Team 6

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 APPEAL FROM THE
UNITED STATES COURT OF APPEALS
FOR THE THIRTEENTH CIRCUIT

BRIEF FOR THE RESPONDENT

TEAM NUMBER 6
COUNSEL FOR RESPONDENT

January 18, 2024

QUESTIONS PRESENTED

1. Whether an increase in equity in a debtor's property that accrues post-petition, pre-conversion inures to the benefit of the debtor or to the bankruptcy estate upon conversion of a case from Chapter 13 to Chapter 7 pursuant to 11 U.S.C. § 348.
2. Whether the avoidance powers created by Chapter 5 of the Bankruptcy Code are property of a debtor's bankruptcy estate that can be sold by the trustee to a third party.

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STATEMENT OF JURISDICTION

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

OPINIONS BELOW

The United States Bankruptcy Court for the District of Moot held for Respondent, Corporal Eugene Clegg, on both issues. Specifically, the Bankruptcy Court found that (1) any post-petition increase in equity prior to the date of conversion is not property of the Chapter 7 estate and belongs to the debtor pursuant to 11 U.S.C. § 348(f)(1); and (2) a Chapter 7 trustee's ability to avoid and recover preferential transfers under 11 U.S.C. §§ 547 and 550 are statutory powers that, therefore, cannot be sold. On timely direct appeal from the United States Bankruptcy Court for the District of Moot, as authorized by 28 U.S.C. § 158(d)(2)(A) and Federal Rule of Bankruptcy Procedure 8006, the United States Court of Appeals for the Thirteenth Circuit affirmed on both issues.

PERTINENT STATUTORY PROVISIONS

The pertinent statutory provisions of the Bankruptcy Code are 11 U.S.C. §§ 348, 541, 544, 547, 550, and 551.[1] The relevant portions are provided herein.

11 U.S.C. § 348. Effect of conversion

(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

[1] References within this brief to Title 11 of the United States Code may be to the Bankruptcy Code or to the statutory section provisions.

the debtor on the date of conversion[.]

. . . .

(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. § 541. Property of the estate

(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) 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(m), 543, 550, 553, or 723 of this title.

(4) Any interest in property preserved for the benefit of or ordered transferred to the estate under section 510(c) or 551 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.

11 U.S.C. § 544. Trustee as lien creditor and as successor to certain creditors and purchasers

(a) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by—

(1) a creditor that extends credit to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect to such credit, a judicial lien on all property on which a credit on a simple contract could have obtained such a judicial lien, whether or not such a creditor exists;

(2) a creditor that extends credit to the debtor at the time of the commencement of the case, and obtains, at such time and with respect to such credit, an execution against the debtor that is returned unsatisfied at such time, whether or not such a creditor exists; or

(3) a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser and has perfected such transfer at the time of the commencement of the case, whether or not such a purchaser exists.

(b)(1) Except as provided in paragraph (2), the trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502 of this title or that is not allowable only under section 502(e) of this title.

11 U.S.C. § 547. Preferences

(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. Liability of transferee of avoided transfer

(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 transferee.

11 U.S.C. § 551. Automatic preservation of avoided transfer

Any transfer avoided under section 522, 544, 545, 547, 548, 549, or 724(a) of this title, or any lien void under section 506(d) of this title, is preserved for the benefit of the estate but only with respect to property of the estate.

STATEMENT OF THE FACTS AND CASE

The parties do not dispute the following facts. (R. at 10.) Between 2011 and 2012, Corporal Eugene Clegg ("Debtor" or "Mr. Clegg") was transferred a 100% membership interest in The Final Cut, LLC ("Final Cut"), a single-screen movie theater, by his mother. (R. at 5.) At the time, Final Cut was financially stable and provided Debtor with a modest salary that served as his sole income for years. (R. at 5.) In 2016, Final Cut borrowed $850,000.00 from Eclipse Credit Union ("Eclipse") to make renovations to the theatre. (R. at 5.) As security, Eclipse was granted first priority liens on Final Cut's real and personal property, and Debtor executed an unconditional, unsecured personal guaranty in an unlimited amount. (R. at 5.)

Debtor completed much of the renovations with the assistance of local veterans, who graciously volunteered their time to the project, resulting in greatly reduced labor costs for the renovations. (R. at 5.) With the reduced costs, Final Cut retained approximately $75,000.00 from the loan at the end of the project, which was completed in early 2017. (R. at 5.) Final Cut reopened to the public, and local residents took great civic pride in the theater and all it represented. (R. at 5-6.) To show appreciation for the veterans' generosity and assistance, Final Cut, through Mr. Clegg, donated the remaining $75,000.00 loan proceeds to the Veterans of Foreign Wars ("VFW") (R. at 5.)

Final Cut was profitable until it was required to close due to the COVID-19 pandemic in March 2020, and remained inoperable for approximately a year. (R. at 6.) Because Final Cut served as his sole source of income, Debtor borrowed, on an unsecured basis, $50,000.00 from his mother on September 8, 2020. (R. at 6.) Debtor also incurred credit card debt and fell behind on his mortgage serviced by Another Brick in the Wall Financial Corporation ("Servicer"), which commenced foreclosure after several months of missed payments. (R. at 6.)

To stop the foreclosure, Debtor filed a Chapter 13 bankruptcy case on December 8, 2021 ("Petition Date"). (R. at 6.) At that time, Debtor maintained no equity in his home as of the Petition Date. (R. at 7.) He listed the value of his home on Schedule A/B at $350,000.00, subject to a secured mortgage obligation of $320,000.00, as listed on Schedule D and the maximum $30,000.00 homestead exemption allowed by the State of Moot law as reflected on Schedule C. (R. at 6-7.) Additionally, Debtor's Schedules E/F and H included a contingent, unliquidated debt in an unknown amount owed to Eclipse. (R. at 6.) Debtor also disclosed in his Statement of Financial Affairs aggregate payments to his mother of $20,000.00 during the previous year. (R. at 7.) Debtor proposed to fund his plan through the future income he would receive from Final Cut. (R. at 7.)

During the meeting of creditors, Eclipse was angry when it learned of the donation to VFW and commenced an adversary proceeding to have Debtor's obligation related to Eclipse's $850,000.00 loan to Final Cut declared nondischargeable pursuant to 11 U.S.C. § 523(a)(2)(A). (R. at 7.) Eclipse also objected to confirmation of Debtor's proposed plan based on bad faith. (R. at 8.) Eclipse and Debtor eventually reached a resolution whereby Eclipse withdrew its objection to confirmation in exchange for a $150,000.00 claim, of which $15,000.00 Debtor agreed would be nondischargeable even if the case was converted. (R. at 8.) The bankruptcy court approved the settlement and confirmed the Chapter 13 plan, at which time all property re-vested in Debtor. (R. at 8.)

Debtor made payments under the confirmed plan for eight months but was unable to continue making plan payments after he contracted long-COVID. (R. at 8.) In September 2022, Final Cut closed permanently, and Eclipse commenced foreclosure proceedings. (R. at 8.) Debtor converted his case to Chapter 7, and Vera Lynn Floyd was appointed as the Chapter 7 trustee ("the

Trustee"). (R. at 8-9.) In his conversion schedules, Debtor once again valued his home at $350,000.00 and disclosed the $20,000.00 payments to his mother. (R. at 9.) Debtor also listed the debts to Eclipse in the amount of $200,000.00 and to Servicer in an undisclosed amount on his house, which Debtor indicated he would reaffirm. (R. at 9.) According to the Chapter 13 trustee's final report, Servicer received total disbursements of $10,000.00 on Debtor's mortgage, and the funds the Chapter 13 Trustee was holding as a result of Debtor's settlement with Eclipse were returned to Debtor. (R. at 8 & n.7.) The parties have stipulated that Debtor's conversion to Chapter 7 did not occur in bad faith (R. at 8 n.8)

Based on an appraisal commissioned by the Trustee, the non-exempt equity in Debtor's home had increased by $100,000.00 over the original valuation of the property after the Petition Date. (R. at 9.) When the Trustee marketed the home for sale, Eclipse, perhaps looking for retribution and redemption for Debtor's $75,000.00 donation to VFW with loan proceeds, offered to purchase the home and the Trustee's potential preference claim against Debtor's mother for $470,000.00. (R. at 9.) The Trustee was satisfied that the offer maximized the value of the assets for the benefit of the estate and filed a motion to sell the home and the preference claim to Eclipse pursuant to 11 U.S.C. § 363(b) ("Sale Motion"). (R. at 9.)

Mr. Clegg objected to the Sale Motion, arguing that he, rather than the bankruptcy estate, retained the benefit of any post-petition, pre-conversion increase in the equity of his home and that the Trustee's statutory authority to avoid and recover transfers under the Bankruptcy Code could not be sold to a third party. (R. at 10.) The Bankruptcy Court ruled in Debtor's favor on both objections, and the Trustee timely filed her appeal (R. at 10.) On direct appeal, the Court of Appeals affirmed the Bankruptcy Court's decision on both issues. (R. at 24.)

STANDARD OF REVIEW

The facts in this case are not disputed by either party. (R. at 10.) Because the issues presented are purely questions of law, the standard of review is *de novo*. *Highmark Inc. v. Allcare Health Mgmt. Sys., Inc.*, 572 U.S. 559, 563 (2014). Under a *de novo* review, the issues will be decided as if this Court is the original deciding court. *Razavi v. Comm'r*, 74 F.3d 125, 127 (6th Cir. 1996).

SUMMARY OF ARGUMENT

The Thirteenth Circuit correctly ruled in favor of Mr. Clegg when it held that pursuant to 11 U.S.C. § 348(f)(1)(A), any post-petition, pre-conversion equity accrued in Debtor's home did not belong to the Chapter 7 estate upon conversion. Following the tenants of statutory interpretation, the Thirteenth Circuit correctly determined the term "property" within § 348(f)(1)(A) was ambiguous as to whether it included equity accrued in the property between the petition date and conversion. Due to this ambiguity, it was necessary to consult the legislative history of § 348(f)(1)(A) as required by statutory construction principles. In drafting § 348(f)(1)(A), Congress clearly intended for any post-petition, pre-conversion equity accrued in a debtor's property to inure to the debtor and not the bankruptcy estate. The Thirteenth Circuit's interpretation fits within the context of the Bankruptcy Code, is cohesive with 11 U.S.C. § 348(f)(2), and should, therefore, be affirmed.

Further, the Thirteenth Circuit's holding that avoidance actions cannot be sold because they are not property of the estate should be affirmed because any other interpretation results in the inclusion of superfluous language throughout Chapter 5. Congress could have extended a trustee's avoidance powers to Chapter 7 debtors as it did for Chapter 11 debtors in possession but purposely declined to do so. The Thirteenth Circuit's decision also correctly reflects the Congressional intent

of avoidance powers because they are reserved for the estate's fiduciary alone to ensure that any avoided preferences benefit the bankruptcy estate as a whole. Granting third parties standing to pursue avoidance actions in a Chapter 7 case is neither statutorily authorized nor necessary because other remedies already exist. Finally, avoidance powers cannot be sold because 11 U.S.C. § 541 unambiguously limits property of the estate to property interests the debtor possesses before the commencement of the case or interests in property that the estate acquires after the commencement of the case. Avoidance powers arise upon the commencement of the case, and these temporal issues bar them from being considered property of the estate.

Accordingly, this Court should affirm the Thirteenth Circuit Court of Appeals on both issues.

ARGUMENT

I. THE THIRTEENTH CIRCUIT CORRECTLY INTERPRETED 11 U.S.C. § 348(F)(1)(A) AND FOUND THAT ANY POST-PETITION, PRE-CONVERSION INCREASE IN EQUITY IN A DEBTOR'S PROPERTY INURES TO THE BENEFIT OF THE DEBTOR UPON CONVERSION FROM A CHAPTER 13 TO CHAPTER 7.

At the commencement of a bankruptcy case, an estate is created that includes "all legal or equitable interests of the debtor in property as of the commencement of the case" and "[p]roceeds, 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." 11 U.S.C. § 541(a)(1), (6).[2] The Chapter 13 estate expands this basic definition to include, in addition to a debtor's non-exempt assets at the date of the petition, post-petition property interests that the debtor acquires or earns "after the commencement of the case, but before the case is . . . converted

[2] Debtors may exempt certain property, and these exemptions are determined as of the date of the commencement of the case. *See* 11 U.S.C § 522. Such property that may be exempted from the bankruptcy estate includes any service medals awarded to Corporal Clegg, regardless of whether they were orange, red, and blue, or found in the zoo. Pink Floyd, *Corporal Clegg* (Apple 1968).

to a case under chapter 7." 11 U.S.C. § 1306(a)(1). The Bankruptcy Code authorizes conversion of a case from Chapter 13 to Chapter 7 pursuant to 11 U.S.C. § 1307(a), and in such instance, the property of the converted estate "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[.]" 11 U.S.C. § 348(f)(1)(A).

Following the principles of statutory interpretation, the plain language of § 348(f)(1)(A), when read in context of the Bankruptcy Code as a whole, is ambiguous as to whether the term "property" includes equity accrued in real property. The Thirteenth Circuit appropriately consulted the legislative history of § 348(f)(1)(A) and found Congress clearly intended for debtors to retain equity accrued in their property upon conversion. This interpretation fits squarely within the surrounding Code sections and accurately reflects Congressional intent.

A. The Plain Language of 11 U.S.C. § 348(f)(1)(A), Read in the Context of the Bankruptcy Code as a Whole, Supports a Determination That Equity Acquired Post-Petition Would Not Be Included in Property of the Estate as of the Petition Date.

A debtor may convert his or her case from Chapter 13 to another chapter, including Chapter 7, at any time. 11 U.S.C. § 1307(a). "Conversion from Chapter 13 to Chapter 7 does not commence a new bankruptcy case. The existing case continues along another track, Chapter 7 instead of Chapter 13, without 'effect[ing] a change in the date of the filing of the petition.'" *Harris v. Viegelahn*, 575 U.S. 510, 515 (2015) (quoting 11 U.S.C. § 348(a)). Absent bad faith, property of the converted estate consists of all estate property as of the date of the petition that is still in the debtor's possession on the date of conversion. 11 U.S.C. § 348(f)(1)(A).[3]

[3] In a bad faith conversion, property of the converted estate consists of property of the estate as of the date of conversion. 11 U.S.C. § 348(f)(2). The parties stipulated that Debtor did not convert in bad faith. (R. at 8 n.8.)

"It is 'a cardinal principle of statutory construction' that 'a statute ought, upon the whole, to be so construed that, if it can be prevented, no clause, sentence, or word shall be superfluous, void, or insignificant.'" *TRW Inc. v. Andrews*, 534 U.S. 19, 31 (2001) (quoting *Duncan v. Walker*, 533 U.S. 167, 174 (2001) (internal quotation marks omitted)); *see also United Savs. Ass'n of Tex. v. Timbers of Inwood Forest Assocs., Ltd.,* 484 U.S. 365, 371 (1988) ("Statutory construction . . . is a holistic endeavor. A provision that may seem ambiguous in isolation is often clarified by the remainder of the statutory scheme-because the same terminology is used elsewhere in a context that makes its meaning clear"). "Statutory language . . . 'cannot be construed in a vacuum. It is a fundamental canon of statutory construction that the words of a statute must be read in their context and with a view to their place in the overall statutory scheme.'" *Roberts v. Sea-Land Servs*., 566 U.S. 93, 101 (2012) (quoting *Davis v. Mich. Dep't of Treasury*, 489 U.S. 803, 809 (1989)). "A provision that may seem ambiguous in isolation is often clarified by the remainder of the statutory scheme—because the same terminology is used elsewhere in a context that makes its meaning clear, or because only one of the permissible meanings produces a substantive effect that is compatible with the rest of the law." *United Savs. Ass'n of Tex.*, 484 U.S. at 371 (citations omitted). Furthermore, when "'Congress includes particular language in one section of a statute but omits it in another'—let alone in the very next provision—this Court "presume[s]' that Congress intended a difference in meaning." *Loughrin v. United States*, 573 U.S. 351, 358 (2014) (quoting *Russello v. United States*, 464 U.S. 16, 23 (1983)).

Taking the statutory language as written, it is clear that property of the estate "as of the date of the filing of the petition" would not include any post-petition appreciation of assets that was not present on the petition date. *In re Robinson*, 472 B.R. 854, 857 (Bankr. M.D. Fla 2012). The *Robinson* court determined that upon conversion from a Chapter 13 to Chapter 7 case, post-

petition equity in the debtor's vehicles belonged to the debtors. *Id.* The court relied on the statutory scheme of § 348(f), which indicated that the date for determining property of the Chapter 7 estate upon conversion is the original petition date. *Id.* The court ruled in favor of the debtors, reasoning "at the time of their filing of the petition, the Debtors had no equity in either vehicle. The accumulated equity . . . is not property of the Chapter 7 estate pursuant to 11 U.S.C. § 348(f)." *Id.* This reasoning likewise fits well within the context of § 348(f)(2), which provides a bad-faith punishment exception where property of the estate is to be determined "as of the date of conversion." Pursuant to § 348(f)(2), including post-petition appreciation of pre-petition assets in estate property only in cases of bad faith serves as a deterrent, and thus, the same appreciation is not included in cases converted under § 348(f)(1)(A). In other words, "by providing that a debtor who converts in bad faith is not entitled to this post-petition property, § 348(f)(2) logically requires that a debtor receive the property if he acts in good faith." *In re Michael*, 699 F.3d 305, 314 (3d Cir. 2012).

In *Harris*, this Court held that upon conversion from a Chapter 13 case to a Chapter 7, post-petition wages not distributed to creditors by the time of conversion inured to the debtor and did not become part of the Chapter 7 estate. *Harris*, 575 U.S. at 515. This Court reasoned that the language of § 348(f)(1)(A) clearly states the converted estate is to consist of property of the estate upon the date of the original Chapter 13 petition and would not include wages earned post-petition. *Id.* at 517-18. Further, as explained in *Harris*, the exception for bad faith conversions is instructive: simply, if the debtor converted the case in bad faith, the converted Chapter 7 estate would "consist[] of the [Chapter 13] estate *as of the date of conversion*." *Id.* at 518 (quoting 11 U.S.C. § 348(f)(2) (emphasis added)). Because § 348(f)(2) was intended to penalize debtors who converted in bad faith "by making their postpetition wages available for liquidation and

distribution to creditors," this Court deduced there was no such penalty for good faith conversion, and "[s]hielding a Chapter 7 debtor's postpetition earnings from creditors enables the 'honest but unfortunate debtor' to make the 'fresh start' the Bankruptcy Code aims to facilitate." *Id.* (quoting *Marrama v. Citizens Bank of Mass*., 549 U.S. 365, 367 (2007) (internal quotations omitted)). The language of § 348(f)(2) clearly establishes that absent bad faith, any property that was not part of the estate at the date of original the Chapter 13 petition date belongs to the debtor upon conversion. *Id.* at 518-19.

Similarly, post-petition increases in the equity of a vehicle owned by the debtor at the time of the Chapter 13 petition do not become part of the Chapter 7 estate upon conversion. *In re Woodland*, 325 B.R. 583, 586 (Bankr. W.D. Tenn. 2005). Based upon the plain language of § 348(f)(1)(A), the "Chapter 7 estate relates back to what was property of the bankruptcy estate when the Chapter 13 was commenced and since the Debtor still has the vehicle in his possession, the present 'equity' in the vehicle does not belong to the Chapter 7 trustee[.]" *Id.*; *see also In re Robinson*, 472 B.R. at 856 ("The Court finds the greater weight of authority, and the legislative intent, supports the Debtors' position that the subject accumulated equity is not part of the converted Chapter 7 estate."). This result is the same whether "appreciation [came] from an overall increase in market values—inflation—[or] from increased value caused by renovations to the property paid for by a debtor." *Leo v. Burt* (*In re Burt*)*,* No. 01–43254–JJR–7, 2009 WL 2386102, at *6 (Bankr. N.D. Ala. July 31, 2009); *see also In re Pruneskip*, 343 B.R. 714, 717 (Bankr. M.D. Fla. 2006) ("Thus, the equity in the collateral, which accrued prior to the conversion to a Chapter 7, did not become property of the debtor's estate following the conversion.").

Under the plain language of § 348(f)(1)(A), property of the converted Chapter 7 estate does not include the $100,000.00 increased equity in Debtor's home. The parties do not dispute, as of

the Petition Date, Mr. Clegg's home was valued at $350,000.00, and he retained no equity in the home on that date. (R. at 6-7.) Instead, the home had acquired $100,000.00 in equity as of the conversion date. (R. at 9.) Therefore, the equity in Mr. Clegg's home was not present at the Petition Date, was acquired post-petition, and would not have been included within the scope of § 541(a) were it not for the provisions of § 1306(a)(1). There is no similar Code section applicable to Chapter 7 cases, and § 348(f) only allows post-petition equity in Debtor's home to be included in the converted Chapter 7 estate if Mr. Clegg had converted in bad faith.

The Trustee will likely argue that post-petition appreciation in pre-petition property is included in the converted Chapter 7 estate pursuant to § 541(a)(1) and (6). She will also likely argue that § 348(f)(2) references newly acquired post-petition property rather than post-petition appreciation in pre-petition property. Both arguments, however, are misguided. If property of the estate in a converted case is to be defined solely under § 541(a), then the property acquired post-petition would already have become property of the estate by operation of law under 11 U.S.C. § 541(a)(7)[4] as of the conversion, thus rendering § 348(f)(2) superfluous. *In re Hodges*, 518 B.R. 445, 451 (E.D. Tenn. 2014). Further, the interpretation of § 348(f)(1)(A)'s reference to property as it existed on the petition date "fits well within the bankruptcy code as a whole." *In re Barrera*, 620 B.R. 645, 651 (Bankr. D. Colo. 2020), *aff'd*, *Rodriguez v. Barrera* (*In re Barrera*), BAP No. CO-20-003, 2020 WL 5869458 (B.A.P. 10th Cir. Oct. 2, 2020), *aff'd*, 22 F.4th 1217 (10th Cir. 2022). As explained by the Bankruptcy Court for the District of Colorado, "statutes in the Code

[4] Subsection (a)(7) brings into the estate "[a]ny interest in property *that the estate acquires* after the commencement of the case." 11 U.S.C. § 541(a)(7) (emphasis added).

freeze the relative rights of the debtor, the creditors, and the estate as of the petition date." *In re Barrera*, 620 B.R. at 651.[5]

The Ninth Circuit held in *Matter of Castleman*, 75 F.4th 1052 (9th Cir. 2023), that because appreciation of property in a Chapter 7 case belongs to the estate, the same is true for conversion from Chapter 13 case to Chapter 7 case pursuant to § 541(a)(6). However, as Judge Tallman explains in his dissent, applying the § 541(a) definition of "property of the estate" under a normal Chapter 7 estate to § 348(f)(1)(A) without looking at the broader context of the Bankruptcy Code is incorrect, and "[b]y adopting the trustee's preferred interpretation of § 348(f), the majority sacrifices the text of the bankruptcy statutes on the altar of simplicity." *Castleman*, 75 F.4th at 1060.

The $100,000.00 increase in equity of Mr. Clegg's home did not become part of the Chapter 7 estate because property of the estate relates back to the Petition Date, i.e., the Chapter 13 commencement date, pursuant to § 348(f)(1)(A). Any other interpretation fails to appropriately consider the context and principles of the Bankruptcy Code. Therefore, the Thirteenth Circuit should be affirmed.

B. **To the Extent It Found the Statute Ambiguous, the Thirteenth Circuit Properly Consulted the Legislative History of 11 U.S.C. § 348(f)(1)(A) to Determine Congress Did Not Intend Post-Petition, Pre-Conversion Equity in a Home to be Included in the Chapter 7 Estate Upon Conversion.**

When interpreting statutes, the Court's role is to "construe the language so as to give effect to the intent of Congress." *United States v. Am. Trucking Ass'ns*, 310 U.S. 534, 542 (1940). In doing so, the Court must "look first to its language, giving the words their ordinary meaning," but

[5] The *Barrera* court cites the exemption statute as an example: "Section 522 allows a debtor to exempt certain assets up at a specific dollar amount of value [which is defined as] the fair market value '*as of the date of the filing of the petition*.'" 620 B.R. at 651 (quoting 11 U.S.C. § 522(a)(2) (emphasis added)). *See also* 11 U.S.C §§ 362(a)(4); 541; and 707.

that meaning must be within the context of the Code. *Roberts*, 566 U.S. at 100. When a statute is unambiguous, the "judicial inquiry is complete." *Conn. Nat'l Bank v. Germain*, 503 U.S. 249, 254 (1992). However, a statute is ambiguous if it is "capable of being understood in two or more possible senses or ways." *Chickasaw Nation v. United States*, 534 U.S. 84, 90 (2001). Courts should seek to construe Congressional intent "so that effect is given to all provisions, so that no part will be inoperative or superfluous, void or insignificant." *Ysleta Del Sur Pueblo v. Texas*, 142 S. Ct. 1929, 1939 (2022) (quoting *Corley v. United States*, 556 U.S. 303, 314 (2009) (internal quotation marks omitted)). In discerning Congressional intent, the existing statutory text must be examined first "and not the predecessor statutes." *Lamie v. United States Tr.*, 540 U.S. 526, 534 (2004) (citing *Hughes Aircraft Co. v. Jacobson*, 525 U.S. 432, 438 (1999)). "[W]hen the statute's language is plain, the sole function of the courts—at least where the disposition required by the text is not absurd—is to enforce it according to its terms." *Id.* (quoting *Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 6 (2000) (internal quotation marks omitted)). "The Court may not 'replace the actual text with speculation as to Congress' intent.'" *Okla. v. Castro-Herta*, 142 S. Ct. 2486, 2496 (2022) (quoting *Magwood v. Patterson*, 561 U.S. 320, 334 (2010)). "[T]he Court 'will presume more modestly' that 'the legislature says what it means and means what it says.'" *Id.* (quoting *Henson v. Santander Consumer USA Inc.*, 582 U.S. 79, 89 (2017) (internal citations omitted)).

An overwhelming majority of courts addressing the issue have held that property of the estate under § 348(f)(1)(A) means property of the estate as it existed on the date of the petition such that it does not include post-petition appreciation in pre-petition assets. *See In re Barrera*, 22 F.4th at 1221 (holding that proceeds from a post-confirmation, pre-conversion sale of the debtor's home were not included in the property of the Chapter 7 estate upon conversion); *In re Hodges*,

518 B.R. at 451 (holding that post-confirmation, pre-conversion equity accrued in debtor's home was not included in property of the Chapter 7 estate upon conversion.); *In re Woodland,* 325 B.R. at 586 (holding that equity acquired in the debtors' motor vehicle post-commencement of their Chapter 13 case did not become property of the estate upon conversion to a Chapter 7 case); *In re Pruneskip*, 343 B.R. at 717 ("[T]he property of the estate and the Debtor's equity in the [property] is determined as of the filing date of the Chapter 13 Petition, and not the date on which the Debtor's case was converted to a Chapter 7 case[.]"). Conversely, a minority of courts have interpreted property of the estate to include any physical property of the estate as of the petition date, including any post-petition appreciation in value. *See Matter of Castleman*, 75 F.4th at 1060 (holding that assets in the debtor's possession at the time of original filing and retained until conversion become part of the Chapter 7 bankruptcy estate and "any change in the value of such an asset is also part of that estate."); *In re Goetz*, 647 B.R. 412, 416 (Bankr. W.D. Mo. 2022) ("Because equity is not a distinct item of property, §§ 348(f)(1) and 541(a)(1) include it in the converted estate." (internal citations omitted)), *aff'd*, *Goetz v. Weber* (*In re Goetz*), 651 B.R. 292 (B.A.P. 8th Cir. 2023). Therefore, the question of whether equity in property is considered separate from the physical property under § 348(f)(1)(A) is ambiguous because the term has been construed or understood in different ways. As stated by the Tenth Circuit Bankruptcy Appellate Panel,

> [w]e can think of no person more well-informed in the nuances of the Bankruptcy Code than a bankruptcy judge. If two bankruptcy judges do not agree whether postpetition appreciation in value of property belongs to a chapter 7 estate upon conversion, then § 348(f)(1)(A) is open to two or more interpretations. A split on the issue in other jurisdictions also suggests the statute's plain language is ambiguous.

In re Barrera, 2020 WL 5869458, at *5. Because the term "property" within § 348(f)(1)(A) is ambiguous, the Thirteenth Circuit properly turned to legislative history to ascertain Congressional intent.

Section 348(f) was added to the Bankruptcy Code through the Bankruptcy Reform Act of 1994. Congressional intent behind the amendment is provided in the House of Representatives Committee on the Judiciary report:

> This amendment would clarify the Code to resolve a split in the case law about what property is in the bankruptcy estate when a debtor converts from chapter 13 to chapter 7. The problem arises because in chapter 13 (and chapter 12), any property acquired after the petition becomes property of the estate, at least until confirmation of a plan. Some courts have held that if the case is converted, all of this after-acquired property becomes part of the estate in the converted chapter 7 case, even though the statutory provisions making it property of the estate do not apply to chapter 7. Other courts have held that property of the estate in a converted case is the property the debtor had when the original chapter 13 petition was filed. These latter courts have noted that to hold otherwise would create a serious disincentive to chapter 13 filings. For example, a debtor who had $10,000 equity in a home at the beginning of the case, in a State with a $10,000 homestead exemption, would have to be counseled concerning the risk that after he or she paid off a $10,000 second mortgage in the chapter 13 case, creating $10,000 in equity, there would be a risk that the home could be lost if the case were converted to chapter 7 (which can occur involuntarily). If all of the debtor's property at the time of conversion is property of the chapter 7 estate, the trustee would sell the home, to realize the $10,000 in equity for the unsecured creditors and the debtor would lose the home.
>
> This amendment overrules the holding in cases such as *Matter of Lybrook*, 951 F.2d 136 (7th Cir. 1991) and adopts the reasoning of *In re Bobroff*, 766 F.2d 797 (3d Cir. 1985). However, it also gives the court discretion, in a case in which the debtor has abused the right to convert and converted in bad faith, to order that all property held at the time of conversion shall constitute property of the estate in the converted case.

H.R. Rep. No. 103-835, at 57 (1994), *as reprinted in* 1994 U.S. Code Cong. & Adm. News 3340, 3366.

The debtors in *In re Lybrook* inherited $70,000.00 worth of land post-Chapter 13 petition but pre-Chapter 7 conversion. *In re Lybrook*, 951 F.2d 136 (7th Cir. 1991). The Seventh Circuit applied § 1306(a)(1), providing that property acquired after the case's commencement but before the case is closed, dismissed, or converted belongs to the estate. *Id.* at 139. Perhaps because this determination was made before the House Report publication, the *Lybrook* court incorrectly held

that because the land became property of the estate during the Chapter 13 case, the land also belonged to the Chapter 7 estate. *Id*. at 138-39. The court reasoned this result was necessary to discourage debtors from filing a Chapter 13 case before converting to a Chapter 7 in order to retain post-petition acquired property. *Id*. Conversely, in *In re Bobroff,* 766 F.2d 797 (3d Cir. 1985), the debtor accrued multiple tort causes of action post-Chapter 13 petition but prior to Chapter 7 conversion. The Third Circuit determined the causes of action were not part of the converted Chapter 7 estate, explaining that "[i]f debtors must take the risk that property acquired during the course of an attempt at repayment will have to be liquidated for the benefit of creditors if chapter 13 proves unavailing, the incentive to give chapter 13—which must be voluntary—a try will be greatly diminished." *Bobroff*, 766 F.2d at 803.

Upon examination of the text, the Tenth Circuit Bankruptcy Appellate Panel found the House Report to be a "'sufficiently specific, clear and uniform . . . indicator of intent' to suggest Congress intended to encourage debtors to proceed with a chapter 13 filing without being punished should they later convert to chapter 7." *In re Barrera*, 2020 WL 5869458, at *7 (quoting *Miller v. Comm'r*, 836 F.2d 1274, 1282 (10th Cir. 1988)). Additionally, the court stated that "interpreting § 348(f)(1)(A) in this manner does not contradict or otherwise impair other provisions of the Bankruptcy Code. Rather, such a reading complements other Code sections." *Id.* The Tenth Circuit later affirmed the Bankruptcy Appellate Panel's reasoning:

> Those debtors who try a repayment plan, but ultimately fail, are generally no worse off upon a good-faith conversion than if they had originally filed under Chapter 7. And those debtors who convert from Chapter 13 to Chapter 7 in bad faith are punished because their otherwise immune post-petition property interests are available for liquidation and distribution to creditors.

In re Barrera, 22 F.4th at 1221.

Allowing debtors to retain any post-petition, pre-conversion property upon conversion to Chapter 7 is the clear intent of § 348(f)(1)(A), and to hold otherwise would place debtors "in a worse position than if the petition had been filed in Chapter 7 initially." *Brown v. Barclay* (*In re Brown*), 953 F.3d 617, 620 (9th Cir. 2020); *see also Pisculli v. T.S. Haulers, Inc.* (*In re Pisculli*), 426 B.R. 52, 63 (E.D.N.Y. 2010) (stating that Congress's intent behind enacting § 348(f) was "to equalize the treatment that a debtor would receive" in a converted Chapter 7 case "with the treatment that the debtor would have received if he or she had filed a Chapter 7 petition originally. . . thereby vitiating any disincentive toward voluntary repayment plans under Chapter 13" (internal citations omitted)), *aff'd*, *Pisculli v. T.S. Haulers, Inc.* (*In re Pisculli*), 408 F. App'x 477 (2d Cir. 2011); *Bogdanov v. Laflamme* (*In re Laflamme*), 397 B.R. 194, 201 (Bankr. D.N.H. 2008) ("Congress was concerned that a contrary rule would greatly dissuade debtors and create a serious disincentive to chapter 13 filing because debtors would fear that property acquired after filing could be lost if the case were converted." (internal citations omitted)); *In re Fobber*, 256 B.R. 268, 277–78 (Bankr. E.D. Tenn. 2000) ("By adopting *Bobroff* in its enactment of § 348(f)(1)(A), Congress intended to avoid penalizing debtors for their chapter 13 efforts by placing them in the same economic position they would have occupied if they had filed chapter 7 originally." (internal citations omitted)).

As emphasized by other courts' analyses of the legislative history of § 348(f)(1)(A), post-petition, pre-conversion equity accrued in a property belongs to the debtors upon conversion from Chapter 13 to Chapter 7. *See, e.g., In re Nichols*, 319 B.R. 854, 857 (Bankr. S.D. Ohio 2004) ("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."); *In re Boyum,* No. 05–1044–AA, 2005 WL 2175879, at *2 (D. Or. Sept. 6, 2005) ("Therefore, to the

extent that appellant acquired equity in the Subaru Forester after the filing her Chapter 13 petition, such equity is not property of the estate upon conversion to Chapter 7."). Further, the House provided an example that specifically speaks to equity accrued in a home post-petition but pre-conversion. H.R. Rep. No. 103-835, at 57 (1994), *as reprinted in* 1994 U.S. Code Cong. & Adm. News 3340, 3366. Within that example, Congress made clear it intended for post-petition, pre-conversion equity in a home inure to the debtor, not the Chapter 7 estate. While the example speaks to equity accrued through the debtor's payment of mortgage as opposed to appreciation due to a significant upswing in the housing market, it nonetheless demonstrates Congressional intent that any equity accrued post-petition is not part of the estate as of the date of the conversion. Additionally, the example further supports interpreting § 348(f)(1)(A) in conjunction with § 348(f)(2), whereby any equity accrued as of the conversion date becomes property of the Chapter 7 estate only when a debtor converts in bad faith. This deterrent would serve no purpose if the Code required the same equity to become property of the estate regardless of a debtor's bad or good faith. H.R. Rep. No. 103-835, at 57 (1994), *as reprinted in* 1994 U.S. Code Cong. & Adm. News 3340, 3366.

The Thirteenth Circuit correctly held that when a debtor converts from Chapter 13 to Chapter 7 in good faith, he or she retains any post-petition, pre-conversion equity accrued in a home. This finding is supported by both the Congressional intent expressed in the legislative history of § 348(f)(1)(A) and how the statute fits within the context of the Bankruptcy Code as a whole. This Court should affirm the Thirteenth Circuit because the language of the statute is clear, the statute should be read in context of the Code in its entirety, and legislative history supports the finding that good-faith debtors retain post-petition, pre-conversion equity accrued in a home.

II. AVOIDANCE ACTIONS CANNOT BE SOLD BECAUSE THEY ARE RIGHTS AND POWERS OF A TRUSTEE THAT CANNOT BE INCLUDED WITHIN 11 U.S.C. § 541(A)'S DEFINITION OF PROPERTY OF THE ESTATE WITHOUT VIOLATING STATUTORY CONSTRUCTION PRINCIPLES.

A trustee's inability to sell avoidance actions is supported by the Code's statutory construct in Chapter 5, and designating avoidance powers as property of the estate would require a court to coexist with glaring surplusage within the Code. Additionally, avoidance actions are not property of the estate because a Chapter 7 trustee alone, as the estate's fiduciary, is granted the right and power to avoid transfers. Permitting such powers to be sold devalues the neutral role of a trustee and threatens the integrity of crucial bankruptcy principles. Lastly, avoidance actions cannot cross the threshold timing requirements established in § 541 as the debtor must have held an interest *before* the commencement of the case, or the estate must acquire an interest *after* the commencement of the case. Avoidance powers spring to life *upon* the commencement of the case, and do not, therefore, qualify as property of the estate under § 541. This Court should affirm the Thirteenth Circuit's decision because avoidance actions are not property of the estate as that term is unambiguously defined by the Code, and Congress exclusively vested avoidance powers in the bankruptcy estate's fiduciary.

A. Determining Avoidance Actions are Property of the Estate Would Create Surplusage and Would Require a Court to Overlook the Statutory Construction of Chapter 5.

When interpreting the language of a statute, the starting point is always the language of the statute itself. *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 197 (1976). Basic principles of statutory construction require that each word, clause, and section of a statute be given independent meaning whenever possible. *Parker Drilling Mgmt. Servs., Ltd. v. Newton*, 139 S. Ct. 1881, 1890 (2019). "[O]ne of the most basic interpretative canons" is that "'[a] statute should be construed so that effect is given to all its provisions, so that no part will be inoperative or superfluous, void or

insignificant.'" *Corley*,.556 U.S. at 314 (quoting *Hibbs v. Winn*, 542 U.S. 88, 101 (2004)). The sections of Chapter 5 governing avoidance actions consistently differentiate between a trustee's avoidance powers and a trustee's recovery of the property interests accrued as a result of avoided transfers. *Compare, e.g.,* 11 U.S.C. § 544 (empowering a trustee with the "strong arm power" to avoid transfers that would be voidable by a hypothetical bona fide purchaser or lien creditor) *with* §§ 550 (authorizing a trustee to recover the value of avoided property for the benefit of the estate) and 551 (automatically preserving, for the benefit of the estate, any transfer avoided by the trustee); *see also Suhar v. Burns (In re Burns)*, 322 F.3d 421, 425 (6th Cir. 2002) (explaining that avoidance allows trustees to nullify transfers that deplete the bankruptcy estate, but recovery "is a statutory mechanism through which property may be returned to the estate."). Overlooking this differentiation directly violates statutory construction principles and creates an absurd result within the bankruptcy process.

"The clear and unambiguous language of § 544 confers avoidance powers upon the trustee, not the debtor." *Hansen v. Green Tree Servicing, LLC* (*In re Hansen*), 332 B.R. 8, 12 (B.A.P. 10th Cir. 2005). The express language of this section does not refer to a debtor, and unlike Chapters 11 and 12, there is no provision in Chapter 7 expressly conferring debtors with the powers of a trustee. Instead, the language of § 544 is clear, and as this Court has repeatedly stated, when "the statute's language is plain, the sole function of the courts"—at least where the disposition required by the text is not absurd— "is to enforce it according to its terms." *United States v. Ron Pair Enters., Inc.,* 489 U.S. 235, 241 (1989). Section 550 provides in part that when a transfer is avoided under Chapter 5,[6] a trustee may recover "the property transferred, or, if the court so orders, the value of such property. . . ." 11 U.S.C. § 550. Correspondingly, § 541(a)(3) provides that any interest

[6] 11 U.S.C. §§ 544, 545, 547, 548, 549(a) (these sections are the general avoidance powers provided for by the Bankruptcy Code).

recovered by § 550 is property of the estate. Alternatively, under § 551, any transfer avoided is "preserved for the benefit of the estate . . . ." 11 U.S.C. § 551. Similarly, § 541(a)(4) is the correlating mechanism through which interests preserved under § 551 are included within property of the estate. Determining that avoidance powers are property of the estate by operation of law renders the language of §§ 550 and 551, and their correlating subsections in § 541, superfluous.

Both sections 550 and 551 contain the phrase "for the benefit of the estate." 11 U.S.C. §§ 550, 551. If avoidance actions themselves were property of the estate, this phrase would serve no purpose in either section. Instead, the cause of action to avoid any transfer would be owned and prosecuted by the estate, and any recovery from the cause of action would inure to the estate as the owner of the action. There would be no explanation for Congress's use of the phrase "for the benefit of the estate" that was not riddled with redundancies. As established and reinforced time and again, "[w]here Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion." *Duncan*, 533 U.S. at 173; *see also Essangui v. SLF V-2015 Trust* (*In re Essangui*), 573 B.R. 614, 622 (Bankr. D. Md. 2017) (stating "when Congress chooses to use different words in different places within a statute, that choice is intentional and conveys meaning."). As evidenced by the language of §§ 550 and 551, Congress clearly created avoidance powers to benefit the bankruptcy estate.

Moreover, were avoidance powers property of the estate, § 541(a)(6), which brings "[p]roceeds, product, offspring, rents, or profits of or from property of the estate" into the estate, would strip subsections (a)(3) and (a)(4) of any purpose. "Proceeds" under subsection (a)(6) includes income "derived from estate assets that form part of the estate," *United States v. Mitchell*, 476 F.3d 539, 544 (8th Cir. 2007), such that a judgment or recovery made on an estate's cause of

action under subsection (a)(1) is proceeds of that property. A trustee's recovery under § 550 or preservation of value under § 551 would, therefore, be proceeds of an avoidance action. This cause-and-effect results in unnecessary verbiage, and "[t]he canon against surplusage is strongest when an interpretation would render superfluous another part of the same statutory scheme." *City of Chicago v. Fulton*, 141 S. Ct. 585, 591 (2021).

The issue of superfluity continues when the same analysis is applied to § 541(a)(7), which includes "[a]ny interest in property *that the estate acquires* after the commencement of the case." 11 U.S.C. § 541(a)(7) (emphasis added). If avoidance powers are property of the estate, § 550 recoveries and § 551 preservations would constitute after-acquired property under § 541(a)(7). Again, subsections (a)(3) and (a)(4) would be rendered obsolete by this interpretation because they serve to escort property interests that are recovered or preserved by an avoidance action into the estate. By including a trustee's avoidance powers within property of the estate, this task has already been assigned to subsection (a)(7), and neither § 550 nor § 551 would be necessary.

A trustee's avoidance powers cannot be included within § 541's definition of property of the estate without also rendering other Code provisions – primarily, §§ 550 and 551 – superfluous. Based on the cardinal principles of statutory construction that Congress intends for every word, clause, and section to have meaning, such an interpretation does not conform to Congressional intent as evidenced by the plain language of the statute. The Thirteenth Circuit should be affirmed because determining avoidance powers are sellable property of the estate is a misinterpretation of the Code and contradicts clear Congressional intent.

B. Avoidance Powers Were Created for the Benefit of the Estate, and the Estate's Fiduciary Alone Has Standing to Bring Avoidance Actions.

i. Avoidance Powers were Created for the Benefit of the Estate and Must, Therefore, be Executed by the Estate's Fiduciary.

Avoidance powers exist solely to benefit the entire bankruptcy estate. *See* 11 U.S.C. § 550(a). "The concept of benefit to the estate includes benefit to administrative claimholders, secured claimholders, priority claimholders, as well as the general unsecureds." *Gordon v. Love (In re Pullen)*, No. 09-61108-MGD, 2013 WL 6000568, at *3 (Bankr. N.D. Ga. Nov. 10, 2013). While "[e]quality of distribution among creditors is a central policy of the Bankruptcy Code," *Begier v. I.R.S.*, 496 U.S. 53, 58 (1990), "[t]here is no requirement that an avoidance action recovery be distributed (or "committed") in whole or in part to creditors. *Trans World Airlines, Inc. v. Travellers Int'l AG* (*In re Trans World Airlines, Inc.*), 163 B.R. 964, 972 (Bankr. D. Del. 1994). Creditors are not guaranteed to receive a distribution of any funds from an avoided transfer. *See Centennial Indus., Inc. v. NCR Corp.* (*In re Centennial Indus., Inc.*), 12 B.R. 99, 102 (Bankr. S.D.N.Y. 1981) (finding, under the Bankruptcy Act, that unsecured creditors receiving some benefit from recovery of a preference, even if it was not an increase in what they would receive, was the operative question). In the context of a Chapter 7 liquidation case, exclusively granting the trustee avoidance powers prevents a "race to the courthouse by creditors and facilitate[s] equality of distribution among creditors." *Richardson v. Wells Fargo Bank* (*In re Churchill Nut Co.*), 251 B.R. 143, 149 (Bankr. N.D. Cal. 2000). Therefore, in Chapter 7 filings, a bankruptcy trustee is always appointed as the estate's fiduciary. 11 U.S.C. § 701(a).

To further the goal of benefitting the estate through avoidance actions, Congress exclusively assigned avoidance powers to the estate's fiduciary because "the U.S. trustees are responsible for protecting the public interest and ensuring that bankruptcy cases are conducted

according to law." *Adams v. Zarnel* (*In re Zarnel*), 619 F.3d 156, 162 (2d Cir. 2010). A Chapter 7 trustee serves to protect the integrity of the bankruptcy process and has a duty to "collect and reduce to money the property of the estate for which such trustee serves." 11 U.S.C. § 704(a)(1). A "primary role [of a chapter 7 trustee] in administering a debtor's bankruptcy estate is to liquidate property for the benefit of unsecured creditors." *In re Moreno*, 554 B.R. 504, 509 (Bankr. D.N.M. 2016). Chapter 5 repeatedly makes the point that avoidance powers are reserved rights and powers of the trustee. Those Chapter 5 provisions include the following:

- "The trustee shall have" the "rights and powers" of a lien creditor and "may avoid" transfers voidable by a lien creditor. 11 U.S.C. §544(a);
- "The trustee may avoid any transfer . . . ." 11 U.S.C. §544(b);
- "The trustee may . . . avoid" preferences. 11 U.S.C. §547(b);
- "The trustee may avoid" fraudulent conveyances. 11 U.S.C. §548(a)(1);
- "The trustee may avoid a transfer . . . ." 11 U.S.C. §549(a).

Several contextual features in Chapter 5 support the conclusion that exclusivity is intended. "First, a situation in which a statute authorizes specific action and designates a particular party empowered to take it is surely among the least appropriate in which to presume nonexclusivity." *Hartford Underwriters Ins. Co.*, 530 U.S. at 6–7. Here, as is statutorily required, the Trustee was appointed to Debtor's case upon conversion to Chapter 7. (R. at 8-9). Throughout Chapter 5, the trustee alone is granted the authority to avoid transfers as appropriate under the Code. *See* 11 U.S.C. §§ 544, 547, 548, and 549(a). "Where a statute . . . names the parties granted [the] right to invoke its provisions, . . . such parties only may act." *Hartford Underwriters Ins. Co.*, 530 U.S. at 7 (quoting 2A Norman J. Singer, *Sutherland on Statutory Construction* § 47.23, p. 217 (5th ed.1992) (internal quotation marks omitted)); *see also Fed. Election Comm'n v. Nat'l Conservative*

Political Action Comm., 470 U.S. 480, 486 (1985) ("The plain language of the Fund Act and the FECA suggests quite emphatically that the Democrats do not have standing to bring a private action against another private party."). Debtor does not dispute that the Trustee was empowered by the Code to take steps to liquidate his assets for the benefit of the estate. (R. at 9.)

"Second, the fact that the sole party named—the trustee—has a unique role in bankruptcy proceedings makes it entirely plausible that Congress would provide a power to him and not to others." *Hartford Underwriters Ins. Co.*, 530 U.S. at 7. "Congress knew how to give debtors avoidance powers (as evidenced by § 522(h)); Congress could also have expressly given 'debtors' the avoiding powers of § 544, § 545, § 547, § 548, and § 549(a). Instead, Congress expressly conferred the avoiding powers on the trustee." *In re Hansen*, 332 B.R. at 13. The Code authorizes the trustee alone to exercise these rights and powers, and for that reason, they are "generally deemed to be nonassignable." *Quad City Bank v. Chapman* (*In re Chapman Lumber Co.*), 343 B.R. 217, 220 (Bankr. N.D. Iowa 2006) (further stating "[i]ndividual creditors of the bankruptcy estate do not have standing to assert claims of voidable transfers.").

"The reasons [avoidance powers are preserved for the Chapter 7 trustee] are self-evident: The power to avoid a preference is one which is to be exercised in the interests of securing equality of distribution among creditors." *United Cap. Corp. v. Sapolin Paints, Inc*. (*In re Sapolin Paints, Inc.*), 11 B.R. 930, 937 (Bankr. E.D.N.Y. 1981) (referencing *Canright v. General Fin. Corp.*, 35 F.Supp. 841, 844 (E.D. Ill. 1940), *aff'd*, 123 F.2d 98 (7th Cir. 1941)); 4 Collier on Bankruptcy ¶ 547.01 (Lawrence P. King ed. 15th ed. 1980). Eclipse's offer to purchase the Trustee's potential preference claim against Debtor's mother (R. at 9) contradicts the Congressional intent behind the exclusivity of avoidance powers. Why third parties may not purchase preference claims from a neutral position is evidenced by Eclipse's possible motive of retribution and redemption. (R. at 9.)

Therefore, transferring rights and powers vested intentionally by Congress in a neutral party is a direct threat to the integrity created by the trustee's role. Congress intended such power to be granted to the estate's fiduciary alone, a fact stated and reemphasized throughout the Code.

ii. Congress Extended Independent Avoidance Standing to Chapter 11 Debtors in Possession, and Chapter 7 Debtors Do Not Enjoy the Same Right.

Congress exercised its ability and intent to extend avoidance powers when it created 11 U.S.C. § 1107(a), which states that "a debtor in possession shall have all the rights . . . and powers, and shall perform all the functions and duties . . . of a trustee serving in a case under this chapter." Because "there is no analogous provision applicable in Chapter 7," *Higgins v. Erickson* (*In re Higgins*), 270 B.R. 147, 153 (Bankr. S.D.N.Y. 2001), only the *trustee* or debtor in possession in Chapter 11 has *independent* standing to pursue Chapter 5 avoidance actions and other estate causes of action.[7]

Absent a specific statutory authorization in the Bankruptcy Code, a Chapter 7 debtor does not have the power to exercise the avoidance power in § 547 or § 550. This is consistent with the theory and purpose of preference avoidance, which is designed not to benefit the debtor but the bankruptcy estate. *Tronox Inc. v. Anadarko Petroleum Corp.* (*In re Tronox Inc.*), 464 B.R. 606, 614 (Bankr. S.D.N.Y. 2012). Section 547 makes it the trustee's responsibility to see that all property that may have been transferred to creditors during the preference period is recovered by the estate, to be divided equally among all unsecured creditors. The avoidance power is granted to the trustee so that the avoidance of transfers benefits the estate, and ultimately the remaining creditors, to the end that all creditors may recover on an equal, pro rata basis. *See* 5 Collier on

[7] 11 U.S.C. §§ 544, 545, 547, 548, 549(a), 550, 551 (these sections are the general avoidance and recovery powers provided for by the Bankruptcy Code).

Bankruptcy ¶ 547.11[2] at 547–95 (Lawrence P. King ed. 15th ed. rev. 1996) ("A debtor who is not a debtor in possession cannot maintain an action to set aside his or her own transfer as preferential under § 547."); *N.E. All. Fed. Credit Union v. Garcia (In re Garcia*), 260 B.R. 622, 635–36 (Bankr. D. Conn. 2001) ("[T]he Debtor-Defendants lack standing to void a pre-petition transfer since only a Trustee is authorized to bring such an action" (citing 11 U.S.C. § 547(b)); *In re White,* 258 B.R. 129, 131 (Bankr. D.N.J. 2001) ("Bankruptcy Code § 547(b), however, does not confer standing upon a debtor to avoid such transfers. Instead, § 547(b) grants the avoidance power solely to the bankruptcy trustee.").

That a Chapter 11 debtor in possession has standing to exercise Chapter 5 avoidance powers is also consistent with the purpose of Chapter 11 filings. In describing the purpose of Chapter 11, the Supreme Court has observed:

> In proceedings under the reorganization provisions of the Bankruptcy Code, a troubled enterprise may be restructured to enable it to operate successfully in the future. . . . . By permitting reorganization, Congress anticipated that the business would continue to provide jobs, to satisfy creditors' claims, and to produce a return for its owners. . . . . Congress presumed that the assets of the debtor would be more valuable if used in a rehabilitated business than if "sold for scrap."

United States v. Whiting Pools, Inc., 462 U.S. 198, 203 (1983) (citing H.R. Rep. No. 95–595, p. 220 (1977), *reprinted in* 1987 U.S. Code Cong. & Adm. News 5787, 6179). "Chapter 11 strikes a balance between a debtor's interest in reorganizing and restructuring its debts and the creditors' interest in maximizing the value of the bankruptcy estate." *Fla. Dep't of Rev. v. Piccadilly Cafeterias, Inc.,* 554 U.S. 33, 51 (2008) (*citing Toibb v. Radloff,* 501 U.S. 157, 163 (1991)). This balance furthers "Chapter 11's twin objectives of preserving going concerns and maximizing property available to satisfy creditors." *Id.* at 50 (*quoting Bank of Am. Nat'l Tr.t & Savs. Ass'n. v. 203 N. LaSalle St. P'ship,* 526 U.S. 434, 453 (1999) (internal quotation marks omitted)). Thus,

permitting a Chapter 11 debtor in possession to pursue avoidance actions under § 544 is not only logically connected to the purpose of Chapter 11 but is statutorily authorized by § 1107(a).

Allowing a debtor in possession to exercise avoidance powers furthers the foregoing goals of a Chapter 11 case, the dynamics of which are entirely different from those of a Chapter 7. In a Chapter 11 case, the default is that a Chapter 11 debtor will operate as a debtor in possession, and a trustee is appointed only "for cause" or "in the interests of creditors." 11 U.S.C. 1104(a). Unlike in Chapter 11, however, a trustee is always appointed in a Chapter 7 case. 11 U.S.C. 701(a). The trustee does not have the potential for conflicts of interest with creditors and other parties in interest as a debtor in possession sometimes has since the trustee has no prepetition relationship with the debtor's management, shareholders, or creditors. As noted by the Bankruptcy Court for the Northern District of Texas,

> [t]he trustee also is expected to be a gatekeeper and to exercise reasonable business judgment in deciding what actions to bring and what are not worth the expense. In theory at least (and hopefully in reality), the trustee is a fair, balanced, and experienced (not to mention bonded, *see* 11 U.S.C. § 322) official who can be depended upon to exercise good litigation judgment.

Reed v. Cooper (*In re Cooper*), 405 B.R. 801, 812 (Bankr. N.D. Tex. 2009).

Further, the trustee has a unique role and perspective as an independent fiduciary that is simply not comparable to either a debtor's or individual creditor's perspective: "Because of the unique role of a trustee, there would seem to be no equitable rationale to deviate from the Bankruptcy Code's apparent remedial scheme *vis-a-vis* avoidance actions and other estate causes of action." *Id*. If creditors do not like the job the trustee is doing, they can file a motion to compel him or her to act or a motion for removal of the trustee under 11 U.S.C. § 324. Such would not have been the case here, as the Trustee was performing her statutory duties, as evidenced by her commissioning an appraisal and marketing Mr. Clegg's home. (R. at 9.)

While it is clear that a Chapter 7 debtor does not have independent standing to bring forth avoidance actions, some bankruptcy courts have held creditors in Chapter 7 cases have derivative standing. *See, e.g., Hyundai Translead, Inc. v. Jackson Truck & Trailer Repair, Inc.* (*In re Trailer Source, Inc.*), 555 F.3d 231 (6th Cir. 2009); *PW Enters., Inc. v. N. Dakota Racing Comm'n* (*In re Racing Servs., Inc.*), 540 F.3d 892 (8th Cir. 2008); *Claridge Assocs., LLC v. Schepis* (*In re Pursuit Cap. Mgmt., LLC*), 595 B.R. 631 (Bankr. D. Del. 2018); *In re Dzierzawski*, 518 B.R. 415 (Bankr. E.D. Mich. 2014). As noted by the Eighth Circuit, "derivative standing is available to a creditor to pursue avoidance actions when it shows that a Chapter 7 trustee (or debtor-in-possession in the case of Chapter 11) is 'unable or unwilling' to do so." *In re Racing Servs., Inc.*, 540 F.3d at 898 (citing *Nangle v. Lauer (In re Lauer),* 98 F.3d 378, 388 (8th Cir.1996)). These courts have granted creditors derivative standing if they show "(1) it petitioned the trustee to bring the claims and the trustee refused; (2) its claims are colorable; (3) it sought permission from the bankruptcy court to initiate an adversary proceeding; and (4) the trustee unjustifiably refused to pursue the claims." *Id*. at 900.

However, even within this context, bankruptcy courts are rightly hesitant to grant derivative standing to creditors in Chapter 7 filings for an obvious reason: "If creditors could obtain derivative standing too readily, they 'could usurp the central role that the trustee or debtor-in-possession plays as the representative of the estate.'" *Id*. at 899-900 (quoting *Scott v. Nat'l Century Fin. Enters.* (*In re Baltimore Emergency Servs. II, Corp.),* 432 F.3d 557, 562 (4th Cir. 2005)). The need to reserve avoidance powers for a trustee (or Chapter 11 debtor in possession) is once again emphasized by the heightened standard of granting creditors derivative standing to bring Chapter 5 actions. Furthermore, this remedy is not supported by the statute; the appropriate remedy is for a creditor to file a motion to compel the trustee to pursue an avoidance action under 11 U.S.C. §

105. Allowing a creditor to stand in the shoes of a Chapter 7 trustee is synonymous with allowing a creditor to "'hijack' a Chapter 7 bankruptcy case in a manner Congress did not envision." *In re Cooper,* 405 B.R. at 807 (citing *Official Comm. Of Unsecured Creditors of Cybergenics Corp. v. Chinery,* 330 F.3d 548, 561 (3d Cir. 2003) (en banc)). It is "an unwise idea to allow a creditor to usurp the trustee's role as a representative of the estate—including being a gatekeeper for what actions make sense and the evaluator of the potential benefits of litigation. *Id.* at 813.

The Bankruptcy Code is clear: avoidance powers belong solely to the estate's fiduciary. Congress reiterated the exclusivity of this function when it granted the Chapter 11 debtor in possession as the estate's fiduciary, the power to avoid preferences. Congress did not confer avoidance powers to anyone but the trustee in Chapter 7 filings for two reasons. First, because a trustee is always assigned in Chapter 7 cases, avoidance powers are appropriately exercised according to their statutory purpose. Second, a remedy resolving any potential remission of avoidance actions already exists because third parties can file a motion to compel a trustee to act or, in the most egregious of cases, seek to remove the trustee under 11 U.S.C § 324.[8]

Section 544 clearly and unambiguously confers avoidance powers upon the trustee. Unlike in Chapter 11, Congress chose to not extend this power to a Chapter 7 debtor and made clear that avoidance powers are solely for the benefit of the Chapter 7 bankruptcy estate. The Thirteenth Circuit correctly held the Trustee's statutory authority to avoid and recover transfers under the Bankruptcy Code could not be sold to a third party. (R. at 24.) Therefore, its holding should be affirmed because the Code grants avoidance powers exclusively to the bankruptcy estate's

[8] After notice and hearing, a court may remove a Chapter 7 trustee "for cause." 11 U.S.C. § 324(a). While "cause" is not defined by the Code, most courts require "cause be something that both the law and sound public policy recognize as sufficient to warrant removing the trustee, and that relates to and affects the administration of the trustee's office." *In re United Tax Grp., LLC*, 622 B.R. 148, 156 (Bankr. D. Del. 2020). This is an extreme remedy because a trustee removed for "cause" in one case will be removed from all other cases in which the trustee is serving, "unless the court orders otherwise." 11 U.S.C. § 324(b).

fiduciary, Chapter 7 cases always have trustees assigned, and third parties do not have standing to bring avoidance actions.

C. A Trustee is Permitted to Sell Only Property of the Estate, and Avoidance Powers Do Not Fall within the Definition of Property of the Estate.

As previously discussed, the "estate is comprised of all the following property, wherever located: . . . all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a). Because subsection (a)(1) expressly includes "all legal or equitable interests of the debtor in property *as of the commencement* of the case[,]" 11 U.S.C. § 541(a)(1) (emphasis added), avoidance actions, which do not arise until a case is commenced, cannot overcome the temporal hurdle to fall within the definition of property of the estate.

"[The filing of] a petition 'creates an estate' that, with some exceptions, comprises 'all legal or equitable interests of the debtor in property as of the commencement of the case.'" *Fulton*, 141 S. Ct. at 587 (citing 11 U.S.C. § 541(a)(1)). Section 541 "generally compris[es] all of the debtor's property," *Law v. Siegel*, 571 U.S. 415, 417 (2014) (citing 11 U.S.C. § 541(a)(1)), but the "estate cannot possess anything more than the debtor itself did outside bankruptcy." *Mission Prod. Holdings, Inc. v. Tempnology, LLC*, 139 S. Ct. 1652, 1663 (2019) (citing 11 U.S.C. § 541(a)(1); *Bd. of Trade of Chicago v. Johnson*, 264 U.S. 1, 15 (1924)). Clearly, § 541(a)(1) unambiguously limits property of the estate to the debtor's property interests at the time of filing the bankruptcy petition, proceeds therefrom, or interests that *the estate* acquires post-petition. 11 U.S.C. § 541(a)(1), (a)(6), (a)(7) (emphasis added).

The Bankruptcy Code establishes the perimeters for property of the estate, but state law determines whether the debtor has a property interest in the first place. *Butner v. United States*, 440 U.S. 48, 54-55 (1979) (stating "Congress has generally left the determination of property rights in the assets of a bankrupt's estate to state law," and "[p]roperty interests are created and defined

by state law."). Therefore, to bring Chapter 5 avoidance actions within the estate under § 541(a)(1), the debtor must have some state- or federal-based interest in those types of actions. As this Court has previously held, "[w]hat constitutes a transfer and when it is complete' is a matter of federal law. This is unsurprising since . . . the statute itself provides a definition of 'transfer.' But the definition in turn includes references to parting with 'property' and 'interest in property.' In the absence of any controlling federal law, 'property' and 'interests in property' are creatures of state law." *Barnhill v. Johnson*, 503 U.S. 393, 397-98 (1992) (quoting *McKenzie v. Irving Tr. Co.*, 323 U.S. 365, 370 (1945)).

A trustee is vested with the power to avoid pre-petition transfers by the Code alone. *See* 11 U.S.C. §§ 544, 546, 547, 548, 549(a); *Saline State Bank v. Mahloch*, 834 F .2d 690, 694 (8th Cir. 1987). "Although the recovery of an avoided transfer certainly augments the estate, the trustee's ability to actually avoid the transfer is not an interest acquired from the debtor, but rather a power that derives from the Code itself." *Meoli v. Huntington Nat'l Bank* (*In re Teleservices Grp., Inc.*), 463 B.R. 28, 34 (Bankr. W.D. Mich. 2012). A trustee's avoidance powers are neither derived from nor related to a debtor's property interest because that property interest is nonexistent outside of the Code. *McKenzie*, 323 U.S. at 370.

While consulting legislative history is required when statutes are ambiguous, the Justices of this Court have routinely referred to legislative history during their decision-making process. *In re Butts*, 45 B.R. 34, 36 (Bankr. D.N.D. 1984). As explained by Justice Sotomayor,

> Legislative history can be particularly helpful when a statute is ambiguous or deals with especially complex matters. But even when, as here, a statute's meaning can clearly be discerned from its text, consulting reliable legislative history can still be useful, as it enables us to corroborate and fortify our understanding of the text. Moreover, confirming our construction of a statute by considering reliable legislative history shows respect for and promotes comity with a coequal branch of Government.

Digital Realty Tr., Inc. v. Somers, 583 U.S. 149, 171 (2018) (Sotomayor, J., concurring (citations omitted)). The legislative history for § 541 makes note of the broad scope of the definition of property of the estate but also makes clear that the definition was not designed to enlarge the debtor's rights against others beyond those existing at the commencement of the case. *N.S. Garrett & Sons v. Union Planters Nat'l Bank of Memphis* (*In re N.S. Garrott & Sons*), 772 F.2d 462, 465-466 (8th Cir. 1985) (citing S. Rep. No. 95-989, 95th Cong., 2d Sess. and H.R. Rep. No. 95-595, 95th Cong., 2d Sess. *reprinted in* 1978 U.S. Code Cong. & Adm. News 5868, 6323).

The Third Circuit Court of Appeals correctly distinguished causes of action belonging to the debtor at the time of filing a petition from causes of action arising once the Code becomes applicable. *In re Cybergenics Corp.*, 226 F.3d at 243. The *Cybergenics* court made clear that, even in a Chapter 11 context where the debtor in possession is empowered with the duties of a trustee pursuant to 11 U.S.C. § 1107(a),

> [t]he fact that section 544(b) authorizes a debtor in possession, such as Cybergenics, to avoid a transfer using a creditor's fraudulent transfer action does not mean that the fraudulent transfer action is actually an asset of the debtor in possession, nor should it be confused with the separate authority of a trustee or debtor in possession to pursue the prepetition debtor's causes of action that become property of the estate upon the filing of the bankruptcy petition.

Id.

As previously discussed, while causes of action belonging to the debtor at the commencement of the case are included within the definition of property of the estate, "[a]voidance actions accrue when a debtor commences a case by filing a bankruptcy petition." *Myers v. Raynor* (*In re Raynor*), 406 B.R. 375, 381 (B.A.P. 8th Cir. 2009), and not before then. Therefore, a debtor could not have an interest in avoidance actions arising under § 541(a)(1) "as of" the filing of his or her petition.

Additionally, like § 541(a)(1), a timing issue bars avoidance actions from being considered property of the estate under subsection (a)(7), which includes "any interest in property that the estate acquires after the commencement of the case." 11 U.S.C. § 541(a)(7). Simply, this subsection ushers property interests into the estate "*after* the commencement of the case." 11 U.S.C. § 541(a)(7) (emphasis added). A trustee's power to avoid transfers occurs simultaneously with the petition filing and is therefore untouched by subsection (a)(7). Because the power to avoid a transfer is not a property interest either before or after the commencement of the case, it is not property of the estate as defined by § 541. Therefore, this Court should affirm the Thirteenth Circuit's decision that a trustee's avoidance power is not property of the estate that can be sold to a third party.

CONCLUSION

Statutory construction principles require a court to apply statutes as written when the language is clear and to consult legislative history where ambiguity exists. The Thirteenth Circuit appropriately considered Congressional intent expressed in the legislative history of 11 U.S.C. § 348(f)(1)(A) because the term "property" could be interpreted in more ways than one. Based upon the overall scheme of the Bankruptcy Code and the relevant legislative history, the Thirteenth Circuit correctly interpreted the statute to read that post-petition, pre-conversion equity accrued in Mr. Clegg's home did not belong to the Chapter 7 estate upon conversion. The language of Chapter 5 pertaining to avoidance powers, however, contains no ambiguities. Therefore, the Thirteenth Circuit properly held a Chapter 7 trustee cannot sell avoidance powers because only the estate's fiduciary may exercise these powers, and they do not fall within the Code's definition of property of the estate. For the foregoing reasons, this Court should affirm the Thirteenth Circuit Court of Appeals on both issues.