debtor in this case. In June 2005, the attorney decided the debtor could benefit from refinancing his mortgage and subsequently filed a motion on the debtor’s behalf seeking permission to incur debt to refinance the loan. The attorney then acted in his capacity as a mortgage consultant with Wells Fargo to refinance the loan. Although the Motion to Incur Debt did state that the debtor agreed to the attorney’s dual representation, no written consent was submitted with the Motion, nor was it made clear that the attorney received a commission for the refinanced loan. The Trustee opposed the Motion to Incur Debt and also filed a Motion for Order Denying Attorney Fees and Directing Disgorgement of Fees Paid in the debtor’s bankruptcy case. The court granted the Motion to Incur Debt. However, after a hearing on the matter, the court granted the Motion to Deny Attorney Fees and required the attorney disgorge any fees he received for his legal services in this case. The attorney appealed the decision.

## A.O. Smith sought sanctions against Ball for his role in bringing the suit.

# RECENT DEVELOPMENTS

**HOLDING:** Affirmed.

**REASONING:** The attorney argued the Debtor knowingly and willingly consented to the dual representation. Additionally, the attorney's representation of Wells Fargo did not adversely affect his legal representation of the Debtor because the transaction allowed an early completion of and withdrawal from the Chapter 13 filing. Because of the Debtor's consent and the lack of adverse affect on the Debtor, the attorney argued, his actions fell within those allowed by the Rules of Professional Conduct. The court, however, determined that the attorney could not have represented the Debtor with absolute loyalty because his legal advice was likely tainted by his desire to remain employed with Wells Fargo.

These conflicting duties of loyalty created an obvious conflict of interest. Even though the attorney obtained the Debtor's consent regarding the dual representation, the court cited the Missouri Supreme Court's holding that some conflicts can't be cured by the client's knowing and voluntary consent. *State ex rel. Union Planters Bank, N.A. v. Kendrick*, 142 S.W. 3d 729, 739 (Mo. 2004) (en banc).. The court also determined the attorney's dual representation constituted a *per se* conflict of interest and, as such created "such an inherent and impermissible conflict that it cannot be waived." As a result, the court upheld the bankruptcy court's decision to deny attorney's fees and order the attorney to disgorge fees received for legal services rendered in this case.

## MISCELLANEOUS

### VOIR DIRE QUESTIONS PREVIEWING WHETHER EVIDENCE IS OUTCOME DETERMINATIVE ARE WITHIN TRIAL COURT DISCRETION

*Hyundai Motor Co. v. Vasquez*, 189 S.W. 3d 743 (Tex. 2006).

**FACTS:** Plaintiffs Victor and Brenda Vasquez filed suit against Hyundai Motor Company and Hyundai Motor America, Inc. ("Hyundai") after Plaintiffs' daughter died in a low-speed automobile collision. Plaintiffs alleged that Hyundai's airbag was defective, deploying with so much force as to break their daughter's neck. Hyundai responded that the Plaintiff's daughter would not have been injured if she had been wearing a seat-belt as required by state law or if she had been placed in the back seat as recommended by the automobile manufacturer.

The trial judge dismissed two jury panels after voir dire. During voir dire of the first two jury panels, the jurors were asked whether their decisions would be predisposed by the lack of a seat belt in the accident. Because a significant number of jurors answered affirmatively to the question, the judge dismissed the first two jury panels. During voir dire for the third jury panel, the judge allowed general questions regarding the jurors' seat belt habits but prohibited disclosure regarding the lack of a seat belt in the case. Then three jurors were excused for cause; twelve jurors and one alternate were selected.

The jury found in favor of Hyundai, and the trial court rendered a take-nothing judgment. On appeal, Plaintiffs argued that the trial court erred in disallowing voir dire questions regarding the lack of a seat belt in this case. The Fourth Court of Appeals first affirmed. However, upon subsequent rehearing en banc, the Fourth Court of Appeals reversed and held that the trial court abused its discretion in disallowing the voir dire question. Hyundai petitioned the Texas Supreme Court for review.

**HOLDING:** Reversed and remanded.

**REASONING:** Voir dire serves the purpose of determining whether a potential juror is disqualified by statute because of bias or prejudice. In *Compton v. Henrie*, 364 S.W. 2d 179 (Tex. 1963), the court stated bias would be found in a juror whose state of mind would naturally infer that he will not act impartially. Prejudice was defined as prejudgment. Voir dire questions addressing bias and prejudice are appropriate.

*Cortez v. HCCI-San Antonio, Inc.*, 159 S.W. 3d 87 (Tex.

2005) held that voir dire questions are improper if they seek to determine how jurors would respond when given case-specific facts. The general rule lies on the policy that a fair and impartial juror reaches a verdict on the basis of the evidence. Similarly, the Court in *Babcock v. Northwest Memorial Hospital*, 767 S.W. 2d (Tex. 1989), differentiated between voir dire questions that assessed the weight jurors placed on external versus case-specific evidence. The Court held that questions regarding bias or prejudice that arise from societal influence outside the case are permissible. Questions regarding an operative fact, however, would improperly skew jurors' view of the case facts.

In Texas the trial judge has broad discretion in conducting voir dire. The Court disagreed with the court of appeals' ruling that the proposed questions "clearly focuses on the ability of the juror to be fair." Instead, the Court reasoned that the question focused on a fact that was specific and material to the case. Although the question was worded in terms of preconceived notions, it emphasized a relevant fact of the case. It is the substance, not the form, of the question which is determinative. Thus, the Court reversed the ruling of the court of appeals.

### AMENDING A COMPLAINT TO ADD A DEFENDANT "COMMENCES" A NEW SUIT UNDER THE CLASS ACTION FAIRNESS ACT OF 2005

*Braud v. Transport Serv. Co. of Illinois*, 445 F.3d 801 (5th Cir. 2006).

**FACTS:** On August 30, 2004, Pamela Braud and certain other plaintiffs ("Braud plaintiffs") brought a putative class action in state court against Transport Service Company of Illinois ("Transport"), arising from a chemical spill. On April 8, 2005, the Braud plaintiffs amended their petition to add Ineos Americas, LLC ("Ineos"), as an additional defendant, contending that Ineos was the owner and co-shipper of the chemical that allegedly spilled. Ineos was served on April 19, 2005.

On May 19, 2005, Ineos timely removed the action to federal court, basing removal jurisdiction on the Class Action

**It is the substance, not the form, of the question which is determinative.**