No. 23-0115

IN THE SUPREME COURT OF THE UNITED STATES

IN RE EUGENE CLEGG, DEBTOR

VERA LYNN FLOYD, CHAPTER 7 TRUSTEE, PETITIONER

V.

EUGENE CLEGG, RESPONDENT

On Writ of Certiorari to the United States Court of Appeals for the Thirteenth Circuit

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BRIEF FOR PETITIONERS

Team 1
Counsel for Petitioner

QUESTIONS PRESENTED

I. Does post-petition, pre-conversion appreciation of estate property belong to the estate as is indicated by the Bankruptcy Code's unambiguous text?

II. Does section 541(a)'s expansive reach cover sections 547 and 550 causes of action, enabling the trustee to sell these property rights in accordance with its statutory duties?

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OPINIONS BELOW

The United States Bankruptcy Court for the District of Moot ruled for the Respondent on both issues. (R-4.) On direct appeal, the United States Court of Appeals for the Thirteenth Circuit affirmed both rulings (R-10–24).

STATEMENT OF JURISDICTION

The formal statement of jurisdiction is waived in accordance with the Rules of the Duberstein Bankruptcy Moot Court Competition.

STATEMENT OF FACTS

When Eugene Clegg (the "Debtor") filed his petition for Chapter 13 relief on December 8, 2021 (the "Petition Date"), his only relevant scheduled asset was a homestead valued at $350,000 and subject to a $320,000 mortgage. (R-6.) He claimed a $30,000 state law exemption, accounting for his total equity in the homestead as of filing. (*Id.*) The only unsecured claim scheduled was an unliquidated debt owed to Eclipse Credit Union ("Eclipse"), originally worth $850,000. (R-6., R-5.) Within one year prior to filing, the Debtor transferred $20,000 to his mother ("Pink"). (R-7.) Since the transfer was to an insider and occurred on the eve of bankruptcy, it is avoidable under section 547(b) of the Bankruptcy Code (the "Code").

On February 12, 2022, the Debtor's Chapter 13 plan was confirmed by the court. (R-8.) After making plan payments for eight months, unfortunate circumstances made it impossible for the Debtor to continue under the plan. (*Id.*) Faced with the threat of dismissal, the Debtor opted to convert his case to Chapter 7. (*Id.*) Between petition and conversion, the estimated value of the Debtor's homestead had appreciated by $100,000. (R-9.) At this point, the estate was otherwise "bereft of assets" and Eclipse was still owed $200,000. (*Id.*) Seeking recovery of the $100,000 in appreciation and the $20,000 transferred to Pink, Eclipse offered to purchase both the homestead and Trustee's § 547 and § 550 claims for a total of $470,000. (*Id.*) Vera Lynn Floyd, the Chapter 7 Trustee, moved to sell such property to Eclipse under § 363(b) (the "Sale Motion"), which was denied by the bankruptcy court. (*Id.*). On direct appeal, the Thirteenth Circuit affirmed the bankruptcy court's decision. (R-24).

SUMMARY OF THE ARGUMENT

The Thirteenth Circuit erred in granting the benefit of post-petition, pre-conversion appreciation to the debtor. By operation of Code sections 541(a) and 348(f)(1)(A), such appreciation must inure to the converted estate. Indeed, the estate's interest is in the equity of all estate property, reduced only by the claims of secured creditors and the debtor's claimed exemptions. This interest is unaffected by confirmation of the Chapter 13 plan and remains in effect through conversion. The increased equity to which the estate lays claim is not a separate, after-acquired property interest. Rather, it is an inseparable characteristic of the underlying property, which belongs to the estate from commencement onward. Policy implicated by the Code's operation should have no bearing on this result since the text is unambiguous.

As for the second issue, sections 547 and 550 claims fall within section 541(a)'s capacious definition of estate property. The Code and courts alike classify these sections as causes of action, and courts consistently find that causes of action are property of the estate. Specifically, section 541(a)(1) pertains to inchoate property interests that the estate obtains upon commencement, and section 541(a)(7), an all-embracing provision, pertains to interests the estate acquires after commencement. Both can house the section 547 preference claim and the section 550 claim for recovery. Moreover, with respect to section 550, this Court has previously expressed that section 541(a)(3) may also shelter such claims. And despite contention otherwise, the finding that these causes of action are estate property does not create surplusage, but rather the type of permissible redundancy that many statutes contain.

The trustee's prescribed duty under section 704(a)(1) encourages a Code reading that authorizes a trustee to sell Chapter 5 causes of action—subject to section 363(b) safeguards. And the benefits undergirding derivative actions and 363(b) sales in the Chapter 11 reorganization

context endorse allowing a trustee to sell these property interests in a Chapter 7 liquidation. Finally, to further cement these findings, the circuit courts that have expressly considered whether an avoidance action is property of the estate have found that they are. Thus, the Thirteenth Circuit erred in its ruling, warranting reversal by this Court.

I. THE THIRTEENTH CIRCUIT RULED IN ERROR BECAUSE ANY POST-PETITION, PRE-CONVERSION INCREASES TO THE VALUE OF DEBTOR PROPERTY MUST INURE TO THE CONVERTED ESTATE.

"The principal purpose of the Bankruptcy Code is to grant a 'fresh start' to the 'honest but unfortunate debtor.'" *Marrama v. Citizen's Bank*, 549 U.S. 365, 367 (2007) (quoting *Grogan v. Garner*, 498 U.S. 279, 287 (1991)). Traditionally, individual debtors seeking "a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt" may file a petition for bankruptcy under Chapter 7 or Chapter 13 of the Bankruptcy Code. *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934). In the proceeding that follows, this principal interest is balanced against the collective interests of the debtor's unsecured creditors. In service of creditors' interests, an estate comprised of "all legal and equitable interests of the debtor in property" is created upon commencement of a bankruptcy case. 11 U.S.C. § 541(a)(1). An appointed bankruptcy trustee will serve as "representative of the estate" and proxy for creditors' interests. 11 U.S.C. § 323(a). "The trustee is 'accountable for all property received,' §§ 704[(a)](2), 1106(a)(1), and has a duty to maximize the value of the estate[.]" *Commodity Futures Trading Com. v. Weintraub*, 471 U.S. 343, 352 (1985) (citing 11 U.S.C. § 704(a)(1)). In the archetypical bankruptcy proceeding—liquidation under Chapter 7—this means a "duty to collect and reduce to money property of the estate." *In re Edmonston*, 107 F.3d 74, 76 (1st Cir. 1997). Tension between this "general Code policy of maximizing the value of the bankruptcy estate," *Toibb v. Radloff*, 501 U.S. 157, 163 (1991), and the debtor's interest in a "fresh start"

underlies federal bankruptcy law. Thus, generally speaking, bankruptcy has no winners—debtors must part with their property while unsecured creditors forgo full repayment of their claims.

While bankruptcy necessarily involves compromise, both debtors and creditors can benefit from proceeding under Chapter 13 of the Code. "A wholly voluntary alternative to Chapter 7, Chapter 13 allows a debtor to retain his property if he proposes, and gains court confirmation of, a plan to repay his debts over a three- to five-year period." *Harris v. Viegelahn*, 575 U.S. 510, 514 (2015). After a Chapter 13 petition is filed, creditors are entitled to the debtor's disposable income until completion of the plan. 11 U.S.C. § 1325(b)(1). If a debtor completes their Chapter 13 plan, creditors can expect to recover more than they would have in a Chapter 7 liquidation. *Harris*, 575 U.S. at 514. Often, however, debtors fail to complete their Chapter 13 plan and must exercise the right to convert their case to Chapter 7 under Section 1307(a), lest the case be dismissed. When a case is converted, a Chapter 7 trustee will be "charged with liquidation of the estate as expeditiously as compatible with the interests of all parties concerned." *In re Lloyd*, 37 F.3d 271, 275 (7th Cir. 1994). This converted estate will consist of all "property of the estate, as of the date of filing of the petition, that remains in the possession of or is under the control of the debtor on the date of conversion[.]" 11 U.S.C. § 348(f)(1)(A).

Though a converted estate is comprised of the same property that was captured at filing, the value of certain assets may have changed during the failed Chapter 13 plan's term. The Code makes no indication that a change in value would have any effect on the estate's claim to all of the debtor's interests in property. *See* 11 U.S.C. §§ 501(a), 348(f)(1)(A). Yet, several courts have insisted that section 348(f)(1)(A), in conjunction with other Code provisions, limits the estate's interest to the debtor's equity as claimed on the petition date and that the debtor is entitled to any

post-petition appreciation. *See generally In re Barrera*, 620 B.R. 645 (Bankr. D. Colo. 2020) (*Barrera I)*; *Rodriguez v. Barrera (In re Barrera)*, 22 F.4th 1217 (10th Cir. 2022) (*Barrera II*); *Black v. Leavitt (In re Black)*, 609 B.R. 518 (B.A.P. 9th Cir. 2019); *In re Cofer*, 625 B.R. 194 (Bankr. D. Idaho 2021); *In re Hodges*, 518 B.R. 445 (Bankr. E.D. Tenn. 2014); *In re Nichols*, 319 B.R. 854 (Bankr. S.D. Ohio 2004); *In re Niles*, 342 B.R. 72 (Bankr. D. Ariz. 2006); *In re Slack*, 290 B.R. 282 (Bankr. D. N.J. 2003); *In re Wegner*, 243 B.R. 731 (Bankr. D. Neb. 2000). By and large, these courts claim to be vindicating some underlying congressional purpose—curiously left unexpressed within the text of the statute. Other courts have come to the opposite conclusion: that the Code expressly grants all pre-petition debtor property, including post-petition appreciation in such property, to the bankruptcy estate. *Castleman v. Burman (In re Castleman)*, 75 F.4th 1052 (9th Cir. 2023); *Potter v. Drewes (In re Potter)*, 228 B.R. 442 (B.A.P. 8th Cir. 1998); *In re Goetz*, 647 B.R. 412 (Bankr. W.D. Mo. 2022); *In re Goins*, 539 B.R. 510 (Bankr. E.D. Va. 2015); *In re Shipman*, 344 B.R. 493 (Bankr. W.D. W.Va. 2006); *In re Moyer*, 421 B.R. 587 (Bankr. S.D. Ga. 2007). This latter interpretation is correct and required by the clear, unambiguous language of sections 541(a) and 348(f)(1)(A).

By operation of the Code's express provisions, title to each item of debtor property is captured upon petition and remains in the estate until disposition or abandonment. The debtor's only claim to estate property is limited to the dollar amount of the applicable statutory exemption, if any. Therefore, the estate must benefit from any post-petition increase in equity when a case is converted from Chapter 13 to Chapter 7. Since this understanding does not conflict with other Code provisions or the general policies that underly the Code, the "inquiry must cease[.]" *Robinson v. Shell Oil Co.*, 519 U.S. 337, 340 (1997).

A. From petition onward, the estate holds title to all of the debtor's pre-petition assets and thereby benefits from any appreciation that might accrue.

Consistent with the creditors' interest in "maximizing the value of the bankruptcy estate," *Toibb*, 501 U.S. at 163, "the term 'property' has been construed most generously and an interest is not outside its reach because it is novel or contingent or because its enjoyment must be postponed." *Segal v. Rochelle*, 382 U.S. 375, 389 (1966). Congress adopted *Segal*'s capacious interpretation when it enacted the sweeping provisions of section 541(a)—

> "[The] estate is comprised of all of the following property, wherever located and by whomever held:
> (1) . . . all legal and equitable interests of the debtor in property as of the commencement of the case. . . . [and]
> (6) Proceeds, product, offspring, rents, or profits of or from the property of the estate, except as are earnings from services performed by the individual debtor after the commencement of the case."

11 U.S.C. § 541(a); *see also In re Barowsky*, 946 F.2d 1516, 1518 (10th Cir. 1991). Pursuant to section 541(a)(1), a debtor's bankruptcy petition automatically transfers all interests in property to the newly created estate without limitation. As the case ensues, existing estate property augments the estate with any proceeds it might generate. *Id.* § 541(a)(6). Indeed, section 541(a) provides only one notable exception to the estate's total capture of debtor assets: "property acquired post-petition by an *individual* debtor is usually not property of the estate." 5 *Collier on Bankruptcy* ¶ 541.02 (16th ed. 2022). "The debtor's interest in property includes 'title' to the property," so as of petition, the estate holds legal and equitable title to all assets formerly owned by the debtor. *Id.* ¶ 541.03 (citing *In re Mays*, 85 B.R. 995, 960 (Bankr. E.D. Pa. 1988)). Title remains with the estate until the underlying asset is disposed of by the trustee. *See* 11 U.S.C. § 554(d) ("[P]roperty of the estate that is not abandoned under this section and that is not administered in the case remains property of the estate."); § 350(a) ("After an estate is fully

administered . . . the court shall close the case.") Nuance involved in conversion from Chapter 13 to Chapter 7 does not affect this prescribed outcome.

i. By design, section 348(f)(1)(A) captures the debtor's pre-petition interests without reservation.

When a debtor files bankruptcy under Chapter 13, the estate includes, "in addition to the property specified in section 541 of this title . . . earnings from services performed by the debtor after the commencement of the case but before the case is closed, dismissed, or converted[.]" *Id.* § 1306(a). Expanding the already broad reach of section 541, these provisions maintain the profit-maximizing objective of the estate. After petitioning the court, "[t]he debtor shall file a plan," *Id.* § 1321, that pledges disposable future income to repay creditors (hence the inclusion of post-petition earnings). *Id.* § 1322(a). If the court determines that the plan adheres to all applicable Code provisions and was proposed in good faith, it will be confirmed. *Id.* § 1325(a).

"[C]onfirmation of a plan vests all of the property of the estate in the debtor," *Id.* § 1327(b), and "the debtor shall remain in possession of all property of the estate" for the remainder of the Chapter 13 proceeding. *Id.* § 1306(b). Such vesting and retention of estate property is necessary for success of the plan—which generally relies on the productive use and proceeds of the debtor's pre-petition assets. As in the present case, when a debtor fails to complete all plan payments, the debtor can exercise the right to convert the Chapter 13 case to Chapter 7. *Id.* § 1307(a).

> "[W]hen a case under Chapter 13 . . . is converted . . . property of the estate in the converted case shall consist of property of the estate, as of the date of filing of the petition, that remains in the possession of or is under the control of the debtor on the date of conversion."

Id. § 348(f)(1)(A). "Conversion . . . does not commence a new bankruptcy case. The existing case continues along another track . . . without 'effect[ing] a change in the date of the filing of

the petition.'" *Harris*, 575 U.S. at 515 (alteration in original) (quoting 11 U.S.C. § 348(a)). By maintaining reference to the original petition date, section 348 aligns with 1325(a)(4)'s policy—that unsecured creditors should recover, at a minimum, the estate's liquidation value as of commencement. *See* 11 U.S.C. § 1325(a) ("[T]he court shall confirm the [Chapter 13] plan if . . . the value . . . of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate . . . were liquidated under Chapter 7"); *see also In re Tanner*, 14 B.R. 933, 936 (Bankr. W.D. Pa. 1981). Hence, section 348(f)'s design is to bring the value of the converted estate as close to value of the original estate as possible. To this end, only transferred estate property and after-acquired property are off limits.

Transferred estate property does not "remain[ ] in the possession of . . . the debtor" and is beyond the trustee's reach. 11 U.S.C. § 348(f)(1)(A). After-acquired property is included in the Chapter 13 estate under section 1306(a)(1); such property is, however, excluded from the converted estate as it would be if the case had proceeded under Chapter 7 from inception. *See id.*§ 541(a)(6) (excluding after-acquired earnings from the estate). Just as creditor expectations are preserved at commencement, there Code is consistent in its treatment in debtors in a Chapter 7 case, converted or otherwise. *Harris*, 575 U.S. at 518 ("[N]othing in the Code denying debtors funds that would have been theirs had the case proceeded under Chapter 7 from the start.")

Section 348(f)(1)(A) attempts to recreate the original estate—composed of "all legal and equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a)(1). From commencement, the estate holds an equitable interest in "[p]roceeds, product, offspring, rents, or profits . *Id.* § 541(a)(6). This interest must survive conversion—it is necessary for effectuating the trustee's duty to "reduce to money and distribute the assets" in a

Chapter 7 case. *Van Huffel v. Harkelrode*, 284 U.S. 225, 228 (1931). "Money received from the sale of property constitutes the proceeds of that property; consequently, when a Chapter 7 trustee sells property of the estate, the trustee is entitled to any post-petition appreciation in the value of the property." *Shipman*, 344 B.R. at 494.

ii. Plan confirmation will vest estate property in the debtor but will not remove said property from the estate or diminish the estate's interest in proceeds thereof.

In a Chapter 13 case, there is palpable "tension between § 1327 on one hand and § 1306 and § 541(a)(6) on the other." *Black*, 609 B.R. at 526. The latter provisions include "property . . . that the debtor acquires after the commencement of the case" as well as "[p]roceeds" in the Chapter 13 estate. 11 U.S.C. §§ 1306(a)(1), 541(a)(6). However, "confirmation 'vests all property of the estate in the debtor,' and renders that property 'free and clear of any claim or interest of any creditor provided for by the plan.'" *Bullard v. Blue Hills Bank*, 575 U.S. 496, 502–03 (2015) (first quoting 11 U.S.C. § 1327(b); and then quoting 11 U.S.C. § 1327(c)). Faced with cases where a debtor sells pre-petition property during the pendency of their Chapter 13 plan, courts have had to square this conflict while deciding whether the debtor or estate is entitled to the sale's realized appreciation. See *Barrera I*, 620 B.R. at 645; *Barrera II*, 22 F.4th at 1217; *Black*, 609 B.R. at 518; *Niles*, 342 B.R. 72.

One such case, *In re Barrera*, bears heavily on the Thirteenth Circuit's present ruling. (R-16.) Yet, the timing of events in that case render it incompatible with the case at bar. In *Barrera*, the debtors sold their home prior to conversion of their Chapter 13 case, receiving proceeds in excess of the lien and claimed exemption thereon. *Barrera I*, 620 B.R. at 647. On review of this case, the Tenth Circuit explained that "[t]he physical house was not 'in possession of or . . . under the control of the [D]ebtor[s] on the date of conversion'—they had sold it." *Barrera II*, 22

F.4th at 1223 (second and third alterations in original) (quoting 11 U.S.C. § 348(f)(1)(A)). The court added that "the proceeds from the sale did not exist on the date of filing the Chapter 13 petition, so the proceeds cannot have "*remain[ed]* in the possession of or [have been] under the control of the debtor on the date of conversion[.]'" *Id*. (alterations in original) (quoting 11 U.S.C. § 348(f)(1)(A)). To rebut the estate's fundamental claim to "proceeds . . . of or from property of the estate," the Tenth Circuit decided that section 541(a)(6) "is operative only before confirmation of the Chapter 13 plan because confirmation 'vests all property of the estate in the debtor.'" *Id.* (quoting 11 U.S.C. § 1327(b)). Adopting reasoning from *In re Niles*, the Tenth Circuit concluded that "proceeds generated from the debtor's property after confirmation do not become property of the estate as the underlying property no longer belongs to the estate." *Id. In re Barrera*, like *In re Niles*, is "premised on the mistaken belief that revesting under § 1327(b) transforms property of the estate into property of the debtor." *In re Aneiro*, 72 B.R. 424, 428–29 (Bankr. S.D. Cal. 1987); *see also Niles*, 342 B.R. at 75 ("[T]he intervening plan confirmation fundamentally changes the 'property of the estate' landscape.") Ignoring for a moment the fallacy of this premise, it is clearly not applicable to the case at bar, in which the relevant property was not sold prior to conversion and is undoubtedly included in the converted estate by section 348(f)(1)(A).

In re Cofer illustrates how the aforementioned premise cannot be rationally applied when, as in the present case, the debtor retains the relevant property through conversion. In *Cofer*, the debtor claimed that plan confirmation "vested absolute ownership of the [h]ome . . . [which] ceased to be property of the estate." *Cofer*, 625 B.R. at 196. Recognizing that so "interpreting § 1327(b)–(c) as preventing the operation of § 348(f)(1)(A) on conversion would create an inconsistency in the code[,]" the court declined to accept this theory. *Id.* at 197. Instead,

the court found the sections to be reconcilable, stating that "a debtor is vested with property of the Chapter 13 estate upon plan confirmation, but upon conversion, any such property . . . that a debtor still possesses or controls (*i.e.*, has not already exercised rights to sell the property) is recaptured into the Chapter 7 estate." *Id*. In any case concerning "property . . . that remains in the possession of or is under the control of the debtor on the date of conversion[,]" 11 U.S.C. § 348(f)(1)(A), this reading is the only operable interpretation of the interplay between sections 1357 and 348(f). *Barrera* and the like should not be applied.

Even in cases involving pre-conversion sale, it is uncertain whether a debtor could be entitled to any appreciation realized since the estate would have maintained an interest in the property through confirmation. Section 1327(c) leaves property "free and clear" of creditor claims, but the estate's claim remains. Indeed, section 1327(b) refers to such property as "property of the estate" and gives no indication that such property is free and clear of its interest. Though some courts have insisted that plan confirmation amounts to "estate termination," *see Black*, 609 B.R. at 529 (citing *In re Jones*, 420 B.R. 506, 514 (B.A P. 9th Cir. 2009)), "[b]y stating that the bankruptcy estate continues to be replenished post-petition property[,] . . . section 1306(a) is actually providing for the continued existence of the bankruptcy estate[.]" *Barbosa v. Soloman*, 235 F.3d 31, 36 (5th Cir. 2000). The estate's interest survives throughout a Chapter 13 case "in spite of the 'vesting' . . . [because] until all payments due under the plan are made, both the trustee and the unsecured creditors have an interest in the preservation of the debtor's financial situation[.]" *Id.* at 37 (quoting 11 U.S.C. § 1327). Thus, "[s]ection 1327 does not remove property . . . from the bankruptcy estate but merely places control of this estate property in the debtor pending conclusion of the Chapter 13 proceedings." *In re Brensing*, 337 B.R. 376, 383 (Bankr. D. Kan. 2006). Based on this understanding, "the Trustee is entitled to post-petition

appreciation . . . because the real estate was *always* property of the estate[.]" *Goins*, 539 B.R. at 515.

The Code's plain language and underlying policy compels this result. Value maximization is the bankruptcy estate's *raison d'être*. Accordingly, sections 348(f) and 541(a)—which collect all value for the estate—must take a capacious view of estate property, which naturally includes appreciation. Congress, sympathetic to the debtor's interest in a "fresh start," tempers the trustee's broad reach by excluding after-acquired property and exemptions from estate acquisition. *See* 11 U.S.C. §§ 541(a)(6), 522(b). Operation of these provisions by their explicit terms effects a balance between the adverse interests of debtor and creditor, to the extent desired by Congress.

B. A debtor's interest in estate property is limited to the dollar amount of any claimed exemption; all unencumbered value in excess thereof must inure to the estate.

Put simply, a bankruptcy case is the adjudication of competing claims to a debtor's assets. At the outset of bankruptcy, such claims and assets are valued and accounted for. *See e.g.,* § 522(b)(1). Debtors, like secured creditors, may lay claim to a portion of the value contained in certain property, placing it beyond the grasp of competing claimants. "A secured creditor has a constitutional right to preserve the value of its secured claim on the petition date." *In re Helder Industries, Inc.*, 131 B.R. 578, 586 (Bankr. D. N.J. 1991) (citing *Wright v. Union Cent. Life Ins. Co.*, 311 U.S. 273, 278 (1940)). Similarly, debtors are accorded the right to exempt certain property value up to a specified dollar amount. 11 U.S.C. § 522(b)(1). The Code sets forth a selection of available federal exemptions in section 522(d) and sanctions alternative state-law exemptions in section 522(b)(3)(A). Exemptions are capped at the dollar amount specified by section 522(d) or its relevant state law analogue. Caps reflect a policy judgment: the dollar value

assigned to each exemption indicates the extent to which Congress (or a state legislature) favors the debtor's interests over the interests of unsecured creditors. Any "portion of the debtor's interest . . . which exceeds the specified [exemption] value cannot be exempt; indeed, to conclude otherwise would render meaningless the value limitations[.]" *In re Gaylor*, 123 B.R. 236, 238 (Bankr. E.D. Mich. 1991).

i. Debtors and secured creditors may hold fixed interests in estate property, but the underlying assets and equitable right to proceeds remain vested in the estate.

An allowed exemption will guarantee to the debtor a portion of the equity in a given asset of the estate. It is not, however, an equity interest entitled to benefit from appreciation, as demonstrated by *In re Hyman*: There, debtors "argue[d] that they're entitled at least to the part of the appreciation that stands in the same proportion to the total appreciation as their homestead exemption stands to the value of their home." 967 F.2d 1316, 1321 (9th Cir. 1992). The court rejected this assertion, ruling that "[t]he California [exemption] statute gives the Hymans a[n] . . . exemption as of the time of sale, not a[n] . . . equity interest in the property." *Id*. It follows that an exemption "is merely a debtor's right to retain a certain sum of money when the court orders sale of [property.]" *In re Reed*, 940 F.2d 1317, 1321 (9th Cir. 1991). "[U]ntil abandonment occurs the property and any equity in it belong to the estate." *In re Paolella*, 85 B.R. 974, 978 (Bankr. E.D. Pa. 1988).

The estate's residual claim to value in excess of allowed liens and exemptions, including appreciation, is implied by its right to "proceeds . . . of or from property of the estate." *Reed*, 940 F.2d at 1323 (quoting 11 U.S.C. § 541(a)(6)). "The fact that proceeds . . . are included in the estate means that when property of the estate is sold, whatever consideration is received belongs to the estate subject to the debtor's potential exemption rights under 11 U.S.C. § 522." *Paolella*,

85 B.R. at 977. This Court has endorsed this framework by defining "the 'property claimed as exempt' as an 'interest' in [the debtor's] [asset], *not* as the [asset itself] *per se*." *In re Orton*, 687 F.3d 612, 615 (3d Cir. 2012) (alterations in original) (quoting *Schwab v. Reilly*, 560 U.S. 770, 783 (2010)). "Nothing . . . [however,] suggests that the estate's interest is anything less than the entire asset, including any changes in its value[.]" *Potter*, 228 B.R. at 424. Thus, "if equity has been created it belongs to the estate." *Paolella*, 85 B.R. at 978.

ii. Valuation fixes secured claims and exemptions, not the equitable right to proceeds, which fluctuates over time.

"[W]hatever rights a debtor has in property at the commencement of the case continue in bankruptcy—no more, no less." *Moody v. Amoco Oil Co.*, 734 F.2d 1200, 1213 (7th Cir. 1984). In keeping with this principle, secured claims and "exemptions are determined on the date of the bankruptcy and without reference to subsequent changes in the character or value of the exempt property." *In re Chappell*, 373 B.R. 73, 77 (B.A.P. 9th Cir. 2007) (citing *In re Chiu*, 266 B.R. 743, 751 (B.A.P. 9th Cir. 2001), *aff'd*, 304 F.3d 905 (9th Cir. 2002)). Indeed, this "snapshot rule," first articulated by this Court in *White v. Stump*, is now settled bankruptcy law. 266 U.S. 310, 313 (1924) ("When the law speaks of . . . rights to exemptions it of course refers to some point of time. In our opinion this point of time is the one as of which the general estate passes out of the bankrupt's control, and with respect to which the status and rights of the bankrupt . . . are fixed.") From this premise, a number of courts have contrived the idea that the estate's interest is also fixed at commencement, based on a theory that "an order confirming a chapter 13 plan is an implicit valuation of the scheduled property." *Warren v. Peterson*, 298 B.R. 322, 325 (N.D. Ill. 2003); *see also Niles*, 342 B.R. at 72; *Slack*, 290 B.R. at 282; *In re Page*, 250 B.R. 465 (Bankr. D. N.H. 2000); *In re Kuhlman*, 254 B.R. 755 (Bankr. N.D. Cal. 2000). Yet, the amended section 348(f) states that "valuations of property and of allowed secured claims in the Chapter 13 case

shall apply only in a case converted to a case under chapter 11 or 12, *but not in a case converted to a case under chapter 7*[.]" 11 U.S.C. § 348(f)(1)(B) (emphasis added). Therefore, the "implicit valuation" theory cannot apply to a case, like the one at bar, which is converted to Chapter 7. *Goetz*, 647 B.R. at 417. Therefore, "what is frozen as of the date of filing the petition is the value of the debtor's exemption, not the fair market value of the property claimed as exempt." *In re Gebhart*, 621 F.3d 1206, 1211 (9th Cir. 2010). The estate's claim to all residual value vests "regardless of whether there was equity beyond liens and exemptions when the case was filed." *In re Peter*, 309 B.R. 792, 794 (Bankr. D. Or. 2004) (citing *In re Vu*, 245 B.R. 644, 649 (B.A.P. 9th Cir. 2000)).

iii. Fixing the value of the estate's interest, rather than the debtor's, produces results incompatible with the Code.

Adverse authority reasons that "it is not illogical to assume that Congress intended to freeze the estate's rights in the debtor's prepetition assets at their prepetition values." *Barrera I*, 620 B.R. at 652. While perhaps "not illogical" in theory, this interpretation is not workable in practice. As the following cases demonstrate, if the estate's claim were fixed at commencement, absurd results would follow.

In *Shipman*, debtors were years into their Chapter 13 case when they moved to purchase their homestead for the scheduled price of $126,900. *Shipman*, 344 B.R. at 494. Though the property had since appreciated to a fair market value of approximately $288,500, debtors insisted that they owned such appreciation because the estate's interest was limited by the initial valuation. *Id.* In the Court's view, compelling the trustee to dispose of estate property for substantially less than fair market value would fly in the face of the Code's express provisions. Such an order would not only deny the estate its entitlement to proceeds under section 541(a)(6) but would also impede the duties of trustee and court vis-à-vis sale of estate property. *Id.* at 494–

95. Per section 363(b), "[t]he trustee . . . may . . . sell . . . property of the estate[,]" subject to the business judgment rule, which imposes "[t]he court's obligation . . . to assure that optimal value is realized by the estate[.]" *In re Lahijani*, 325 B.R. 282, 288 (B.A.P. 9th Cir. 2005). Clearly, the trustee's duty to exercise sound business judgment, as well as the court's duty to evaluate such judgment, would be severely compromised by a rule that fixes the estate's interest with reference to initial valuations. The *Shipman* court rightly denounces this absurd outcome, ruling that "post-petition appreciation of property of the estate enures to the benefit of the Trustee." *Shipman*, 344 B.R. at 495.

The Hyman court identifies another potential absurdity: if debtors benefit from appreciation of estate property, they must likewise suffer depreciation. *Hyman*, 967 F.2d at 1321. If this were the case, a significant loss in property value could swallow up a debtor's claimed exemption in such property, which ought to be guaranteed. *Id.* "Nothing in the bankruptcy law compels (or even suggests) such a drastic interference with the operation of the . . . exemption statute." *Id.* As these cases illuminate, entitling debtors, rather than the estate, to equity and appreciation cannot be reconciled with the Code, when viewed in its totality.

C. Value is an intangible characteristic of property, not a separate, after-acquired property interest.

"As written, § 348(f) only clarifie[s] that newly-acquired, post-petition property would not become part of the converted estate if the debtor had been acting in good faith." *Castleman*, 75 F.4th at 1057–58. The exclusion of after-acquired property by "subsection (f)(1)(A) is elucidated by comparing it to subsection (f)(2)." *Barrera I*, 620 B.R. at 648. This subsection punishes debtors who convert in bad faith by including "property of the estate as of the date of conversion" in the converted estate. 11 U.S.C. § 348(f)(2). "Absent a bad faith conversion, § 348(f) limits a converted Chapter 7 estate to property belonging to the debtor 'as of the date' the

original Chapter 13 petition was filed." *Harris*, 575 U.S. at 517. This restriction does not mean, as Respondent urges, that the converted estate is limited to property "as it existed on the Chapter 13 petition date, with all its attributes, including the amount of equity *that existed on that date*." *Barrera II*, 22 F.4th at 1222. Rather, the estate "captures the debtor's entire ownership interest in each asset that exist[ed] on the petition date without fixing the estate's interest to the precise characteristics the asset ha[d] on that date." *Goetz*, 647 B.R. at 416. Thus, "equity attributable to the post-petition appreciation of the property is not separate, after-acquired property[.]" *Goins*, 539 B.R. at 516.

i. Equity is inseparable from underlying estate assets.

Treating equity as a separate asset "confuses the value of estate property with the legal or equitable interests in that property, as of the commencement of the case." *In re Adams*, 641 B.R. 147, 151 (Bankr. W.D. Mich. 2022). This Court's reasoning in *Crane* ought to dispel confusion: "'property' is the physical thing which is a subject of ownership, or . . . the aggregate of the owner's rights to control and dispose of that thing[;]" in contrast, "'equity' is defined as 'the value of a property above the total of the liens.'" *Crane v. Comm'r of Internal Revenue*, 331 U.S. 1, 6 (1947). "'Equity' is not . . . a synonym [of 'property'], nor do either of the foregoing definitions suggest that it could be correctly so used." *Id.*; *see also Equity*, BLACK'S LAW DICTIONARY (11th ed. 2019). "As this definition illustrates, equity is not a separate item of property; it exists only with reference to and as a characteristic of an underlying asset." *Goetz*, 647 B.R. at 416. Equity can manifest as tangible property only insofar as it is realized upon sale of the underlying asset. Sale converts equity into "proceeds" belonging to the estate per section 541(a)(6). "Because sale does not generally, if ever, occur simultaneously with formation of the bankruptcy estate, § 541(a)(6) mandates that the estate receive the value of the property at the

time of the sale. This value may include appreciation or be enhanced by other circumstances creating equity which occur postpetition." *Paolella*, 85 B.R. at 977 (citing *In re Clark*, 711 F.2d 21, 23 (3d Cir. 1983)). With respect to post-petition proceeds, section 541(a)(6) excludes only "earnings from services performed by an individual debtor after commencement of the case." "A change in the value of an asset does not fall within the purview of 'earnings from services performed by an individual debtor[.]'" *Potter*, 228 B.R. at 424; *see also Moyer*, 421 B.R. at 587 (rejecting a debtor's claim that appreciation in stock value represented earnings from services.)

In sum, "equity cannot be a separate item of after-acquired property that the Bankruptcy Code excludes from the converted estate under [its] plain language[.]" *Goetz*, 647 B.R. at 416. Indeed, even *Niles*, which puts forth a leading argument for the opposite conclusion, admits that "an increase in value to real property is not the same as after-acquired property as that term is traditionally defined under bankruptcy law[.]" *Niles*, 342 B.R. at 75. Despite this recognition, *Niles* and its progeny take the alternate course, guided by policy considerations alone.

D. Policy considerations aside, all equity generated postpetition inures to the estate under the Code's plain meaning.

As detailed above, the Code unambiguously requires "that appreciation inures to the estate, not the debtor." *Reed*, 940 F.2d at 1323. Fearing that this outcome might "create a serious disincentive to chapter 13 filings[,]" certain courts have turned to legislative history in search of support for an alternative interpretation. *Niles*, 342 B.R. at 75. Legislative history does indeed suggest that "Congress did not intend that a chapter 13 debtor should lose the benefit of any equity accrued in an asset because of said debtor's compliance with the chapter 13 plan payments." *Nichols*, 319 B.R. at 857; *see* H.R. Rep. No. 103-835, at 57 (1994). It is worth noting that this argument only applies to "increases in equity produced by payments made as part of Chapter 13 plans." *Hodges*, 518 B.R. at 449. It does not apply more broadly to exclude all

appreciation. Moreover, the Code's unambiguous language does not justify a resort to legislative history in any circumstances.

As written, the Code clearly provides that a "[d]ebtor is not entitled to the appreciation in his property that accrued during the course of his Chapter 13 case." *Goins*, 539 B.R. at 516. "Such value may come not only from an increase in the property's value, but also from pay-down of liens." *Peter*, 309 B.R. at 793. This is because "[s]ection 348 does not explicitly protect an equity cushion that is created by payments made during the pendency of the Ch. 13 case." *Wegner*, 243 B.R. at 735. If Congress does, in fact, wish to protect the debtor's equity beyond the extent of exemptions, it must amend the Code to so provide. Until that point, bankruptcy courts must simply apply the Code as written. *Law v. Siegel*, 571 U.S. 415, 420 (2014) ("[A] bankruptcy court may not contravene specific statutory provisions.")

II. THE TRUSTEE CAN TRANSFER § 547 AND §550 CLAIMS BECAUSE THEY ARE PROPERTY OF THE ESTATE.

Generally speaking, upon the debtor's initiation of bankruptcy proceedings, § 547(b) grants the trustee the ability to avoid of any preferential transfer to a creditor made within 90 days of the petition (or in the case of an insider, within one year). 11 U.S.C. § 547(b). Therefore, upon commencement, the trustee is authorized to claw back that preferential transfer. After doing so, the trustee may recover the value of the avoided transfer under § 550(a).

Here, the disputed issue is whether the trustee can sell those § 547(b) and § 550(a) actions as property of the estate. Chapter 5 of the Bankruptcy Code details several avoidance actions—claims that unwind a debtor's prior transfer to a creditor. E.g., 11 U.S.C. §§ 544; 545, 547, 548, 549, 553(b). These claims include both fraudulent transfers and preferential transfers. *In re Simply Essentials, LLC*, 78 F.4th 1006, 1008 (8th Cir. 2023).

Under the Bankruptcy Code and caselaw alike, avoidance actions[1] are unquestionably classified as causes of action. E.g., 11 U.S.C. § 926 (characterizing sections 544, 545, 547, 548, and 549(a), and 550 as "causes[s] of action"); *Simply Essentials*, 78 F.4th at 1008 ("Avoidance actions, of course, are causes of action."); *see also Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33, 53 (1989) (announcing 11 U.S.C. § 548(a)(2), an avoidance claim for fraudulent conveyance, as "a statutory cause of action.").

Given an avoidance claim's designation as a cause of action, this Court should find that § 547 fits squarely within § 541(a)'s expansive definition of property of the estate. Similarly, in keeping with this Court's prior opinions, this Court should find that the § 550 right to recovery is also estate property. *See United States v. Nordic Vill., Inc*., 503 U.S. 30, 37 (1992) (illustrating "the right to recover . . . under § 550" as a "claim" and "property of the estate).

To effectuate the trustee's statutory duties, this Court should find that a trustee is allowed to transfer its § 547 and § 550 claims. Courts' consistent approach to derivative actions and Chapter 11's treatment of avoidance actions also support this approach as does the mass of caselaw on Petitioner's side.

A. As causes of action, §§ 547 and 550 fall within § 541's broad parameters.

This Court has consistently interpreted § 541(a) to be inclusive. E.g., *United States v. Whiting Pools, Inc.*, 462 U.S. 198, 204–05 (1983) ("Congress intended a broad range of property [under § 541(a)] to be included in the estate." (citing H.R. Rep. No. 95-595, at 367 (1977))). In particular, the Bankruptcy Code defines "property of the [debtor's] estate" as including "all legal

[1] Note that, technically speaking, § 550 may not be an "avoidance action." *See In re AVI, Inc.*, 389 B.R. 721, 734 (B.A.P. 9th Cir. 2008) ("[A]voidance is a necessary precondition to any recovery under § 550."). The distinction does not affect Petitioner's arguments and because avoidance is necessary to effectuate § 550, this Court may nonetheless consider it an "avoidance action."

or equitable interests of the debtor in property as of the commencement of the case" and "[a]ny interest in property that the estate acquires after the commencement of the case." 11 U.S.C. § 541(a)(1), (7).

Courts have consistently stated that the Code captures causes of action as estate property. E.g., *Combs v. Cordish Cos.*, 862 F.3d 671, 679 (8th Cir. 2017) ("The property of a Chapter 7 estate includes 'all legal or equitable interests of the debtor in property as of the commencement of the case,' *including causes of action*" (citing *In re Senior Cottages of Am., LLC*, 482 F.3d 997, 1001 (8th Cir. 2007))) (emphasis added); *In re O'Dowd*, 233 F.3d 197, 202 (3d Cir. 2000) (signaling that property of the debtor's estate "include[es] tangible or intangible property, [and] *causes of action*" (quoting H.R. Rep. No. 95–595, at 367 (1977))) (emphasis added); *In re Salander*, 450 B.R. 37, 45 (Bankr. S.D.N.Y. 2011) ("'Property of the estate' includes all causes of action that the debtor had a right to bring at the time the bankruptcy was filed, including causes of action that the debtor was not aware of prior to the bankruptcy filing.").

Furthermore, the Code and courts alike have stated that Chapter 5 avoidance actions are causes of action. *See e.g.*, 11. U.S.C. § 926(a) (denoting that both §§ 547 and 550 are "cause[s] of action"); *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33, 53 (1989) (classifying § 548(a)(2), an avoidance action for a fraudulent conveyance, as a "statutory cause of action"); *In re Sweetwater*, 884 F.2d 1323, 1327 (10th Cir. 1989) ("[A]voidance claims are also claims of the estate. A claim is defined by § 101(4) as a 'right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured . . . .' This broad definition includes the estate's right to payment under §§ 547, 549 and 553."); *In re Racing Servs., Inc.*, 540 F.3d 892, 896 (8th Cir. 2008) (observing that sections 547 and 548 are "avoidance claims"); (*In re Action*

Foodservices Corp., 39 B.R. 70 (Bankr. D. Mass. 1984) (indicating that a cause of action for fraudulent transfer would be estate property); *see also Nordic Vill.*, 530 U.S. at 37 (intimating that section 550 is property of the estate because it "is clearly a 'claim' (defined in § 101(4)(A)) and is 'property of the estate' (defined in § 541(a)(3))"). Property of the estate includes causes of action and avoidance actions are causes of action. It follows that avoidance actions are transferable property of the estate.

Some courts attempt to delineate between avoidance actions and other types of claims by characterizing them as "powers" the trustee possesses. *See In re McGuirk*, 414 B.R. 878, 879, (Bankr. N.D. Ga. 2009). These courts interpret the powers the Code delegates to the trustee as distinct from the estate. (R-19.); *see also* § 11 U.S.C. § 546(b)(1) (referencing "[t]he rights and powers of a trustee under sections 544, 545, and 549"). Notwithstanding this nomenclature, there is no evidence that Congress used "powers" in an effort to exclude such claims from the estate. Moreover, courts routinely find these "powers" to be estate property, suggesting that powers themselves can be property interests. *See In re Guillot*, 250 B.R. 570, 599 (Bankr. M.D. La. 2000) ("The only way to interpret the 'rights and powers' clause of § 544(a) is as a statute that creates a property interest.")

Similarly, 11 U.S.C. § 541(b), which excludes from the estate "any power that the debtor may exercise solely for the benefit of an entity other than the debtor[,]" demonstrates that Congress knows how to exclude a "power." Because Congress did not exclude any of the trustee's avoidance powers in § 541(b), this Court should find that Chapter 5 claims are property interests of the estate. What is left for this Court to decide is where within § 541(a) these claims fall—either § 541(a)(1) or § 541(a)(7) provides harbor for these claims.

B. The large scope of § 541(a)'s text indicates that avoidance claims are property of the estate, either upon bankruptcy's commencement or acquired thereafter.

In relevant part, 11 U.S.C. § 541(a)(1) states that "property of the estate" encompasses "all legal or equitable interests of the debtor in property as of the commencement to the case." *See Secs. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Secs.*, *LLC*, 460 B.R. 106, 114 (Bankr. S.D.N.Y. 2011) ("The term 'all legal and equitable interests of the debtor in property' is all-encompassing and includes rights of action as bestowed by either federal or state law." (quoting *In re Moore*, 608 F.3d 253, 257–58 (5th Cir. 2010))). This Court has explained that the estate also captures "property in which the debtor did not have a possessory interest at the time bankruptcy proceedings commenced." *Whiting Pools*, 503 U.S. at 37. Indeed, "[P]roperty of the estate includes inchoate or contingent interests held by the debtor prior to the filing of bankruptcy." *Segal*, 382 U.S. at 379; *see also In re Prudential Lines, Inc.*, 928 F.2d 565, 571 (2d Cir. 1991) (examining *Segal* and finding that Congress agreed with the result, as evidenced by the legislative history behind § 541).

In a bankruptcy case, a debtor possesses an equitable interest in the avoidable transfer. *See N.L.R.B. v. Martin Arsham Sewing Co.*, 873 F.2d 884, 887 (6th Cir. 1989) ("Any effort to recover [an avoidable transfer] is essentially an action to recover property that belongs to the debtor."); *In re MortgageAmerica Corp.*, 714 F.2d 1266, 1275 (5th Cir. 1983); *see also In re Rine & Rine Auctioneers, Inc.*, 74 F.3d 854, 861 (8th Cir. 1996) (referencing authority that "h[eld] that the debtor had an equitable interest in money transferred, for purposes of applying § 547(b)"). A related occurrence exists in trust law, where courts find that contingent beneficiaries have property interests. *See e.g.*, *Giagnorio v. Emmett C. Torkelson Trust*, 686 N.E. 42, 45–46 (Ill. App. Ct. 1997) (explaining that an "indirectly identified" beneficiary "has an interest in the Trust property, despite the fact that said interest is contingent and may not vest in possession").

i. Because the debtor has an inchoate interest in the preferential transfer and the right to file for bankruptcy, a § 547 claim becomes property of the estate when the bankruptcy case commences under §541(a)(1).

The only circuit court (Eighth Circuit) to specifically address whether a § 547 avoidance action falls within the scope of § 541(a)(1) found that it did. *Simply Essentials*, 78 F.4th at 1009. In *Simply Essentials*, the Chapter 7 trustee decided to sell avoidance actions that it did not have sufficient funds to pursue. In return, the creditor-purchaser would assume all incidental costs, reduce its claims against the estate, and provide the estate with the first $600,000 recovered and 15% of additional recoveries, after deducting costs and fees incurred. In assessing whether the avoidance actions were property of the estate, the Eighth Circuit emphasized that avoidance actions were causes of action that fit within the broad nature of the estate as described by this Court to include "inchoate or contingent interests held by the debtor prior to the filing of bankruptcy." *Id.* at 1008–09 (citing *Segal*, 382 U.S. at 379). In addition, the court explained that "[a]voidance actions are used to undo transfers made by the debtor prior to the commencement of bankruptcy that were made voidable by the Bankruptcy Code." *Id.* at 1009. The court found that because the transfer could be avoided and recovered, the debtor possessed an inchoate interest in the actions prior to bankruptcy under § 541(a)(1). *Id.*

The Thirteenth Circuit misapprehends the far-reaching nature of § 541(a) by carving out avoidance actions and saying that no claim that exists until the case is filed. (*See* R-20.) A debtor need not have a possessory interest in the property for the estate to inherit it. *See Segal*, 382 U.S. at 379. So although Clegg disposed of the funds transferred to Pink, he still retained an equitable interest in recovery because he retained the right to file for bankruptcy. *See Simply Essentials*, 78 F. 4th at 1008–09. To find otherwise misreads § 541(a)(1) by ignoring the broadness of property of the estate that this Court has insisted upon.

In this case, Clegg maintained an inchoate interest in the $20,000 payments he made to his mother, which then would (and did) transfer to the trustee, Floyd, when the case converted to Chapter 7. Although the avoidance action does not benefit Clegg directly, in the sense of his retaining the money for personal use, it would grant him an equitable interest in the transfer, given the possibility of bankruptcy. Therefore, similar to a contingent beneficiary in trust whose interest may not vest in possession, a would-be debtor has an interest in a preferential transfer under § 541(a)(1). *See Giagnorio*, 686 N.E. at 45–46. In keeping with the "all-encompassing" nature of estate property, then, a § 547 claim becomes estate property on the commencement of the case.

ii. In the alternative, a § 547 action is also property of the estate because the trustee acquires it upon filing pursuant to § 541(a)(7)'s plain language.

Section 541(a)(7) draws into the estate "[a]ny interest in property that the estate acquires after commencement of the case. *See In re McClain*, 516 F.3d 301, 312 (5th Cir. 2008) ("Congress enacted § 541(a)(7) to clarify its intention that § 541 be an 'all-embracing definition and to ensure that property interests created with or by property of the estate are themselves property of the estate."' (quoting *In re Hanley*, 305 B.R. 84, 87 (Bankr. M.D. Fla. 2003)) Furthermore, "[u]pon the filing of a bankruptcy petition, the estate automatically acquires a cause of action to seek avoidance of voidable transfers and to preserve those transfers for the benefit of the estate." *In re Brown*, 2004 WL 5846460 at *2 (Bankr. N.D. Ga. Oct. 8, 2004); *see also In re Wilson*, 624 F.2d 236, 238 (11th Cir. 1982) (indicating that a section 548 avoidance claim would fall within the reach of section 541(a)(7), which covers interests "not covered by a specific statutory provision mandating some other treatment."). In addition, § 541(b)—the Code provision detailing what does not belong in the estate—does not specifically carve out avoidance actions from estate property. *See* 11 U.S.C. § 541(b).

Here, because causes of action are property, they would automatically come within the purview of section 541(a)(7) upon the bankruptcy filing. *See In re Brown*, 2004 WL 5846460 at *2. Moreover, section 541(a)(7) embraces a § 547 avoidance action, considering the Code does not "mandate[e]" that avoidance actions be treated differently. *See In re Wilson*, 624 F.2d at 238. Importantly, Congress has bolstered such a finding by explaining that § 541(a)(7) is "all-embracing." *See In re McClain*, 516 F.3d at 312. Therefore, because the Code does not otherwise expressly provide for different treatment of a § 547 action, and other Chapter 5 claims more generally, then § 541(a)(7) covers such a claim. *See id.*; 11 U.S.C. § 541(b).

iii. This Court's comments in *Nordic Village* establish that a section 550 claim is estate property.

As relevant here, § 550(a) offers that "to the extent that a transfer is avoided under section 544, 545, 547, 548, 549, 553(b), or 724(a) of this title, the trustee may recover, for the benefit of the estate, the property transferred." In *Nordic Village*, this Court considered whether the Bankruptcy Code waived sovereign immunity. U.S. at 31. In reaching its decision, this Court relied in part on its understanding of § 550, stating that "the right to recover a postpetition transfer under § 550 is clearly a "claim" (defined in § 101(4)(A)) and is "property of the estate" (defined in § 541(a)(3))." *Id.* at 37.

It is not the conclusion of this case that ultimately relates to the issue at hand—it is this Court's reasoning in reaching that decision. This Court expressed that § 550, the right to recover itself, not just the recovery, is a claim falling under § 541(a)(3). Nowhere here does this Court intimate that the claim must be avoided first, it is enough to merely have a claim. Thus, a § 550 claim could itself fall under section 541(a)(3) based on this Court's thoughts alone.

Although, here, the § 550 claim relates to a prepetition transfer, if as mentioned above, the debtor has an inchoate interest in the avoidance action, then the debtor must also have an

inchoate interest in the right to recover. Otherwise, the debtor would not be able to recover the proceeds or obtain the tangible property interest to which its intangible interests are tied, which would be nonsensical. Therefore, even if § 541(a)(3) is unavailing and this Court wishes to distinguish prepetition and postposition actions, the above provision of § 541(a)(1) would still work; as would the all-embracing § 541(a)(7), since the Code does not provide treatment otherwise for a § 550 claim.

The Thirteenth Circuit's explanation that *Nordic Village* is inapposite because it was later overruled by statute is meritless. Although the Bankruptcy Reform Act of 1994 implicates the holding of *Nordic Village*—regarding the government's ability to raise a sovereign immunity defense— it does not, whatsoever, address whether a § 550 claim is property of the estate. *See e.g.*, *Hanna Coal Co. v. IRS*, No. CIV.A.92–0071–B, 1994 WL 666928, at *1 (W.D.Va. Oct.12, 1994) (indicating that the Bankruptcy Reform Act overrules the sovereign immunity defense to violations of the automatic stay but does not mention § 550). Thus, because the proposition for which the Petitioner cites *Nordic Village* remains unblemished, this Court should adhere to its prior comments regarding § 550 claims being property of the estate.

iv. The rule against surplusage is not a mandate that precludes finding § 547 and § 550 claims to be property of the estate.

This Court has insisted that the "canon against surplusage is not an absolute rule." *Marx v. Gen. Revenue Corp.*, 568 U.S 371, 385 (2013); *see also Lamie v. U.S. Tr.*, 540 U.S. 526, 536 (2004) ("Surplusage does not always produce ambiguity and our preference for avoiding surplusage constructions is not absolute.") Moreover, when construing the Bankruptcy Code, "redundancy is not the same as surplusage." *In re Piazza*, 719 F.3d 1253, 1266 (11th Cir. 2013); *see also Conn. Nat'l Bank v. Germain*, 503 U.S. 249, 253 (1992) ("Redundancies across statutes are not unusual events in drafting[.]"); *In re Murray Metallurgical Coal Holdings, LLC*, 623

B.R. 444, 509 (Bankr. S.D. Ohio 2021) ("There is nothing superfluous about a statute that makes a claim property of the estate while another part of the statute makes the recovery on the claim property of the estate.").

Because surplusage is not an absolute rule, this Court should not be dissuaded from finding that avoidance actions fall under § 541(a)'s plain meaning. *See Marx*, 568 U.S. at 385; *Lamie*, 540 U.S. at 536. Additionally, a finding that avoidance actions are property would not render § 541(a)(3) as superfluous because § 541(a)(3) includes cross-references to other Code provisions aside from § 550. *See* 11 U.S.C § 541(a)(3) ("Any interest in property that the trustee recovers under section 329(b), 363(n), 543, . . . 553, or 723 of this title."). And, furthermore, this construction of the Code would not even be unusual, which should further increase this Court's confidence in finding § 547 and § 550 claims to be property of the estate. *See Murray Metallurgical*, 623 B.R. at 609.

C. Additional Code Provisions and Bankruptcy Practices Empower the Trustee to Sell Sections 547 and 550 Claims to Maximize the Value of the Estate.

Section 704(a)(1) compels the Trustee to "collect and reduce to money the property of the estate for which such trustee serves." 11 U.S.C. § 704(a)(1); *see also Commodity Futures Trading Com'n v. Weintraub*, 471 U.S. 343, 352 (1986) ("The trustee . . . has the duty to maximize the value of the estate."); Hon. Steven Rhodes, *The Fiduciary and Institutional Obligations of A Chapter 7 Bankruptcy Trustee*, 80 AM. BANKR. L.J. 147, 164–65 (2006) (maximizing the value of the estate includes both maximizing the estate's distribution and minimizing the estate's administrative expenses).

i. Selling a §§ 547 and 550 claims fulfills the trustee's fiduciary duties by maximizing the estate's value.

To carry out its fiduciary duties, this Court should permit the trustee to sell these causes of action. Because § 704(a)(1) requires the trustee to convert property of the estate to money, the trustee must consider how it can liquidate property, and an easy way to do that could be to sell the claims altogether. On the one hand, it may be prohibitively expensive to convert a cause of action to money, leaving a "dead" asset in the estate, one that has value but costs too much to leverage. On the other hand, finding that these claims are estate property allows the trustee to get present-value consideration for claims that may be costly (both in time and money) to litigate, maintaining consistency with the trustee's fiduciary duty to maximize estate distribution and minimize costs, clearly making the option to sell preferable.

ii. A sale pursuant to §363(b), by definition, must be in the best interest of the estate.

Additionally, § 363(b)(1) states that "[t]he trustee, after notice and a hearing, may use, *sell*, or lease, other than in the ordinary course of business, property of the estate." 11 U.S.C. § 363(b)(1) (emphasis added). A § 363 sale must be one of estate property. *See Moore*, 608 F.3d at 258 ("A trustee may sell only assets that are property of the estate."). Furthermore, these sales "must be supported by an articulated business justification, good business judgment, or sound business reasons." *Id.* at 263. Moreover, before these sales can take place, there must be notice, a hearing, and court approval. *Id.* In essence, then, if a § 363 sales occurs, it is in the best interest of the estate. *See e.g.*, *Lahijani*, 325 B.R. at 288 ("The court's obligation in § 363(b) sales is to assure that optimal value is realized by the estate under the circumstances.").

And although this Court in *Hartford Underwriters Ins. Co v. Union Planters Bank, N.A.* appeared to preclude transfer of rights that are specifically granted to a trustee, this Court

actually specified that it was not deciding whether a court may allow "other interested parties to act in a trustee's stead." 530 U.S. 1, 6–7, 13 n.5 (2000). Furthermore, this Court suggested that trustee and court approval could remove the bar on a non-trustee pursuing an estate claim. *See id.* at 13 n.5; *see also Mellon Bank, N.A. v. Dick Corp*, 351 F.3d 290, 292 (7th Cir. 2003) ("The Supreme Court's decision in *Hartford Underwriters* did not disturb decisions allowing a lineal descent of statutory rights.").

A § 363(b) sale is protected by proper safeguards that prevent unsavory outcomes. Because there must be "good business judgment" for a sale of avoidance actions to occur, a trustee is prevented from offloading these property rights at its sole discretion. *See Moore*, 608 F.3d at 263. Additionally, as the Respondent concedes Eclipse did in this case, (*see* R-35), the purchaser must pay "optimal value" for the property, rather than getting these causes of action at a steep discount. And if that were not enough, both the court and the trustee must approve of the transfer, which inserts prophylactic measures to ensure that similarly situated creditors are not treated disparately. *Moore*, 608 F.3d at 263.

Hartford Underwriters is not applicable here because this Court said that the holding did not pertain to instances where someone might act in the trustee's stead. *See* 530 U.S. at 13 n.5. Even if that language were not present, because a sale requires court and trustee approval, the exception this Court carved out would apply, rendering the case moot as to this issue. *See id.*

iii. <u>This Court can extend the policies undergirding the sales of claims in a Chapter 11 case to the Chapter 7 Context.</u>

Sales of Chapter 5 causes of action have been recognized in Chapter 11 reorganizations, Chapter 11 liquidations, and Chapter 7 liquidations but are most prevalent in Chapter 11 reorganizations. *See e.g.*, *In re P.R.T.C., Inc.*, 177 F.3d 774, 781 (9th Cir. 1999) (explaining that these sales are well-established in Chapter 11 reorganizations and that they may occur "outside a

Chapter 11 reorganization," such as a Chapter 11 or Chapter 7 liquidation); *see also Murray Metallurgical*, 623 B.R. at 507 ("Courts in Chapter 11 cases regularly approve motions to sell assets that include requests to sell avoidance actions.") With respect to Chapter 11 reorganization, courts permit these sales because they insert essential financing into the estate. *See e.g.*, *U.S. Dep't of Treasury v. Off. Comm. of Unsecured Creditors of Motors Liquidation Co.*, 475 B.R. 347, 354 (Bankr. S.D.N.Y. 2012) (indicating DIP lenders would get liens on avoidance actions in return).

The reasons to authorize sales in a Chapter 11 reorganization are also present in Chapter 7 liquidation. As the business in a Chapter 11 receives vital funds, the estate in a Chapter 7 would receive money in exchange for these property rights, thereby aiding the trustee in maximizing the distribution of the estate. Thwarting these sales in Chapter 7 hamstrings the trustee from doing the very action courts in Chapter 11 permit: trading property rights for money to help attain a successful bankruptcy for both the debtor and creditors.

iv. The similarities and shortcomings of derivative standing encourage finding that § 547 and § 550 claims can be sold for the benefit of the estate.

Broad inquiry into all kinds of bankruptcy cases reveals that "every circuit court that has ruled on the question of derivative standing after *Hartford* [*Underwriters*] has allowed it." (*In re Roman Catholic Church of Archdiocese of Santa Fe*, 621 B.R. 502, 506 (Bankr. D.N.M. 2020) (noting that the Second, Third, Fifth, Sixth, Seventh, Eighth, and Ninth Circuits have all allowed, in one context or another, a creditor to pursue a claim on behalf of the estate through derivative standing). Additionally, "[a]lmost all bankruptcy courts, BAPs, and district courts have ruled the same." *Id.*; *see also In re Adelphia Comm. Corp.*, 330 B.R. 364, 373 (Bankr. S.D.N.Y. 2005) (describing derivative standing as "longstanding, and nearly universally recognized.").

Regarding chapter 7 cases in particular, many courts permit a creditor's derivative standing. E.g., *In re Racing Servs., Inc.*, 540 F.3d 892, 898 (8th Cir. 2008) ("[D]erivative standing is available to a creditor to pursue avoidance actions when it shows that a Chapter 7 trustee . . . is "unable or unwilling" to do so."); *Fogel v. Zell*, 221 F.3d 955, 965 (7th Cir. 2000) ("If a trustee unjustifiably refuses a demand to bring an action to enforce a colorable claim of a creditor, the creditor may obtain the permission of the bankruptcy court to bring the action in place of, and in the name of, the trustee."); *see also Hatchett v. United States*, 330 F.3d 875, 885–86 (6th Cir. 2003) (permitting derivative standing in a Chapter 7 where the trustee had abandoned the property under § 554(a)).

The widespread practice of derivative standing indicates that someone other than a trustee can pursue an avoidance action. Because interested parties can already pursue causes of action on behalf of the estate, it would not be a large leap for this Court to similarly permit the outright sale of those causes of action. *See Fogel*, 221 F.3d at 965.

Section 363(b) sales offer benefits, to both the estate and creditors, that are unavailable in derivative standing. Chief among them is the immediate injection of cash into the estate. Instead of waiting for a creditor to litigate the action, the estate promptly receives fair consideration for the right to pursue the claim. And the estate does not bear the risk of the claim's unsuccessful prosecution. Additionally, if unsecured creditors only have derivative standing at their disposal, they may be unwilling to pursue such claims because the procurement must be turned over to the estate and thus any priority claimants. Therefore, selling § 547 and § 550 claims provides present value to the estate and incentivizes creditors to prosecute such claims, ultimately maximizing the estate's value.

D. The circuit courts that have addressed the issue have, in unison, interpreted avoidance actions to be property of the estate.

To date, several circuits have explicitly confronted the issue of whether a particular type of avoidance action is property of the estate—all have found that they are. *See In re Ontos, Inc.*, 478 F.3d 427, 431 (1st Cir. 2007) ("It is well established that a claim for fraudulent conveyance is included within this type of property."); *In re Moore*, 608 F.3d 253, 261 (5th Cir. 2010) ("The trustee may therefore sell these state law fraudulent-conveyance actions . . . . Allowing a trustee to sell § 544(b) rights of action is in accord with the trustee's existing powers.") (internal citations omitted); *In re Simply Essentials*, 78 F.4th 1006, 1009 (8th Cir. 2023) ("Because debtors have the right to file for bankruptcy and the debtor in possession or the Trustee may file avoidance actions to recover property, the debtor has an inchoate interest in the avoidance actions prior to the commencement of the bankruptcy proceedings."); *Silverman v. Birdsell*, 796 F. App'x 935, 937 (9th Cir. 2020); ("[A] bankruptcy trustee may sell an estate's avoidance claims . . . ."); *see also Nat'l Tax Credit Partners, L.P. v. Havlik*, 20 F.3d 705, 708–709 (7th Cir. 1994) ("[T]he right to recoup a fraudulent conveyance . . . is property of the estate . . . ."); *Delgado Oil Co. v. Torres*, 785 F.2d 857, 862 (10th Cir. 1986) (considering avoidance actions property of the estate that the trustee can recover); Brendan Gage, *Is There a Statutory Basis for Selling Avoidance Actions?*, 22 J. BANKR. L. & PRAC. 3 Art. 1 (2013) (noting that the majority of circuits, save for the third circuit, have concluded that avoidance actions are estate property).

On the other hand, only one circuit case has indicated that a preference action may not be property of the estate. *In re Cybergenics Corp.*, 226 F.3d 237, 245 (3d Cir. 2000) (electing to not include a fraudulent conveyance action as an asset of the estate). However, the Third Circuit recently clarified that its stance on preference actions in *Cybergenics* was non-binding dicta. *In re Wilton Armetale, Inc.*, 968 F.3d 273, 285 (3d Cir. 2020) ("*Cybergenics* does not hold that

trustees cannot transfer causes of action. It leaves that question open . . . ."); *see also In re Pursuit Cap. Mgmt., LLC*, 595 B.R. 631, 656–57 (Bankr. D. Del. 2018) ("[T]he Third Circuit has not determined whether avoidance actions are property of the estate or whether such claims or a trustee's right to pursue avoidance actions can be sold. . . . *Cybergenics I* did not decide either of these matters . . . .").

After examining the weight of authority on each side, this Court should side with the consensus of circuit courts and decide that an avoidance action, like a § 547 claim, is property of the estate. Moreover, the single case that purportedly cuts against this harmony has been siloed as dicta, indicating that it has little weight, if any. *See Wilton Armetale*, 968 F.3d at 285. Thus, given magnitude of case law supporting the Petitioner's argument, this Court should have increased confidence in finding that avoidance actions are alienable property of the estate.

CONCLUSION

There is no reason to depart from the Code's plain language, which unambiguously provides that post-petition, pre-conversion appreciation inures to the estate. Additionally, because sections 547 and 550 are property of the estate under section 541(a), the trustee, according to its fiduciary duties, can sell the claims pursuant to section 363(b). Therefore, this Court should reverse the Thirteenth Circuit.

APPENDIX

11. U.S.C. § 348

(a) Conversion of a case from a case under one chapter of this title to a case under another chapter of this title constitutes an order for relief under the chapter to which the case is converted, but, except as provided in subsections (b) and (c) of this section, does not effect a change in the date of the filing of the petition, the commencement of the case, or the order for relief.

. . .

(f) (1) Except as provided in paragraph (2), when a case under chapter 13 of this title is converted to a case under another chapter under this title—

(A) property of the estate in the converted case shall consist of property of the estate, as of the date of filing of the petition, that remains in the possession of or is under the control of the debtor on the date of conversion;

(B) valuations of property and of allowed secured claims in the chapter 13 case shall apply only in a case converted to a case under chapter 11 or 12, but not in a case converted to a case under chapter 7, with allowed secured claims in cases under chapters 11 and 12 reduced to the extent that they have been paid in accordance with the chapter 13 plan; and

(C) with respect to cases converted from chapter 13—

(i) the claim of any creditor holding security as of the date of the filing of the petition shall continue to be secured by that security unless the full amount of such claim determined under applicable nonbankruptcy law has been paid in full as of the date of conversion, notwithstanding any valuation or determination of the amount of an allowed secured claim made for the purposes of the case under chapter 13; and

(ii) unless a prebankruptcy default has been fully cured under the plan at the time of conversion, in any proceeding under this title or otherwise, the default shall have the effect given under applicable nonbankruptcy law.

(2) If the debtor converts a case under chapter 13 of this title to a case under another chapter under this title in bad faith, the property of the estate in the converted case shall consist of the property of the estate as of the date of conversion.

11 U.S.C. § 363

. . .

(b) (1) The trustee, after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate, except that if the debtor in connection with offering a product or a service discloses to an individual a policy prohibiting the transfer of personally identifiable information about individuals to persons that are not affiliated with the debtor and if such policy is in effect on the date of the commencement of the case, then the trustee may not sell or lease personally identifiable information to any person

. . .

11 U.S.C. § 541

(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

. . .

(3) Any interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 of this title.

. . .

(6) Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.

(7)Any interest in property that the estate acquires after the commencement of the case.

(b) Property of the estate does not include—

(1) any power that the debtor may exercise solely for the benefit of an entity other than the debtor;

(2) any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease before the commencement of the case under this title, and ceases to include any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease during the case;

. . .

(8) subject to subchapter III of chapter 5, any interest of the debtor in property where the debtor pledged or sold tangible personal property (other than securities or written or printed evidences of indebtedness or title) as collateral for a loan or advance of money given by a person licensed under law to make such loans or advances, where—

(A) the tangible personal property is in the possession of the pledgee or transferee;

(B) the debtor has no obligation to repay the money, redeem the collateral, or buy back the property at a stipulated price; and

(C) neither the debtor nor the trustee have exercised any right to redeem provided under the contract or State law, in a timely manner as provided under State law and section 108(b);

(9) any interest in cash or cash equivalents that constitute proceeds of a sale by the debtor of a money order that is made—

(A) on or after the date that is 14 days prior to the date on which the petition is filed; and

(B) under an agreement with a money order issuer that prohibits the commingling of such proceeds with property of the debtor (notwithstanding that, contrary to the agreement, the proceeds may have been commingled with property of the debtor), unless the money order issuer had not taken action, prior to the filing of the petition, to require compliance with the prohibition; or

. . .

11 U.S.C. § 547

. . .

(b) Except as provided in subsections (c) and (i) of this section, the trustee may, based on reasonable due diligence in the circumstances of the case and taking into account a

party's known or reasonably knowable affirmative defenses under subsection (c), avoid any transfer of an interest of the debtor in property—

(1) to or for the benefit of a creditor;

(2) for or on account of an antecedent debt owed by the debtor before such transfer was made;

(3) made while the debtor was insolvent;

(4) made—

(A) on or within 90 days before the date of the filing of the petition; or

(B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and

(5) that enables such creditor to receive more than such creditor would receive if—

(A) the case were a case under chapter 7 of this title;

(B) the transfer had not been made; and

(C) such creditor received payment of such debt to the extent provided by the provisions of this title.

. . .

11 U.S.C. § 550

(a) Except as otherwise provided in this section, to the extent that a transfer is avoided under section 544, 545, 547, 548, 549, 553(b), or 724(a) of this title, the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from—

(1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or

(2) any immediate or mediate transferee of such initial transferee.

(b) The trustee may not recover under section [1] (a)(2) of this section from—

(1) a transferee that takes for value, including satisfaction or securing of a present or antecedent debt, in good faith, and without knowledge of the voidability of the transfer avoided; or

(2) any immediate or mediate good faith transferee of such transferee.

(c) If a transfer made between 90 days and one year before the filing of the petition—

(1) is avoided under section 547(b) of this title; and

(2) was made for the benefit of a creditor that at the time of such transfer was an insider; the trustee may not recover under subsection (a) from a transferee that is not an insider.

. . .