MISCELLANEOUS

SUPREME COURT UPHOLDS BANKRUPTCY ACT PROVISION

Milavetz, Gallop & Milavetz, P.A. v. United States, 130 S. Ct. 1324 (U.S. 2010)

FACTS: Law firm Milavetz, Gallop & Milavetz, a firm practicing bankruptcy law, the firm's president, an attorney who worked for the firm, and two of the firm's clients ("Milavetz") brought suit against the United States, seeking declaratory judgment that certain provisions of the Bankruptcy Code, added by the Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCA"), were unconstitutional as applied to attorneys and law firms.

The BAPCA amendments created a class of bankruptcy professionals termed "debt relief agenc[ies]." 11 U.S.C. § 101(12A). That class includes, with limited exceptions, "any person who provides any bankruptcy assistance to an assisted person… for… payment…, or who is a bankruptcy petition preparer." *Id.* The amendments prohibit such professionals from "advis[ing] an assisted person… to incur more debt in contemplation of [filing for bankruptcy]…." § 526(a)(4). "Assisted persons" are persons with limited nonexempt property whose debts consist primarily of consumer debt. § 101(3). It also requires them to disclose in their advertisements for certain services that the services are with respect to or may involve bankruptcy relief, §§ 528(a)(3), (b)(2)(A), and to identify themselves as debt relief agencies, §§ 528(a)(4), (b)(2)(B).

Milavetz filed suit, arguing that law firms practicing bankruptcy law are not bound by the debt-relief-agency provisions. The United States District Court for the District of Minnesota, granting summary judgment in favor of Milavetz, found that "debt relief agency" does not include attorneys and that §§ 526 and 528 are unconstitutional as applied to that class of professionals. The government appealed. The Court of Appeals for the Eighth Circuit held that attorneys are "debt relief agenc[ies];" upheld the application of § 528's disclosure requirements to attorneys; and found §526(a)(4) unconstitutional because it broadly prohibits debt relief agencies from advising assisted persons to incur any additional debt in contemplation of bankruptcy even when the advice constitutes prudent prebankruptcy planning.

Shortly after the Eight Circuit opinion, the Fifth Circuit decided a similar case: *Hersh v. United States*, 553 F.3d 744 (5th Cir. 2008). The Fifth Circuit held that attorneys qualify as a debt relief agency when providing bankruptcy assistance; that the prohibition of advising assisted persons to incur more debt only applies to advice that would abuse or improperly manipulate the bankruptcy system; and that the advice and notice provisions do not violate the First Amendment. *Hersh* at 768. The Supreme Court granted certiorari.

HOLDING: Affirmed in part, reversed in part.

REASONING: The Court was presented with two issues: 1) whether attorneys are debt relief agencies when they provide qualifying services; and 2) whether the debt-relief-agency provisions violate the First Amendment rights of attorneys.

The Court reasoned that the "debt relief agency" class includes "any person who provides any bankruptcy assistance to an assisted person in return for… payment…, or who is a bankruptcy petition preparer. § 101(12A). The court found that "bankruptcy assistance" includes several services commonly performed by attorneys and several services that can only be provided by attorneys. In defining "debt relief agency," Congress listed specific exceptions, which did not include attorneys. The Court held that the statutory text clearly indicates that attorneys are "debt relief agenc[ies]" when they provide qualifying services to assisted persons.

Milavetz argued that the amendments should not apply to attorneys because such application would interfere with the States' role in regulating the legal profession when the statute instructed that it should not be "deemed to limit or curtail" States' authority to "determine and enforce qualifications for the practice of law." § 526(d)(2). The Court found that § 526(d)(2) would be made meaningless if the "debt relief agency" provisions did not apply to attorneys. The Court reasoned that such a reading would violate the policy of reading statutes in the manner which gives meaning to all provisions. Further, the Court noted that bankruptcy attorneys have long been exposed to additional strictures and requirements from Congress and the bankruptcy courts.

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Milavetz next argued that 101(12A)'s exception for any "officer, director, employee, or agent of a person who provides" bankruptcy assistance is revealing for its failure to include "partners." Milavetz contended that in light of that omission, treating attorneys as debt relief agencies would obligate entire law firms to comply with §§ 526, 527, and 528 based on the conduct of a single partner, while the agents and employees of debt relief agencies not typically organized as partnerships are shielded from those requirements. The Court noted that there are partnerships in existence that are not law firms and that partnerships are considered "person[s]" under BAPCPA, § 101(41), and therefore can qualify as "debt relief agenc[ies]."

The court held that § 526(a)(4) is not unconstitutional and that the Court of Appeals construed its application too expansively. The Eighth Circuit had characterized the statute as a broad, content-based restriction on attorney-client communications that is not adequately tailored to constrain only speech the Government has a substantial interest in restricting. Milavetz argued that

the provision forbids advice to incur any new debts while considering whether to file for bankruptcy, as well as any discussion of the advantages, disadvantages, or legality of incurring more debt. Milavetz's argued that the ordinary meaning of the phrase "in contemplation of" bankruptcy encompasses any advice given to a debtor with the awareness that he might soon file for bankruptcy, even if the advice seeks to obviate the need to file. Milavetz also argued that a more narrow construction would be so vague as to inevitably chill some protected speech.

The Court held a narrower reading of § 526(a)(4). The Court ruled that the provision prohibits a debt relief agency only from advising a debtor to incur more debt because the debtor is filing for bankruptcy, rather than for a valid purpose. The controlling question under the provision is whether the impelling reason for "advis[ing[an assisted person… to incur more debt" was the prospect of filing for bankruptcy. The Court held that advice to "load up" on debt with the expectation of obtaining its discharge is abusive *per se*.

"Load[ing] up" on debt gained new repercussions under the BAPCPA introduction of the Chapter 7 "means tes[t]," § 707(b)(2)(D) (2006 ed.), where payments on secured debts offset a debtor's monthly income under the formula and effects liquidation, dismissal, or conversion to a structured repayment plan under Chapter 13. The Court noted that the incurrence of this type of debt stands to harm a creditor in lessening the bankruptcy estate and to harm a debtor in that the prepetition conduct can lead a court to hold his debts nondischargeable, convert his case, or dismiss it altogether. The creditor of the new debt, manipulatively incurred but not timely identified as abusive, would suffer the harm of discharge and the dilution of the estate.

Like the Court of Appeals, the Court upheld § 528's disclosure requirements as applied in this case. The court held that § 528's requirements that Milavetz identify itself as a debt relief agency and include certain information about its bankruptcy-assistance and related services are "reasonably related to the [Government's] interest in preventing deception of consumers," *Zauderer v. Office of Disciplinary Counsel of Supreme Court of Ohio*, 471 U.S. 626, 651 (1985). The Court held that § 528 gives Milavetz flexibility to tailor the disclosures to its individual circumstances, as long as the resulting statements are "substantially similar" to the statutory examples. §§ 528(a)(4), (b)(2)(B).

BANKRUPTCY COURT MAY RESTRUCTURE STUDENT LOAN

United Student Aid Funds, Inc. v. Espinosa, 130 S. Ct. 1367 (U.S. 2010)

FACTS: Francisco Espinosa filed a bankruptcy petition under Chapter 13, and listed his four federally guaranteed student loans as his only specific indebtedness. The plan proposed to repay only the principal on the debt, and discharge any accrued interest. The bankruptcy court approved the plan without a required adversarial hearing on the dischargeability of the debt or to determine the presence of undue hardship, and further, the court made no such findings.

The clerk of the court mailed a notice to United Student Aid Funds, the creditor of Espinosa's student loans, both before and after the plan was approved. United made no objection to either the discharge or the absence of an adversarial hearing. After completing payments according to plan, the bankruptcy court discharged Espinosa's student loan interest. Several years later, United began efforts to collect the unpaid interest, prompting Espinosa to file a motion to enforce the discharge order with the bankruptcy court. United subsequently filed a cross-motion seeking to set aside the court's order as void under Federal Rule of Civil Procedure 60(b)(4). The bankruptcy court granted Espinosa's motion, and ordered all claimants to cease and desist their collection efforts. United sought review in the district court, which reversed. Espinosa appealed to the Court of Appeals for the Ninth Circuit, which reversed the judgment of the district court and ultimately held in favor of Espinosa. United appealed, and the Supreme Court granted certiorari.

HOLDING: Affirmed.

REASONING: United argued that the judgment was void for lack of notice, which violated its due process rights, and for fundamental inconsistency with the bankruptcy code. The Court found that a judgment may only be void for either jurisdictional reasons or for violations of due process. Since the bankruptcy court's jurisdiction was unchallenged, the Court focused on United's claim that no proper notice was received. The court quickly dismissed this claim, noting that the actual notice received by United was sufficient to satisfy the technical notice requirements of the bankruptcy code.

The Court went on to note that student loan debt may be discharged only if proper procedures have been followed, including notice given to the creditor and a finding of undue hardship. When these procedures are not followed, the failure is a legal error, but does not affect the enforceability of the judgment. United had actual notice of the deficiencies in the process and judgment but failed to object or appeal timely and, as a result, could not challenge the judgment as being void.

DEFECTIVE SPERM CANNOT BE BASIS FOR PRODUCTS LIABILITY SUITS

D.D. v. Idant Laboratories, 2010 U.S. App. LEXIS 6815 (3rd Cir. Apr. 1, 2010)

FACTS: D.D. was artificially inseminated with semen provided by Idant Laboratories ("Idant"). Shortly after the birth of her daughter, B.D., D.D. began to notice that B.D. had trouble sleeping, tantrums, and development delays. B.D. was diagnosed as a Fragile X carrier. Fragile X is a genetic disease with a wide range of results in the physical, intellectual, emotional, and behavioral characteristic of the patient. The Fragile X gene came from the sperm sold to D.D. by Idant.

In 2008, D.D. filed suit against Idant, on behalf of herself

and her daughter, alleging various product liability claims including, but not limited to: negligence, breach of contract, breach of express and implied warranties of merchantability, and strict products liability. D.D. sought relief for the cost and services needed by B.D. for the treatment of her Fragile X syndrome as well as future costs associated with Fragile X. The district court dismissed D.D's individual claims, finding that they passed the statute of limitations. As to the complaint filed on B.D's behalf, the complaint was dismissed on the ground that New York law does not permit an action for "wrongful life." D.D. appealed arguing that the products liability claims for B.D. were wrongfully dismissed as claims based on an impermissible wrongful life theory.

HOLDING: Affirmed.

REASONING: New York courts have held that a cause of action may not be maintained on an infant plaintiff based on a claim of wrongful life. Wrongful life cases pose special problems because they demand calculation of damages upon a comparison between the choice of life in an impaired state and non-existence. The court found that law is not prepared nor equipped to make such a comparison. Because the laws of New York do not recognize wrongful life cases, all the claims on behalf of B.D. were defective for lack of cognizable injury.

Wrongful life cases pose special problems because they demand calculation of damages upon a comparison between the choice of life in an impaired state and non-existence.

The court held that in arguing that the defective semen caused B.D.'s impairments, D.D. was arguing that B.D.'s genetic makeup was her injury. This was in essence a wrongful life argument. Current New York law does not have a protected right to be born free of genetic defects. The court reasoned that to find contrary and to create such a right would invite litigation for a wide range of claims and force the courts to identify which traits are below some arbitrarily idea of perfection and thus are deemed "injuries."

RESPA CLASS CERTIFICATION REVERSED

Mims v. Stewart Title Guar. Co., 590 F.3d 298 (5th Cir. 2009)

FACTS: Stewart Title Guaranty Company ("Stewart") appealed the district court's order certifying a class action suit brought by mortgagors. The plaintiffs alleged that they were entitled to, but did not receive state law mandated refinancing discounts for title insurance premiums issued by Stewart, and asserted a violation of §8 (b) of the Real Estate Settlement Procedure Act (RESPA). RESPA mandates a prohibition against any person receiving any portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service in connection with a transaction involving a federally related mortgage loan for services not provided. In Texas, when a borrower refinances an existing mortgage, the new lender requires a new title policy. The Texas Department of Insurance's Rate Rule R-8 entitles the borrower to a discount on a policy issued after refinancing if the policy is issued within seven years of the closing of the prior mortgage. The plaintiffs alleged that they refinanced their loan(s) within the mandated discount period but did not receive the discount credit, and Stewart, along with its agents, failed to provide the reissue insurance discount and illegally split the unearned charged on the policies in violation of section §8(b) of RESPA.

HOLDING: Reversed and remanded.

REASONING: The court examined the rule set forth in *Regents of the Univ. of Cal. v. Credit Suisse First Boston*. In *Regents*, the Fifth Circuit concluded that without a class-wide presumption of reliance, the plaintiffs would be left to prove individual reliance on the defendants' conduct which precluded class certification. Applying *Regents*, the court determined that a class action claim under a RESPA violation was improper because the district court's liability model for violations of section §8 (b) required an inquiry into the facts of each individual class members title insurance transaction. The court held that the only way to prove the overall practice violated RESPA, was to examine the reasonableness of payments for goods and services on a transaction-by-transaction basis. The court further ruled that a single finding of liability on an unreasonable relationship between goods and services did not require the conclusion that such unreasonableness existed on a class-wide basis. Therefore, the court concluded that the district court abused its discretion by granting class action certification of the RESPA claim.

CERTIFICATION OF STATE CLASS ACTION CLAIMS AFFIRMED

Mims v. Stewart Title Guar. Co., 590 F.3d 298 (5th Cir. 2009)

FACTS: Mortgagor plaintiffs alleged that they were among numerous consumers who refinanced their home mortgages and failed to receive a mandatory discount on their premiums for new title insurance policies acquired from Stewart Title Guaranty ("Stewart"). Texas Department of Insurance's Rate Rule R-8 entitles the borrower to a discount on a policy issued after refinancing if the policy is issued within seven years of the closing of the prior mortgage. The plaintiffs alleged that they refinanced their loans within the discount period and did not receive the R-8 reissue credit to which they claimed they were entitled. They further alleged that Stewart, through its agents, consistently failed to provide the reissue insurance discount and that Stewart and the agents split the illegal, unearned charges on the policies. In addition to a RESPA violation, plaintiffs raised three state law claims-for money had and received, unjust enrichment, and implied contract. The district court granted the plaintiffs' request for class certification, and Stewart appealed.

HOLDING: Reversed and remanded.

REASONING: Stewart argued that the class definition violated its right to due process and 28 U.S.C.A. 23 because the class was defined using Stewart's Underwriting Guidelines, which were not identical to the legal requirements for eligibility for the R-8 credit. Therefore, Stewart argued, the class as defined may include plaintiffs who are not in fact eligible for the discount. Because this class definition was based on Stewart's own criteria for allowing the R-8 discount, the court found no abuse of discretion in defining the class this way.

Stewart also argued that because of the equitable nature of the plaintiffs' state law claims an individualized factual inquiry was required into the circumstances of each transaction making class certification on these issues an abuse of discretion. The court disagreed, noting that granting the R-8 to an eligible borrower is mandatory. Under Texas law, the court held that disclosure of the discount and waiver are irrelevant because the rate rule sets the maximum amount, net of the applicable discount, that Stewart and other title insurers may charge for reissue title insurance. Accordingly, the court held that the district court did not abuse its discretion by certifying the class as to the state law claims.

The court went on to dismiss the district court's order certifying a class on the RESPA claim and remanded the case to the district court to consider whether it should exercise pendent jurisdiction over the state law claims.

NEGLIGENT ATTORNEY'S FEE ISN'T DEDUCTIBLE FROM MALPRACTICE AWARD

Shoemake v. Ferrer, 225 P.3d 990 (Wash. 2010)

FACTS: Former clients Andrea and Keith Shoemake brought a legal malpractice action against attorney Douglas Ferrer. The Shoemakes had hired Ferrer to represent them in a personal injury case. Ferrer admitted liability for failing to file the Shomakes claim timely and then for failing to show up in court, which resulted in the dismissal of Shoemake's personal injury claim. Both parties moved for summary judgment on damages. The trial court awarded damages of $30,511 and attorney fees of $14,893. Both parties appealed. The Shoemakes argued that the trial court erred as a matter of law in calculating their damage award because it credited Ferrer with his contingent fee, even though the Shoemakes had to pay another attorney a separate contingent fee to fix the results of Ferrer's negligence. Thus the Shoemakes contended that the trial court awarded them insufficient attorney fees. Ferrer contended that the trial court should not have awarded the Shoemakes any attorney fees in the first place. The appellate court reversed the trial court's award of attorney fees because it found that a breach of fiduciary duty was not a recognized ground in equity allowing such an award by the trial court. However the appellate court did not subtract Ferrer's 40 percent contingency fee from the Shoemakes' award. Both Ferrer and the Shoemakes petitioned the Supreme Court of Washington on the issue of whether they could collect reasonable attorney fees in the malpractice action.

HOLDING: Affirmed.

REASONING: The court held that the crux of the case was whether a negligent attorney is entitled to have damages awarded to a successful malpractice plaintiff reduced by the amount of the negligent attorney's contingent fee. Ferrer argued that to not allow such a deduction would constitute a windfall for the plaintiff and subject negligent attorneys to a "unique punitive damages theory." The Shoemakes countered that deducting attorney fees from a legal malpractice award fails to fully compensate the plaintiffs because the very nature of malpractice requires plaintiffs to hire another attorney, and thereby pay additional legal fees in order to be made whole.

The court stated that the general rule is that the measure of damages for legal malpractice is the amount of actual loss sustained as a result of the negligent attorney's conduct. Thus, the goal of any legal malpractice damage award must be to place successful plaintiffs, as close as possible, to the position they would have occupied but for the attorney's malpractice. The court rejected the traditional American rule that clients should bear the burden of paying their own attorneys. In agreement with the appellate court, the court adopted the Restatement (Third) of the Law Governing Lawyers rationale and the modern majority rule that negligent attorneys are not entitled, by reason of equity and unjust enrichment, to be credited with fees that they failed to earn due to their malpractice. Furthermore, the court reasoned that reducing a successful malpractice plaintiff's damages by the negligent attorney's fee would fail in putting the injured plaintiff back in the position he or she would have been sans negligence.

WHETHER CONSUMER RELIED ON SELLER'S MISREPRESENTATION IS QUESTION FOR JURY

Bernstein v. Thomas, 298 S.W.3d 817 (Tex.App.—Dallas 2009)

FACTS: Home purchasers Matthew and Lindsay Thomas brought action against vendors Joshua and Jordana Bernstein, alleging violations of the Texas Deceptive Trade Practices Act. The Bernsteins put their house on the market with a disclosure notice attesting that they had never obtained any report regarding the foundation of the home. A few months later, they contacted a foundation repair company for an estimate after several prospective purchasers had mentioned sloping of the home's floor. The estimator felt that the house needed a significant amount of work. The Bernsteins then withdrew their original listing for the house and listed with a new agent, whose disclosure statement did not ask about any written report. In the disclosure statement, the Bernsteins indicated that they were aware of no defects or malfunctions in the foundation. The Thomases signed a purchase contract. They had the house inspected the next day, and the inspector's report remarked on the sloping and recommended consultation of specialists as a matter of course. Mr. Thomas took measurements with an optical level, and the Thomases purchased the house as scheduled. Several months later, the Thomases received a follow-up letter from the foundation repair company.

The Thomases brought suit alleging fraudulent inducement, common law fraud, fraud in a real estate transaction, breach of contract, and violations of the Texas Deceptive Trade Practices Act. The jury returned a verdict in favor of the Thomases on the DTPA claims. The court entered judgment in accordance with the jury verdict. The Bernsteins appealed.
HOLDING: Affirmed.
REASONING: The Bernsteins argued that the trial court erred in refusing to direct a verdict or to grant their motion notwithstanding the verdict because the professional inspection and independent measurements of the house negated the element of reliance as a matter of law. The Bernsteins relied on *Dubow v. Dragon*, in which the court concluded that buyers initiated a new, independent basis for purchase when they performed a careful inspection of the house and that the new basis superseded any wrongful act by the seller. The court distinguished the case before it because the Thomases did not expressly or exclusively rely on either their inspector or their own observations. Because there was no further negotiation of the purchase price subsequent to the inspection, the evidence indicated a reliance on the Bernsteins' representations. The court ruled that whether the Thomases relied on the Bernsteins' lack of disclosure and the Bernsteins' assurances that there was nothing wrong with the house was a question for the jury.

LAWYER SOLICITATION RULE IS UNCONSTITUTIONAL

McKinley v. Abbott, 2010 U.S. Dist. LEXIS 33499 (W.D. Tex. Mar. 25, 2010)

FACTS: Plaintiffs Donald McKinley and Christopher Villasana facially challenged the constitutionality of the recent amendments to Section 38.12(d) of the Texas Penal Code. The amendments prohibited telephone, in-person or written solicitations by chiropractors licensed to practice in Texas to accident victims within 30 days of an accident, and prohibited attorneys licensed in Texas from sending written solicitation to individuals who had been arrested or served with a summons within 30 days of an arrest or issuance of a summons. Plaintiffs sought a declaration that the amendments to Section 38.12(d) were facially unconstitutional, and an order to permanently enjoin the Texas Attorney General from enforcing the amendments.
HOLDING: Granted.
REASONING: The court held that the amendments regulate commercial speech, and were therefore scrutinized under the intermediate standard set forth in *Central Hudson Gas & Electric Corp. v. Public Service Commission of New York*. Under *Central Hudson*, states may regulate speech that is false, deceptive, misleading, or related to an unlawful activity. If a state wishes to regulate truthful and non-deceptive commercial speech, however, the state bears the burden of proving that its regulation directly and materially advances a substantial state interest and is "narrowly drawn."

Plaintiffs challenged Section 38.12(d)(2)(C) as to written solicitations made by attorneys to individuals recently arrested or served with a summons. The court noted that the Supreme Court case, *Florida Bar v. Went For It*, upheld a ban on solicitations through targeted, direct-mail advertisements to potential personal-injury or wrongful-death clients within 30 days of their accidents. However, the court stated that the Fourth Circuit case, *Ficker v. Curran*, distinguished *Went For It* when applied to solicitations made to criminal or traffic defendants. The court reasoned that the Supreme Court's holding in *Went For It* rested largely on the principle that the privacy of accident victims and potential wrongful-death clients deserves protection so to provide them a period to grieve before seeking redress for an emotional loss. The court held that persons recently arrested or served by a summons, however, do not possess the same need for privacy protection.

Ficker v. Curran held that a criminal defendant's need for a speedy trial and Sixth Amendment right to counsel, both warrant quick access to representation. The court found the Fourth Circuit's reasoning persuasive and proper to apply to the 30-day ban on attorneys' written solicitations to individuals arrested or served with a summons under Section 38.12(d)(2)(C). The court ruled that Section 38.12(d)(2)(C) neither directly or materially advanced a substantial state interest nor was it narrowly drawn under the *Central Hudson* test. Thus, the court concluded that it contravened the First Amendment to the United States Constitution and could not stand.

BANKRUPTCY COURTS CANNOT DECIDE STUDENT LOAN COSTS

In re Kirkland, 600 F.3d 310 (4th Cir. 2010)

FACTS: Lisa M. Kirkland borrowed money from Sallie Mae to finance her education between 1989 and 1995. After filing for Chapter 13 bankruptcy in 2001, Kirkland repaid the loans per her bankruptcy plan over five years. The Chapter 13 trustee misapplied the payments it received, overpaying two of Sallie Mae's nine claims and underpaying the final claim, which was guaranteed by Educational Credit Management Corp ("ECMC"). Instead of reallocating the overpayments to the final obligation, the Chapter 13 trustee refunded the payments directly to Kirkland. However, the error went unnoticed by ECMC until after Kirkland received her Chapter 13 discharge, at which point ECMC notified Kirkland of the outstanding debt via mail. ECMC filed suit to collect the outstanding debt obligation plus interest accrued during the life of the loan and collection costs. Finding that ECMC was negligent during the pendency of Kirkland's bankruptcy, the bankruptcy court found that it was not entitled to collection costs. ECMC then appealed to the district court, alleging that the bankruptcy court (and now the district court) lacked subject matter jurisdiction over the issue of awarding collection costs. The district court rejected these claims and affirmed the findings of the bankruptcy court. ECMC appealed to the 4th Circuit.
HOLDING: Reversed.

REASONING: The court reversed the district court's finding that the bankruptcy court had subject matter jurisdiction over whether to award collection costs to ECMC, and by proxy the bankruptcy court's finding that ECMC was not entitled to loan costs. Bankruptcy courts have jurisdiction over any claim that is a matter specifically described under Title 11, or a civil matter "arising in" or "related to" a bankruptcy petition. The claim must rely on a cause of action created by the bankruptcy code or be one that lacks existence outside the context of bankruptcy. Finding that ECMC's claim for collection costs and post-petition interest arose from language in its loan agreement with Kirkland, the court determined that contract law, not bankruptcy law, should have governed the issue of the costs. The court held that the claim for costs did not "affect an integral aspect of the bankruptcy process," and would have existed regardless of the bankruptcy petition. As such, the court ruled that the bankruptcy court did, indeed, lack subject matter jurisdiction.

STUDENT LOAN FOUND DISCHARGEABLE IN BANKRUPTCY

Walker v. Sallie Mae Servicing Corp., 2010 Bankr. LEXIS 932 (B.A.P. 8th Cir. Apr. 9, 2010)

FACTS: Debtor Michele D. Walker filed a Chapter 7 bankruptcy petition and received a discharge. Three years later, she filed an adversary proceeding seeking to discharge $300,000 in student loan debt for undue hardship under § 523(a)(8) of the Bankruptcy Code. In its Memorandum Opinion, the Bankruptcy Court made extensive findings as to the circumstances surrounding Walker's incurring the student loans, as well as her current family situation. Walker received a bachelor's degree, attended medical school in the hopes of becoming a psychiatrist, was unable to pass the boards and was dismissed from medical school. After working briefly as a pharmacy technician and substitute teacher, she entered a master's degree program in psychology and received her master's degree in school psychology. The Walkers have five children, including twin sons diagnosed with autism. Walker's autistic sons require extensive therapy sessions at home, at which Walker must be present. Walker must also be available to respond quickly during regular school hours to calls from school personnel, in case one of the boys has a "meltdown" at school. As a result, the family's income is limited to Walker's husband's work as a police officer and part-time security officer. The Bankruptcy Court found that requiring Walker to repay her loans would impose undue hardship on her and her dependents, and, therefore, the student loans were dischargeable. Creditor, Educational Credit Management Corporation ("ECMC") appealed.

HOLDING: Affirmed.

REASONING: Dischargeability of student loans is governed by § 523(a)(8), which provides, in relevant part, that a discharge under § 727 does not discharge an individual debtor from any debt for student loans, "unless excepting such debt from discharge under this paragraph would impose an undue hardship on the debtor and the debtor's dependents...." Thus, a debtor's obligation on a student loan remains until there has been an express determination that the loan is dischargeable because it imposes an undue hardship on the debtor and the debtor's dependents.

ECMC argued that the evidence did not support a finding of undue hardship. The court applied a totality-of-the-circumstances test in determining undue hardship under § 523(a)(8). Reviewing courts must consider the debtor's past, present, and reasonably reliable future financial resources, the debtor's reasonable and necessary living expenses, and "any other relevant facts and circumstances." The debtor has the burden of proving undue hardship by a preponderance of the evidence. If the debtor's reasonable future financial resources will sufficiently cover payment of the student loan debt-while still allowing for a minimal standard of living, then the debt should not be discharged.

A debtor's obligation on a student loan remains until there has been an express determination that the loan is dischargeable because it imposes an undue hardship on the debtor and the debtor's dependents.

ECMC asserted that the Bankruptcy Court erred in finding that two of the listed expenses were reasonable and necessary for Walker's support. Specifically, after Walker had received her discharge, her husband took out a second mortgage and used a portion of the proceeds to build a screened-in deck on their house. And, in 2007, Mr. Walker purchased a new vehicle, when he already owned three cars. Courts have held that in order to be reasonable and necessary under § 523(a)(8), an expense must be "modest and commensurate with the debtor's resources."

ECMC asserted that a new vehicle and large deck with combined payments of over $1,200 per month were not modest and commensurate in light of the Walkers' resources. In addition, ECMC correctly pointed out that the payment on the vehicle alone was greater than what Michele's payment would be under the Income Contingent Repayment Program. However, the uncontroverted evidence was that notwithstanding the payments for the new vehicle and the second mortgage, the Walkers' monthly expenses still exceeded their monthly income, and thus they were operating at a deficit.

The panel acknowledged that attempting to discharge a large amount of student loans, while enjoying a new vehicle and deck addition may seem troublesome to the casual observer, the reality of the Walkers' budget was that Walker could not afford to make any payments on her student loans and still maintain a minimal standard of living for herself and her family. That circumstance, based on the evidence offered, was highly likely to continue for many years, regardless of whether the Walkers were able to keep the house and vehicles or not. Therefore, the panel ruled that the Bankruptcy Court did not err in finding

the student loans to be dischargeable under § 523(a)(8) as an undue hardship on Walker and her dependents.

DEBTORS NOT ELIGIBLE FOR CH. 13 RELIEF

In re Pellegrino, 423 B.R. 586 (B.A.P. 1st Cir. 2010)

FACTS: Shortly after filing their Chapter 13 petition, debtors Jonathan and Carolyn Pellegrino ("Debtors") filed their bankruptcy plan ("Plan"). Debtors were below-median debtors with average monthly expenses exceeding their average monthly income. Chase Manhattan Mortgage ("Chase") held two secured claims against Debtors' residence. In the Plan, the Debtors proposed to make a one-time payment of $8,000 to be funded by an unsecured loan from a friend. Debtors also proposed making payments on the first mortgage directly to Chase in order to avoid the second mortgage.

The trustee filed an objection to the confirmation of Debtors' Plan, arguing that Debtors were not eligible to be debtors in a Chapter 13 proceeding. The trustee also filed a motion to dismiss Debtors' petition, also on the grounds that they were not eligible to be debtors in a Chapter 13 proceeding. The trustee argued that because Debtors' schedules reflected a monthly deficit, they did not meet the requirement that "only an individual with regular income… may be a debtor under Chapter 13 of this title" as specified in the Bankruptcy Code.

The bankruptcy court concluded that the Debtors do not have excess income from which to make the Plan payments and are therefore not eligible for Chapter 13 relief. Debtors appealed.
HOLDING: Affirmed.

REASONING: The Bankruptcy Code provides that "only an individual with regular income… may be a debtor under Chapter 13 of this title." Section 101(30) of the Bankruptcy Code states an "individual with regular income" is an "individual whose income is sufficiently stable and regular to enable such an individual to make payments under a plan under Chapter 13 of this title." The panel found the language of Section 101(30) contemplates that a Chapter 13 debtor will have disposable income from which to make plan payments.

The Bankruptcy Code neither defines income for eligibility purposes nor establishes when the eligibility determination should be made.

The Bankruptcy Code neither defines income for eligibility purposes nor establishes when the eligibility determination should be made. Debtors assert that the court should include contributions from a third party when assessing the sufficiency of the debtor's income for purposes of eligibility. The panel noted that although some courts recognize contributions from third parties as part of debtor's income, the test for regular income "is not the type or source of income, but rather its regularity and stability." In this case, the panel did not decide whether the loan proposed in Debtors' plan was income, because, even if it was treated as income, the proceeds from the loan were insufficient to provide payments to the creditors under the Plan's applicable commitment period. Thus, even if Debtors' $8,000 unsecured loan from a friend were considered to be "income," Debtors were still not eligible for Chapter 13 relief.