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How Consumer Bankruptcy Rulings Can Aid Ch. 11 Practice

By **Brian Shaw** (March 9, 2021, 2:48 PM EST)

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On Jan. 14, the U.S. Supreme Court handed down a unanimous opinion in Chicago, Illinois v. Fulton.[1] While Fulton arose out of a series of Chapter 13 cases in Chicago, commercial bankruptcy attorneys should not dismiss the decision's usefulness in Chapter 11 practice.

The city took possession of the individual debtor's vehicle prepetition pursuant to a city ordinance that provides for a possessory lien over the vehicle on account of unpaid parking fines. Chicago then refused to turn it over to the debtor once its Chapter 13 case was filed unless the debtor paid those past due — and prepetition — parking fines to the city.[2]

The debtors claimed that Chicago was violating the automatic stay, Section 362(a)(3) of the Bankruptcy Code, by retaining their vehicles until payment was made and the city responded that its inaction could not amount to the necessary affirmative act required to violate the automatic stay.[3] The Supreme Court agreed with the city.[4]

The heart of the Fulton issue, on a practical level, could not be more consumer oriented: Can a Chapter 13 debtor use bankruptcy to recover her vehicle — and mode of transportation to and from work — from the city without paying past due, prepetition fines?

So it is understandable that while many commercial practitioners were aware of the "Chicago parking dispute" and the Supreme Court's Fulton decision, many of the same practitioners never dug into the substance of the Fulton decision because of a conscious — or even subconscious — aversion to its consumer bent. That, as explained below, is a mistake.

The Bankruptcy Code: One Book, Many Chapters

The Bankruptcy Code is a comprehensive statutory scheme that sets out its provisions in nine chapters.[5]

While each chapter focuses on a particular topical area — i.e., Chapter 3, Case Administration or Chapter 11, Reorganization — they are not meant to be read or implemented in a vacuum and courts routinely turn to other chapters and sections of the Bankruptcy Code for interpretive help with statutory questions.

Examples of this interaction range from the obvious — such as Chapter 5 avoidance actions arising in cases under multiple chapters[6] — to the often used, but less remembered — such as a Chapter 11 liquidating plan governed by the priorities of distribution set forth in Section 726[7] — to the ignored — equally applicable case law arising out of consumer bankruptcy cases.

As such, it is important for commercial bankruptcy practitioners to understand the entire Bankruptcy Code and the case law interpreting it. You would not read and report on a classic novel by simply taking one chapter of it out of the context of the entire book, and you should not do so with the Bankruptcy Code either.

Prevalence of Consumer Case Law

Since 1996, consumer bankruptcy filings have accounted for no less than 96% of all petitions filed annually under the Bankruptcy Code.[8] That results in a lot of published consumer case law, much of which provides pertinent decisions and analysis that are as important in Chapter 11 as they are in Chapter 7.

Your bankruptcy judge, and quite possibly your opponent, will be aware of them and you should be, too. A recent example of one such case is the Fulton decision mentioned above.[9]

As noted above, Fulton involved Chapter 13 debtors and their ability to use Chapter 13 to recover their personal vehicles from the city of Chicago.[10]

The legal question decided by the Supreme Court was whether Chicago's continued post-petition possession of the vehicles, and resulting continued maintenance of its possessory lien on those vehicles, violated Section 362(a)(3).[11] The debtors argued it did. Chicago claimed it did not.

And the Supreme Court agreed with the City of Chicago, holding unanimously that the passive act of doing nothing — in this instance, not returning the vehicle — did not violate Section 362(a)(3) because the city's inaction did not disturb the petition-date status quo.[12]

But what if, instead of an individual, the debtor was a regional HVAC system supplier. And instead of a single Toyota Corolla, the impounded vehicles at issue were the majority of the debtor's service fleet that prodigiously accumulated Chicago parking tickets over the past several years.

Like the reorganizing Chapter 13 debtor, the Chapter 11 debtor also claims it needs its vehicles to successfully reorganize. The Chapter 11 debtor further notes that if it cannot obtain the immediate use of its service fleet, its business will fail and 75 employees will lose their jobs.

Would the Supreme Court's analysis of the issue be any different? It should not be, as both the law and the material facts — the impounded vehicles and Chicago's inaction — are the same. The result should be the same as it was in Fulton and the Chapter 11 debtor should lose.

Fulton Is Latest Example

Chicago v. Fulton does not stand alone in its relevance to commercial bankruptcy practice. Bankruptcy case law at the trial and appellate level is littered with consumer decisions that are often cited for legal principles in Chapter 11 cases without regard to their factual background.

One of the most prominent examples of such a case is the oft cited 2004 Supreme Court case of Till v. SCS Credit Corp.[13] in which the Supreme Court set forth a formulaic approach by which a court could determine the appropriate interest rate when a Chapter 13 debtor crammed down its plan of reorganization on one of its secured creditors.[14]

Specifically, in Till, which was decided under the cramdown provisions of Section 1325, the Supreme Court held that the prime plus or formula rate approach to determining the appropriate cramdown interest rate best comports with the purposes of the Bankruptcy Code and should be used to determine an appropriate interest rate to compensate the crammed down creditor for the time and risk being imposed upon it through a Chapter 13 plan of reorganization.[15]

The Till decision, in which the secured creditor's lien was on the joint, married debtors' truck that they had purchased for approximately $7,000, is an obvious consumer case. Yet, even a casual read of the opinion would alert counsel that the principles of law set forth by the Supreme Court in Till would likely be persuasive in a cramdown scenario under Chapter 11.

This is so because the plurality of the Supreme Court in the Till opinion noted the similarity between the cramdown provisions of Chapters 11 and 12 to the cramdown provision in Chapter 13 and surmised that Congress "likely intended bankruptcy judges and trustees to follow essentially the same approach ... under any of these provisions."[16]

Therefore, it is not surprising that, despite its consumer roots and the passage of 15 years since it

was handed down, Till is a recurring citation in commercial interest rate disputes, with its applicability being demanded by some parties and distinguished by others.[17]

Commercial practitioners who are familiar with both the substance and the background of the Till decision will undoubtedly be better prepared to make and present those arguments to a bankruptcy court equally familiar with the intricacies of Till.

Unlike Till, however, most consumer decisions that apply in a Chapter 11 context live in relative obscurity and need to be found. And they should be found because being unknown does not make them any less relevant or persuasive. A 1996 case from the U.S. Bankruptcy Court for the Western District of Texas, In re: Macias,[18] is an example of one such case.

Macias held that a secured creditor must file a proof of claim in order to receive distribution under a Chapter 13 plan.[19] In reaching its conclusion, the Macias court relied on the language of Section 502 and Rule 3021, as well as the language of Section 1326 that "commands the trustee to make payments to creditors under the plan."[20]

While not necessarily obvious at first blush, the Macias decision is easily applicable to Chapter 11 cases. Why? Because the language of Section 502 and Rule 3021 that was relied upon by the Macias court is equally applicable in Chapter 11 cases and limits distributions from the estate to holders of allowed claims.[21]

Unlike Till, Macias may not be at the tip of every bankruptcy practitioner's tongue, but it is no less relevant to the secured creditor's ability to protect its rights. Rather, it is just harder to find, and a fine example of why consumer decisions should not be overlooked by any bankruptcy practitioner.

Conclusion

There is a single Bankruptcy Code and a large body of case law interpreting it that both apply whether the debtor is an individual with consumer debt or a faltering business. Commercial bankruptcy practitioners should keep this in mind and when your Chapter 11 research comes up nil, consider looking at Chapter 7 or Chapter 13.

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[1] City of Chicago, Illinois v. Fulton et al., 592 U.S. ___ (2021).

[2] Id., at ___ (slip op., at 1).

[3] Id., at _____ (slip op., at 2).

[4] Id.

[5] See, 11 U.S.C. §§ 101 et seq.

[6] 11 U.S.C. §§ 544-549.

[7] 11 U.S.C. § 726

[8] Statista Research Department, January 20, 2021.

[9] 592 U.S. ___ (2021)

[10] Id.

[11] Id., at ___ (slip op., at 1)

[12] Id.

[13] Till v. SCS Credit Corp., 541 U.S. 465 (2004)

[14] Id., at 468-469.

[15] Id., at 479-480

[16] Id., at 474, fn 10.

[17] See, Momentive Performance Materials Inc. v. BOKF, NA 874 F.3d 787, 798-801 (2nd Cir. 2017).

[18] In re: Macias, 195 B.R. 659 (Bankr. W.D.Tex. 1996).

[19] Id.

[20] Id., at 660-661.

[21] See 11 U.S.C. § 502; Federal Rule of Bankruptcy Procedure 3021.
