No. 230115

IN THE

Supreme Court of the United States

IN RE EUGENE CLEGG, INC., DEBTOR

VERA LYNN FLOYD, CHAPTER 7 TRUSTEE, PETITIONER

V.

EUGENE CLEGG, RESPONDENT.

Brief for Petitioner

Team Number 11

January 18, 2024 — Counsel for Petitioner

QUESTIONS PRESENTED

I. Whether any post-petition, pre-conversion increase in equity in a debtor's property 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 and 541.

II. Whether a chapter 7 trustee may sell, as property of the bankruptcy estate, the ability to avoid and recover transfers pursuant to 11 U.S.C. §§ 547 and 550.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

United States Supreme Court Cases

Federal Court of Appeals Cases

Federal Bankruptcy Courts

Statutes

Other Authorities

OPINIONS BELOW

The Thirteenth Circuit Court of Appeals' decision is available at No. 23-0115 and reprinted starting at Record 2. The United States Bankruptcy Court for the District of Moot decided in favor of debtor Eugene Clegg. On appeal, the United States Court of Appeals for the Thirteenth Circuit affirmed.

STATEMENT OF JURISDICTION

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

RELEVANT STATUTORY PROVISIONS

The relevant federal provisions controlling this case are 11 U.S.C. §§ 105(a), 348(f)(1), 541(a), 547(b), 550(a). These provisions are attached in Appendix A.

STATEMENT OF THE CASE

This appeal comes about from Respondent's attempts to hold that the all-encompassing nature of the bankruptcy estate should be unnecessarily restricted against statutory and judicial interpretation holding to the contrary to the detriment of the Chapter 7 estate.

I. FACTUAL HISTORY

Eugene Clegg ("Debtor") is the owner of The Final Cut, LLC ("Final Cut"), which owned and operated a long-standing movie theater in the City of Moot. R. at 5. Final Cut has historically been profitable, and in 2016 borrowed $850,000 ("Loan") from Eclipse Credit Union ("Eclipse") in order to renovate the theater. Eclipse was granted first priority liens on the property of Final Cut, and the debtor issued an unsecured personal guarantee as security of the loan. *Id.*

The loan was exhausted through these renovations as well as a $75,000 charitable donation to the Veterans of Foreign Wars ("VFW"). *Id.* The theater continued to be profitable until March of 2020, when the Covid-19 pandemic and subsequent stay at home measures issued by the State of Moot halted operation of the theater. *Id.* at 6. Without any income from the theater, debtor received an unsecured loan in the amount of $50,000 from his mother, Pink. When the theater reopened the following year, it remained unprofitable, and the debtor incurred credit card debt while falling behind on his mortgage provided by Another Brick in the Wall Financial Corporation ("Servicer"), who initiated foreclosure proceedings on debtor's home. *Id.*

In summary, debtor, at the time of filing for bankruptcy, owed three separate debts to three separate creditors: An unsecured debt to Pink in the amount of $50,000, a contingent and unsecured debt in an unknown amount to Eclipse, and a non-contingent, liquidated, secured debt to Servicer in the amount of $320,000.

II. PROCEDURAL HISTORY

Debtor filed for relief under Chapter 13 of the Bankruptcy Code on December 8, 2021 ("Petition Date"). R. at 6. The Debtor disclosed his financial obligations to Eclipse and the Servicer, as well as a valuation of his home at $350,000, a claim for a state law homestead exemption in the amount of $30,000, and a preferential transfer to Pink made one year prior to the petition date in the amount of $20,000. *Id.* at 6-7. Debtor's chapter 13 plan outlined that payments would be made to creditor's over a three-year period. *Id.* at 7. It further stated that, given his indebtedness with regards to his mortgage and the claimed homestead exemption, the debtor held no equity in the home. *Id.* In order to rectify the preferential transfer to Pink, the debtor agreed to increase the aggregate payments to creditors by $20,000 in exchange for the chapter 13 trustee agreeing to not avoid and recover said preferential payments from Pink. *Id.*

Learning that debtor had used the last of his loan to donate to the VFW, Eclipse filed an adversary proceeding to declare his debt regarding the loan non-dischargeable under section 11 U.S.C. § 523(a)(2)(A). *Id.* This objection was withdrawn after settling on an estimated claim in the amount of $150,000 with $25,000 being deemed non-dischargeable. *Id.* at 8. The plan was confirmed by the bankruptcy court on February 12, 2022, incorporating the debtor's agreement with the Chapter 13 trustee. *Id.* The settlement between debtor and Eclipse was also approved, though separately from the plan. *Id.*

The debtor made timely payments until September of 2022, and Final Cut closed its doors permanently in October. *Id.* The debtor had the case converted to chapter 7 pursuant to 11 U.S.C. §§ 348 and 1307, with the chapter 13 trustee declaring in her final report that $10,000 had been distributed to the Servicer. *Id.* The funds held in reserve for Eclipse were likewise returned to the debtor upon conversion. *Id.* at 9.

Vera Lynn Floyd was appointed as the trustee of the debtor's chapter 7 estate *Id.* The conversion petition again disclosed the value of his home and the preferential transfers to pink, as well as an indebtedness to Eclipse in the amount of $200,000 and a desire to reaffirm his mortgage debt with the Servicere. *Id.* The trustee commissioned an appraisal of the debtor's home which found that its equity had increased by $100,000 since the petition date. *Id.* After putting up the home for sale to liquidate the assets to the benefit of the creditors, Eclipse offered to purchase both the home and the avoidance action against Pink for $470,000. *Id.* Satisfied with this offer, the trustee moved to sell the home and the preference claim to Eclipse under 11 U.S.C. § 363(b). *Id.*

The debtor objected to this sale motion, arguing that (1) any post-petition, pre-conversion increase in equity in a debtor's property inures to their benefit upon conversion of a case from chapter 13 to chapter 7 pursuant to 11 U.S.C. §§ 348 and 541, and (2) a chapter 7 trustee may not sell, as property of the bankruptcy estate, the ability to avoid and recover transfers pursuant to 11 U.S.C. §§ 547 and 550. *Id*. at 10. The bankruptcy court ruled in favor of the debtor on both counts, and Ms. Lynn filed an appeal to the United States Circuit Court for the Thirteenth Circuit, which similarly ruled in favor of the debtor. *Id*. at 10-24.

STANDARD OF REVIEW

The parties do not dispute the facts set forth in this record. Both issues presented before the court are issues of law. Therefore, this court is bound by a *de novo* standard of review. *See, e.g., Fox v. Hathaway (In re Chicago Mgmt. Consulting Grp.)*, 929 F.3d 804, 809 (7th Cir. 2019) "Under a de novo standard of review, the reviewing court decides an issue as if the court were the original trial court in the matter." *See, e.g., Razavi v. Comm'r of Internal Revenue*, 74 F.3d 125, 127 (6th Cir. 1996)

SUMMARY OF THE ARGUMENT

This Court should overturn the decision of the Thirteenth Circuit Court of Appeals because the appreciation in the equity in a debtor's property that occurs post-petition, but before conversion to a Chapter 7 case, inures to the benefit of the bankruptcy estate.

Where the language of a statute is plain, the court's only responsibility is to enforce the provision as written. Section 348(f)(1)(A) provides that the property of the estate in a converted case consists of the property of the estate as of the petition date of the original Chapter 13 case that remains in the control of the debtor. Property of the estate is clearly and broadly defined by section 541(a) of the Bankruptcy Code, and as such, any property newly acquired or any proceeds newly received by the debtor are not included in the converted Chapter 7 case. However, an appreciation in the value of a piece of property already in the estate as of the petition date is not a separate, newly acquired property interest. This appreciation in equity is part of the estate, per sections 348(f)(1)(A) and 541(a), and will be sold by the Chapter 7 trustee, with the sale proceeds distributed to the creditors.

As the language of the Code is unambiguous, this Court should not rely upon the legislative history of section 348(f)(1) in its decision. Moreover, the case law further interpreting 348(f)(1) has observed that the legislative history concerns the issue of newly acquired property, and does not apply at all to the appreciation in value of a piece of property already belonging to the estate.

With respect to the sale of the ability to avoid and recover transfers pursuant to sections 547 and 550, this Court should additionally overturn the decision of the Thirteenth Circuit Court of Appeals and include, as property of the chapter 7 bankruptcy subject to liquidation, the trustee's statutory ability to to avoid and recover preferential transfers, generally referred to as chapter 5 avoidance powers.

Above all else, a chapter 7 trustee has the responsibility of maximizing the value of the estate to the benefit of the parties involved. To facilitate this, courts and the Bankruptcy Code itself construe the estate's property widely to embrace as much equity as possible. This is outlined explicitly by section 704(a)(1) and provides for an estate that is "all-embracing" to include intangible property interests such as statutory causes of action. Indeed, courts throughout the country have given permission for such inclusion should it serve the interests of the estate. Section 541(a) of the Bankruptcy Code further accounts for such breadth to directly include "all legal or equitable interests" held by the debtor not subject to any listed exemption. A bankruptcy cause of action is demonstrably such an interest that exists beyond just the trustee and should thus be accounted for in the liquidatable equity of the estate.

The trustee, as the arbiter of the estate and its liquidation, should be permitted to transfer causes of action such as avoidance powers in order to effectively and efficiently pay creditors without incurring significant administrative expense. In the present case, the funds provided to the estate in the sale of both the home and the preference claim ensure that Pink stands to benefit far more than she otherwise would have had the chapter 7 trustee pursued the action or waived it. As such, the benefit to the estate vastly outweighs any reservations one may hold regarding a creditor unduly benefitting at the expense of another.

For the foregoing reasons, both the post-petition, pre-conversion increase in equity to the debtor's home as well as the trustee's chapter 5 preference claim should be included in the chapter 7 estate and salable therein.

ARGUMENT

I. <u>Post-Petition, Pre-Conversion Appreciation in the Equity in a Debtor's Property Belongs to the Chapter 7 Bankruptcy Estate</u>

A. Appreciation in the Equity in a Debtor's Property Does Not Create a New, Distinct Interest in a Piece of Property

The plain language of Section 348(f)(1)(A) and the broad reach of Section 541(a) of the Bankruptcy Code mandate that any appreciation in value of an asset of the estate inures to the benefit of the bankruptcy estate, not the debtor. As the Supreme Court explained in *United States v. Ron Pair Enters., Inc.*, "[t]he task of resolving the dispute . . . begins where all such inquiries must begin: with the language of the statute itself . . . [I]t is also where the inquiry should end, for where . . . the statute's language is plain, 'the sole function of the courts is to enforce it according to its terms.'" 489 U.S. 235, 241 (1989) (*See also Castleman v. Burman (In re Castleman)*, 75 F.4th 1052, 1057 (9th Cir. 2023) "[T]he existence of a division of judicial authority does not itself establish ambiguity in the text.") The provision in question, Section 348(f)(1)(A) of the Bankruptcy Code, states that "property of the estate in the converted case shall consist of property of the estate, as of the date of the filing of the petition, that remains in the possession of or is under control of the debtor on the date of conversion[.]" 11 U.S.C. § 348(f)(1)(A). Section 348 does not define "property of the estate," but under Section 541(a)(1), "filing for bankruptcy creates an estate which includes 'all legal or equitable interests of the debtor in property as of the commencement of the case.'" *In re Castleman*, 75 F.4th at 1056 (quoting 11 U.S.C. § 541(a)). The estate also includes the "[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." § 541(a)(6). Further, 11 U.S.C. § 541(b) exempts certain property of the debtor from the estate.

Section 348(f)(1) is not ambiguous, as property of the estate "includes all debtor's interest, both legal and equitable, with some exceptions not applicable here." *Goetz v. Weber (In re Goetz)*, 651 B.R. 292, 299 (B.A.P. 8th Cir. 2023). Similar to the circumstances in *Goetz*, as of the petition date, the Debtor's home became part of the bankruptcy estate, and the record shows no evidence of bad faith. R. 6. Throughout the Chapter 13 case, and upon the conversion of the case to Chapter 7, the home remained in the control and possession of the Debtor. *Id*. The Debtor also properly claimed a state law homestead exemption in the amount of 30,000. *Id*.

The Debtor's home is an asset that is part of the bankruptcy estate under sections 348(f)(1)(A) and 541(a), as it is an equitable interest in property, and any increase in the value of a piece of a property is "an attribute or incident of the property, not a separate right or interest in the property. *In re Adams*, 641 B.R. 147, 151 (Bankr. W.D. Mich. 2022). Although 11 U.S.C. § 1327 provides that confirmation of the Chapter 13 plan "vests all of the property of the [bankruptcy] estate in the debtor," the Supreme Court clarified that "when a debtor exercises his statutory right to convert, the case is placed under Chapter 7's governance, and no Chapter 13 provision holds sway." *Harris v. Viegelahn*, 575 U.S. 510, 520 (2015) (*see also* § 103(i), "Chapter 13 . . . applies only in a case under [that] chapter")[1]. Additionally, "where Congress wanted to exclude assets or certain interests of the debtor from the bankruptcy estate, it had done with specificity. *See, e.g.*, § 541(a)(6) (excluding post-petition earnings by an individual in a Chapter 7 case.") *In re Castleman,* 75 F.4th at 1057. As the dissenting opinion in the lower court aptly

[1] In the context of a Chapter 7 case that has not been converted, courts find that an appreciation in equity inures to the benefit of the estate. *See Coslow v. Reisz,* 811 Fed.Appx. 980, 984 (6th Cir. 2020); *Hyman v. Plotkin (In re Hyman)* 967 F.2d 1316, 1321 (9th Cir. 1992) ("Were we to accept the Hymans' argument that they're entitled to post-filing appreciation, we would also have to hold that a debtor is subject to post-filing depreciation, which would give debtors in falling property markets less than the [homestead exemption] guaranteed them by state law."); *In re Lents,* 644 B.R. 479, 489 (Bankr. D.S.C. 2022); *In re Ostendorf,* 2011 WL 1060992, at *1 (Bankr. D. Neb. Mar. 23, 2011); *In re Moyer,* 421 B.R. 587, 594 (Bankr. S.D. Ga. 2007); *In re Shipman,* 344 B.R. 493, 495 (Bankr. N.D. W.Va. 2006).

explained, "the statute does not limit the subsequent chapter 7 estate to the 'equity in' or the 'value of' the property as of the filing of the chapter 13 petition." R. at 28 (citing *In re Peter,* 309 B.R. 792, 795 (Bankr. D. Or. 2004).

In *Castleman*, the Debtors listed their home with a value of $500,000, a mortgage with an outstanding balance of $375,077, and a homestead exemption of $124,923. 75 F.4th at 1054. The Castlemans could not complete their Chapter 13 plan and converted to Chapter 7, at which time their home had risen in value by an estimated $200,000. *Id*. The court considered arguments that the equity belonged to the Debtors but ruled that "the broad definition of 'property of the estate' in § 541(a) 'captures the debtor's entire ownership interest in each asset that exists on the petition date without fixing the estate's interest to the precise characteristics the asset has on that date.'" *Id*. at 1057 (quoting *In re Goetz*, 651 B.R. at 416.).

Similar to *Castleman,* the Debtor in the present case listed the value of his home as $350,000 on his Schedules, as well as a non-contingent, liquidated and undisputed secured debt to the Servicer in the amount of $320,000, and a homestead exemption in the amount of $30,000. R. 6. The lower court argues that *Castleman* is not persuasive because of its reliance on the decisions from *Schwaber v. Reed (In re Reed),* 940 F.2d 1317 (9th Cir. 1991) and *Wilson v. Rigby*, 909 F.3d 306 (9th Cir. 2018), as well as—in the lower court's view—an incomplete reading of the statutory text. However, the decisions in both *Reed* and *Wilson* are only unpersuasive based on the reasoning that an appreciation in the value of property creates a new property interest and is not an equitable interest that is property of the estate under 541(a). 541(a) governs what is included in property of the estate, and "[e]quity is merely a descriptive term for that portion of a debtor's property which represents value in excess of encumbrances." *In re Hayes,* No. 15-20727, 2019 Bankr. LEXIS 4203, at *9, *14 (Bankr. D. Colo. Mar. 28, 2019). As such, "[n]othing in Section 541 suggests that the estate's interest is anything less than the entire asset, including any changes in its value which might occur after the date of filing." *Potter v. Drewes (In re Potter),* 228 B.R. 422, 424 (B.A.P. 8th Cir. 1999).

In reaching their conclusion that any post-petition, pre conversion appreciation in property of the estate should inure to the benefit of the debtor, the lower court claims there exists a conflict in the statutory scheme between section 348(f)(1)(A) and both sections 348(f)(2) and section 522. However, this interpretation is flawed as the lower court does not follow the authority from the Supreme Court and other circuits that Section 541 governs what is property of the estate and includes all legal and equitable interests of the debtor. § 541(a)(1). First, the lower court explained, "If Congress had truly intended to include post-petition, pre-conversion interests in property—such as the increase in the Debtor's home—as property of the estate under Section 348(f)(1)(A), it would not have needed to enact section 348(f)(2)." R. at 13. However, the bad faith provision is not in conflict with Section 348(f)(1)(A), it just does not apply. As the court said in *Goetz,*

> In enacting section 348(f), Congress distinguished between property of the estate at the time of conversion that remains in the possession or control of the debtor from property acquired after the petition. The former is property of the estate (Goetz's residence), the latter is property of debtor unless she converted in bad faith. The bad faith provision neither hinders nor advances Goetz's claim to the equity increase in her residence.

651 B.R. at 302.

This reasoning applies to our case. The increase in equity is not a separate property interest that would put section 348(f)(1)(A) in conflict with 348(f)(2), but simply an attribute of the property that is part of the estate. The lower court further claims that Section 522 is in conflict with the Trustee's interpretation because if, "section 348(f)(1)(A) is not similarly subject to a snapshot rule, the Bankruptcy Code would be rendered nonsensical in that it could result in vastly different valuations as to the same property." R. at 14. However, the only case the lower court cites as support for this assertion is *Rockwell v. Hull,* 968 F.3d 12 (1st Cir. 2020). In *Rockwell,* the court adopted the snapshot rule in a completely different circumstance, explaining, "When the snapshot rule applies to an asset and the snapshot is 'complete,' the asset will retain whatever status (i.e., exempt or part of the estate) it had when the debtor filed for bankruptcy and cannot be altered by circumstances that change later." *Id*. at 19. Thus, the snapshot rule that the lower court cites applies to how exemptions are evaluated by focusing on what the property was at the petition date. Furthermore, other courts have recognized the capacity for change in the valuation of property that is part of the estate. *See In re Paolella,* 85 B.R. 974, 977 (Bankr. E.D. Pa. 1988) ("[B]ecause sale does not generally, if ever, occur simultaneously with the formation of a 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 post-petition.").

B. Even if Section 348(f)(1) was Ambiguous on its Face, the Legislative History is not Dispositive of the Issue

Even if the statute was ambiguous on its face, the legislative history of 348(f)(1) does not mandate a different outcome, as the lower court argues. "The plain meaning of a statute is conclusive, except in the 'rare cases [in which] the literal application of a statute will produce a result demonstrably at odds with the intentions of its drafters.'" *Goetz,* 651 B.R. at 302 (quoting *Griffin v. Oceanic Contractors, Inc.,* 485 U.S. 564, 571 (1982)); *see also* Megan McDermott, *Justice Scalia's Jurisprudence: The Right Judicial Philosophy for the Modern Bankruptcy Code?*, 5 UTAH L. REV. 939, 975 (2017) ("The legislative history of bankruptcy laws may be particularly problematic, as it tends to reflect highly specialized interests rather than those of the main stakeholders in bankruptcy."). Section 348(f) is consistent with the legislative intent. *Id*. First, "the legislature's intent in enacting section 348(f)(1) was to overrule an interpretation of the statute by some courts who had held that property that the debtor *first acquired* during the course of his or her chapter 13 case became property of the chapter 7 case upon conversion." R. at 28 (citing H.R. Rep. No. 103-835, at 57 (1994), *as reprinted in* 1994 U.S.C.C.A.N. 3340, 3366). To support their proposition that the legislative history supports post-petition, pre-conversion equity inuring to the benefit of the debtor, the lower court cites *Rodriguez v. Barrera (In re Barrera),* 22 F.4th 1217 (10th Cir. 2022). However, *Barrera* addresses a situation where the debtor sold their home during the chapter 13 proceedings and the case centered on which party was entitled to the proceeds from the sale. The court concluded that, "[b]ased on the plain language of § 348(f)(1)(A), then, the sale proceeds—a property interest distinct from the physical house from which they were derived—do not enter the converted Chapter 7 estate." *Id*. at 1224. By its own language, the court admits section 348(f)(1)(A) has a plain meaning, and any property newly acquired after the petition date would inure to the benefit of the debtor, and not the estate. Moreover, "the proceeds from the sale of the physical house 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.* (citing David Carlson, *The Chapter 13 Estate and its Discontents*, 17 Am. Bankr. Inst. L. Rev. 233, 280 (2009)).

The legislative history and case law support relied on by the lower court do not apply in our case. Both concern the issue of property newly acquired after the petition date, not a change in the aspect of a piece of property already belonging to the estate and in control by the debtor as of the conversion date. The lower court also relies upon a factual scenario discussed by the House Report where, during a Chapter 13 case, a home's value appreciates. Reliance on this example is flawed for two reasons. First, as the court in *In re Goins* states, the example, "arguably sheds light on 'paydown' cases, i.e., the cases where the Debtor creates equity by paying down secured debt during the courts of the case . . . [i]t is not helpful, however, in determining which party, the Debtor or the Trustee, is entitled to the equity created by appreciation of the property while the Debtor is in Chapter 13." 539 B.R. 510, 516 (Bankr. E.D. Va. 2015) (citing H.R. Rep. No. 103-835 at 57 (1994), as reprinted in 1994 U.S.C.C.A.N. 3340, 3366). Second, this example was not included in the statutory text. The reasoning provided by the court in *Goetz* illustrates this issue well:

> Congress's failure to address the example included in the legislative history does not mean this omission was inadvertent. Recognizing that statutes are often the result of compromise, we decline to accept [the debtor's] invitation to assume that Congress intended that debtors may retain post petition pre conversion market appreciation and equity resulting from debt payments without language articulating this intent.

651 B. R. at 299.

"Chapter 7 allows a debtor to make a clean break from his financial past, but at a steep price: prompt liquidation of the debtor's assets." *Harris,* 575 U.S. at 513. Although the outcome for a debtor who originally sought to keep his home through Chapter 13 may be unfavorable, section 348(f)(1) of the United States Bankruptcy Code plainly mandates that any appreciation in the value of property of the estate inures to the benefit of the estate. From there, a "Chapter 7 trustee is then charged with selling the property in the estate, § 704(a)(1), and distributing the proceeds to the debtor's creditors, § 726." *Id*.

II. The Ability to Avoid and Recover Transfers Pursuant to 11 U.S.C. §§ 547 and 550 is Property of the Chapter 7 Estate that May be Sold and Transferred by the Trustee

As a matter of law, a trustee of an estate under any bankruptcy chapter may, in accordance with the U.S. Bankruptcy Code, avoid any transfers made by the debtor to a creditor prior to the commencement date and recover such payments to the benefit of the bankruptcy estate pursuant to 11 U.S.C. §547(b) and 11 U.S.C. §550(a) respectively. This ability is colloquially referred to as a trustee's chapter 5 causes of action, or more specifically "avoidance powers," and are vital to ensure that payments to creditors during a bankruptcy proceeding are distributed without preference. *Union Bank v. Wolas*, 502 U.S. 151 (1991); *Bergier v. IRS*, 496 U.S. 53, 58 (1990).

A trustee may only liquidate property of the chapter 7 bankruptcy estate to make payments to creditors. 11 U.S.C. §704(a)(1). As such, for the trustee to sell and assign avoidance powers, it is crucial that we demonstrate that they constitute property of the estate. The lower court held that there is no statutory basis to uphold this interpretation, and that assigning avoidance powers would lead to results that are opposed to, if not antagonistic to, the goal of the Bankruptcy Code. On the contrary, chapter 5 causes of action have historically been recognized as property of the estate created upon the filing of a bankruptcy petition and the ability to reduce these actions to money is in the best interest of the estate and the parties involved in the current proceeding.

The Bankruptcy Code is widely interpreted as holding two central aims: to relieve debtors of their financial obligations while maximizing total creditor return on debts. The sale and transfer of the trustee's avoidance powers works to accomplish both goals.

A. The Chapter 7 Trustee has a Statutory Duty to Maximize Payment to Creditors Under 11 U.S.C. §704(a)(1) and Interpreting the Estate as "All Embracing" Accomplishes this Goal.

The Bankruptcy Code explicitly outlines the duties of a chapter 7 trustee in facilitating bankruptcy proceedings. Specifically, it states that a chapter 7 trustee *shall "*close such estate as expeditiously as is compatible with the best interests of the party." 11 U.S.C. §704(a)(1). This provision is widely understood in the eyes of courts throughout the country to convey a statutory obligation upon the trustee to maximize the value of the estate on behalf of creditors. *See*, *Commodity Futures Trading Comm'n v. Weintraub*, 471 U.S. 343, 352 (1985); *Martin v. Martin (In re Martin)*, 91 F.3d 389, 394 (3d Cir. 1996); *Nelson v. A-C Product Liability Trust*, 549 B.R. 87, 98 n.9 (Bankr. E.D. Penn. 2016). This axiom clearly underlies the entirety of the Bankruptcy

Code and serves to further one of the primary aims of bankruptcy as a legal mechanism to provide to creditors what is owed – that being as much as is not statutorily restricted.

The lower court was correct in stating that the Bankruptcy Code is "to be read as a whole." *King v. St. Vincent's Hosp.*, 502 U.S. 215, 221 (1991). The statutory goal of maximizing the value of the estate in a bankruptcy proceeding comports with the all-embracing nature of the estate itself. Section 541 of the Bankruptcy Code defines what is to be included, or perhaps more accurately, what explicitly is *not* to be included. Much of section 541 is dedicated to the specified exclusions of the bankruptcy estate, whereas what is included is largely encompassed in broad strokes by section 541(a) as the inclusion of "all legal or equitable interests" as of the commencement of the case. 11 U.S.C. §541(a); *see also Parker v. Goodman (in re parker),* 499 F.3d 616, 624 (6th circuit 2007). Generally, pursuant to 11 U.S.C. §102, "including" is not to be construed as a limitation, and we must therefore defer to exceptions whenever possible to decide what is not included in the estate. While the text of the statute speaks for itself, this reading seemingly falls in line with the legislative history therein. *See* H.R. Rep No. 95-595 at 549 (1977). The purpose of this language is clear – including as much property as possible in the estate, and thereby maximizing its value in the best interest of creditors, is in the best interest of the estate.

The exclusionary specificity of section 541 is important, as courts often exclude property from the estate solely if it falls under one of the listed exceptions. In *Patterson v. Shumate*, a debtor's interest in a pension plan under the Employee Retirement Income Security Act of 1974 (ERISA) was restricted from the debtor's bankruptcy estate not because it was not a "legal or equitable interest," but because restricting it from being included was "enforceable under applicable nonbankruptcy law" as is outlined as an exception under section 541(c)(2). *Patterson v. Shumate*, 504 U.S. 753, 758 (1992); 11 U.S.C. §541(c)(2). The lower court does not follow this line of interpretation of section 541, instead choosing to exclude an interest because of its omission rather than its inclusion as a listed exception. R. at 19. Section 541 should not be read as a "limitation" but a clarification of the "definition of what is included in the estate." *U.S. v. Whiting Pools, Inc.*, 462 U.S. 198, 203 (1983). The *Patterson* court did not equivocate in this regard – the estate is summarily intended to be "broad." 504 U.S. 753, 757. The lower court's interpretation is contrary to the all-encompassing language of the section as well as the relevant case law regarding what is to be included in the estate.

B. Bankruptcy Causes of Action Have Long Been Recognized as Property of the Estate that may be Liquidated on its Behalf.

Because the basis for what is to be included in the bankruptcy estate starts and often ends barring a listed exception with "legal or equitable interest," it is imperative to establish whether causes of action such as avoidance powers fall under this broad definition. Fortunately, there is no jurisprudential dearth of answers to this question. Various causes of action, from those included explicitly in the Bankruptcy Code to those that exist under state law, have been recognized definitively as property of the estate. *See Whiting Pools, Inc.*, 462 U.S. 198; *Cadle Co. v. Mims (in re Moore)*, 608 F.3d 253 (5th Cir. 2010), *Pitman Farms v. ARKK FOOD CO., LLC (In re Simply Essentials)*, 78 F.4th 1006 (8th Cir. 2023), *Duckor Spradling & Metzger v. Baum Trust (In re. P.R.T.C., Inc.)*, 177 F.3d 774 (9th Cir. 1999), *United States v. Nordic Vill., Inc.*, 503 U.S. 30 (1992). Clearly, causes of action were not uniformly intended to be exempt from property of the estate.

The basis for *which* causes of action may constitute property of the estate is the subject of some debate. However, including avoidance powers in this definition seems to comport with the language and purpose of the Bankruptcy Code. The Southern District of New York put it most succinctly by holding that "Property of the estate… includes any cause of action the debtor had on the petition date as well as avoidance actions created on the petition date." *Sec. Inv'r Prot. Corp. v. Bernard L. Madoff Inv. Sec, LLC*, 460 B.R. 106 (Bankr. S.D. N.Y. 2011) (citing *Jackson v. Novak,* 593 F.3d 171 at 176 (2nd cir. 2010) and *Delgado Oil, Inc. v. Torres*, 785 F.2d 857 (10th cir. 1986)). The lack of cross-reference to section 547 in section 541(a) should not be dispositive – section 541 provides exceptions with specificity while broadening inclusions as much as possible with the term "all legal or equitable interests." *Shumate*, 504 U.S. 753, 757. Because section 541 provides that the estate be all-encompassing, and because causes of action are undoubtedly a "legal or equitable interest" without any listed exception, avoidance causes of actions should be included in the estate barring any statutory or implicit exemption.

i. The Trustee is Not the Sole Party Holding an Interest in Avoidance Actions According to 11 U.S.C. §522(h) and 11 U.S.C. §503(b)(3)(B).

The lower court points out that property of the estate may only include these legal or equitable interests that existed "as of the commencement of the estate" under 11 U.S.C. §541(a)(1) as justification for exclusion from the estate. R. at 20. However, because the debtor "has an inchoate interest in the avoidance actions prior to the commencement of the bankruptcy proceedings," avoidance actions clearly fall under the statutory definition established by section 541(a)(1). *In re Simply Essentials,* 78 F.4th 1006, 1009. The lower court's dismissal of this case relies on the false assumption that *In re Simply Essentials* delineates the funds of the preferential transfer and the avoidance action itself as separate property interests and only allows for the former to be included in the estate, but the eighth circuit could not have been more clear – "avoidance actions are property of the estate under section 541(a)(1)." *Id*. To understand this, it behooves us to precisely define what a property interest is – it is not necessarily the physical ownership of a piece of property, but "includes the right to possess and to use it." T. Plank, *The Outer Boundaries of the Bankruptcy Estate*, 47 Emory L.J. 1193, 1214-1215 (1998). The debtor maintains an interest in those funds *and* the transfer of those funds into the estate, both of which are embodied under the trustee's avoidance powers. Therefore, they are a "legal or equitable interest" that constitute property of the estate under section 541(a).

The debtor's interest in a trustee's avoidance power is not only inchoate or theoretical – it is practicable in many instances. The lower court held that because sections 547 and 550 explicitly grant avoidance power to the trustee, they clearly intended only for the trustee and no one else to exercise this power. 11 U.S.C. §547(b), 11 U.S.C. §550(a). The basis for this logic is found in *Hartford Underwriters Ins. Co v. Union Planters Bank*, *N.A. ("Hen House")*, 530 U.S. 1, 6-7 (2000), wherein an administrative claimant was barred from recovering payments from a debtor's collateral in a chapter 11 bankruptcy proceeding under 11 U.S.C. §506(c). While it is true that this ruling held that the statutory language of section 506(c) entitled only the trustee to this specific collection power, this is not applicable to the current cause of action in question. Indeed, if we are to read the Bankruptcy Code "as a whole" as provided by *St. Vincent Hosp.*, 502 U.S. 215 at 221, we need not look any further than section 522(h), wherein a *debtor* "may avoid a transfer of property… if such transfer is avoidable by the trustee under section… 547." 11 U.S.C. 522(h)(1). Clearly, the Bankruptcy Code does not place avoidance power exclusively under the jurisdiction of the trustee – in many instances, a debtor may unequivocally exercise that power.

It is true that the avoidance powers provided to a debtor by section 522(h) are not entirely symmetrical to those held by the trustee under sections 547 and 550 as a debtor may only exercise them for property that may otherwise be exempted from the estate. *Id.* However, concurrent authority between the trustee and the debtor for exercising avoidance powers over a particular interest are addressed by the Bankruptcy Code itself, as bankruptcy courts ultimately have authority to confirm or deny an avoidance action. *Cohen v. Eiler* (*In re Cohen)*, 305 B.R. 886, 899

(9th Cir. 2004). Section 522(h) is clear – a debtor may exercise avoidance powers granted to trustees under section 547. The ability to supervise powers that are held concurrently between two or more parties is a tool central to the Bankruptcy Code and ensures the entirety of the text remains in harmony.

Even if the debtor's interest in the avoidance actions does not exist prior to the commencement of a bankruptcy proceeding, the avoidance actions "clearly qualify as property of the estate under subsection (7) which includes [a]ny interest in property that the estate acquires after the commencement of the case." *In re Simply Essentials*, 78 F.4th 1006, 1009. The trial court argued that avoidance actions are neither formed before nor after the petition date; they are instead "statutorily created by operation of law." R. at 21. However, any "third period of time" existing would "frustrate the bankruptcy policy of broad inclusion of property in the estate." *Id*. Bankruptcy causes of action are absolutely subject to inclusion in the estate under the Code, and excluding those that form in this "third period" unnecessarily restrict a plethora of bankruptcy causes of action in opposition to the plain language of the statute, all of which are created by operation of law.

Furthermore, courts have repeatedly recognized the ability for creditors to exercise a trustee's avoidance powers derivatively under specific circumstances. Specifically, "The sale or assignment of those claims may be permitted as long as the trustee consents and the court finds that the sale or assignment is in the 'best interest' of the estate and 'necessary and beneficial to the fair and efficient resolution of the bankruptcy proceedings.'" *Republic Credit Corp. I. v. Boyer (In re Boyer)*, 372 B.R. 102, 105–06 (D. Conn. 2007) (quoting *In re Commodore Int'l Ltd.*, 262 F.3d 96, 99 (2d Cir. 2001)). Whether Eclipse's acquisition of Floyd's avoidance power meets this criterion is presently immaterial – what is clear is that a trustee's chapter 5 avoidance power is unequivocally *not* under the sole authority of the trustee throughout the Bankruptcy Code, as the lower court stated was implied by *Hen House*, 530 U.S. 1. This is further corroborated by 11 U.S.C. §503(b)(3)(B), which allows for the reporting of administrative expenses incurred by creditors that recover from a debtor's pre-petition transfer. While a trustee certainly has the most widespread authority to exercise it, other parties may, and often do, employ avoidance powers either directly or derivatively with the consent of the trustee and/or the bankruptcy court. Because various parties have an interest in these avoidance powers, they should be read in conformity with breadth of 11 U.S.C. §541(a) and included in the estate itself.

ii. The Decisions of In Re Cybergenics Corp. and In re Clements Mfg. Liquidation Co. Do Not Outright Prevent Avoidance Powers from Being Property of the Bankruptcy Estate.

The lower court largely defers to tools of statutory interpretation to assert that the trustee and *only* the trustee may exercise avoidance powers. This deferment is largely due to "differing interpretations" regarding this question. R. at 18. However, this conflict is largely misrepresented by the court through two key cases. *Official Comm. Of Unsecured Creditors of Cybergenics Corp. v. Chinery (In re Cybergenics Corp.)*, 226 F.3d 237 (3d Cir. 2000) specifically deals with a state-law fraudulent transfer claim that was not to be included as part of a court-approved sale of the debtor-in-possession's assets under Chapter 11. *In re Clements Mfg. Liquidation Co., LLC,* 558 B.R. 187 (Bankr. E.D. Mich. 2016) expressly forbade the transfer of avoidance powers based on the facts specific to that case, not because avoidance powers are never assignable as property of the estate. Both cases present fact patterns wholly separate from the current appeal and should not be read as dispositive of the question of avoidance actions as estate property.

With regards to *In re Cybergenics Corp.*, the Third Circuit was tasked with deciding whether a debtor-in-possession's assets included a state-law fraudulent transfer claim under 11

U.S.C. §544(b). This is decidedly different from asserting whether such a claim would be included in the bankruptcy estate itself. Indeed, the court noted that "Issues relating to property of the estate are simply not relevant to the inquiry into whether the fraudulent transfer claims in the Committee's complaint were assets of Cybergenics as debtor or debtor in possession" 226 F.3d 237 at 246. The exceptions outlined in section 541 make it necessary to distinguish between the two, as the property interests of the debtor are not always included in the estate. 11 U.S.C. §541(a); T. Plank, *The Outer Boundaries of the Bankruptcy Estate*, 47 Emory L.J. 1193, 1214-1215 (1998). At best, *In re Cybergenics* merely asserts that avoidance actions are not property of the debtor themselves, without touching on whether they are therefore property of the estate.

Likewise, *In re Clements Mfg. Liquidation Co., LLC* does not definitively state whether avoidance actions are property of the estate. Instead, it refers to the supposed "split in the case law" regarding the issue to draw a conclusion based on whether such action is assignable based on the facts before them. 558 B.R. 187, 188-189. Notably, they based their decision on *In re Cybergenics* as well as *In re. Boyer*. The former again makes no affirmative declaration as to questions of property of the estate, while the latter seems to allow for avoidance action assignability based on the benefit to the estate. *In re. Boyer*, 372 B.R. 102, 105–06. This is far from a definitive statement regarding an estate's property interest in avoidance actions and should not be interpreted as such. Rather, it is necessary to look to the circumstances surrounding the assignment of a cause of action to determine its validity

This court should find that the language of the Bankruptcy Code as well as the judicial history of including causes of action into the estate supports a finding that avoidance actions are similarly property of the estate and are salable in the present case.

C. Even if, as the Lower Court Held, Eclipse is Acting in its own Self-Interest in Acquiring the Trustee's Avoidance Powers, Potential Harms to Other Creditors and to the Estate are Outweighed by the Benefits of Assignment.

The lower court held, without affirmative evidence in the record, that Eclipse is seeking to exercise the trustee's avoidance action "to pursue personal vendettas." R. 24. While it is impossible for us to peer into the mind of Eclipse, we can objectively decide whether Eclipse buying and potentially utilizing the trustee's avoidance power would be in the best interest of the estate. This should ultimately guide the decision notwithstanding any personal motivations of either Ms. Floyd or Eclipse absent a factual determination of bad faith.

i. Creditors May Derivatively Assert Avoidance Actions on Behalf of the Estate.

It bears repeating briefly that a statutorily valid avenue for recovery of preference payments exist in the ability for a creditor to derivatively assert a trustee's avoidance powers. 11 U.S.C. §503(b)(3)(B). While this is not the same as designating the avoidance powers property of the estate, they should effectively serve the same outcome: to ensure equal payment among creditors of a particular class. *In re Boyer*, 372 B.R. 102, 106. Indeed, cases that have explicitly tackled the issue of avoidance actions as property of the estate often hinge on the benefit to the estate of third-party assignment of this cause of action. *See, eg. In re P.R.TC., Inc*., 177 F.3d 774, 781–82; *In re Clements Mfg. Liquidation Co., LLC*, 558 B.R. 187, 188-189; *In re Carragher*, 249 B.R. 817, 820 (Bankr. N.D. Ga. 2000). Of course, 11 U.S.C. §704(a)(1) provides as much, holding the "best interest" of the parties involved to be paramount to a chapter 7 proceeding.

ii. Selling the Avoidance Action is in the Best Interest of the Estate.

If the intention of any preference avoidance action, whether commenced by the trustee or derivatively by a creditor, is to serve the best interest of the estate, then any sale and transfer of said action must likewise serve this interest. *In re Simply Essentials*, 78 F.4th 1006, 1008. The trustee is likewise statutorily bound to this maxim. 11 U.S.C. §704(a)(1). Part of this maximization serves one of the twin aims of the bankruptcy code: to return what is owed in an orderly and efficient fashion. If a trustee believes that selling their avoidance power statutorily provided to them is in the best interest of the estate, then they are merely exercising that role with "due diligence". 11 U.S.C. § 547(b). In the present case, Ms. Floyd has agreed to sell her avoidance power to Eclipse to enrich the estate. Certainly, selling the avoidance power would increase the equity of the estate in a more expeditious manner than pursuing the preference payment personally. Her judgment in this regard should hold some persuasive authority in determining whether such a sale is indeed in the best interest of the estate.

This is not to say that a trustee's judgment should blindly be followed, as the court ultimately holds a determinative authority to carry out the provisions of the Code. 11 U.S.C. § 105. However, when it can be objectively determined that such judgment would benefit both the estate and its creditors, there is no practicable reason to oppose it. It is important to note the purpose behind avoidance actions – to ensure that one creditor does not receive "a greater payment than others of his class." *Wolas*, 502 U.S. 151, 160-161. Eugene Clegg's preference payment to Pink prior to the commencement of this bankruptcy proceeding amounts to $20,000. Eclipse's proposed payment amounts to $470,000, presumably $450,000 for the value of the home and $20,000 for the value of the avoidance power. In essence, the estate would be furnished with the same amount of money it would have had it pursued the preference payment itself. Through this lens, it seems reasonable to say that Floyd's desire to sell the avoidance action for the value of the preference payment is a tacit approval of such an action that would result in the same equity being imbued in the estate.

The *total* amount being added to the estate through the debtor's purchase would, fittingly, eclipse the $20,000 currently in contention. Because the liquidated assets of the estate are distributed pro-rata to creditors of an alike class pursuant to 11 U.S.C. § 726(b), Pink stands to gain as much if not more under this sale than she would have had the trustee herself pursued avoidance action. The Servicer, as a secured creditor to the debtor, would be given a preferred status on payments from the estate. 11 U.S.C. §§ 506 and 507. After the $310,000 they are at most owed is distributed to them,[2] $160,000 would remain in the estate to be distributed pro-rata to both unsecured creditors, Pink and Eclipse. Distributing these funds pro-rata would result in an aggregate payment of 64% of their total owed funds – in other words, Pink would receive $32,000 from this sale alone, a $12,000 increase from the preferential transfer prior to the petition date.[3]

As a final note, the administrative expenses from such an expedited sale would be significantly lessened, increasing the amount available to distribute to Pink. In essence, this sale would minimize the administrative expenses garnered by the trustee in pursuing an avoidance action and liquidating the home while maximizing the value of the estate for both unsecured creditors. This is fundamental to the central responsibilities of the trustee in a chapter 7 estate under section 726 and should therefore be permissible.

CONCLUSION

This Court should reverse the decision of the Thirteenth Circuit Court of Appeals and hold that (1) post-petition, pre-conversion increase in equity in a debtor's property inures to the benefit of the bankruptcy estate rather than the debtor upon conversion of a bankruptcy case from chapter

[2] The chapter 13 trustee disclosed that she had distributed $10,000 of the $320,000 owed to the Servicer. R. at 8.
[3] "Pro-rata" payments are calculated by the percentage of the total debt owed that can be distributed with the funds available. $160,000 is 64% of the $250,000 owed to Eclipse and Pink. Each creditor would receive 64% of what is owed to them, ie. Pink would receive 64% of $50,000 – $32,000. American Bankruptcy Institute, *Chapter 11 – "101"*, American Bankruptcy Institute (2004).

13 to chapter 7 pursuant to 11 U.S.C. §§ 348 and 541, and (2) a chapter 7 trustee may sell, as property of the estate, the ability to avoid and recover transfers pursuant to 11 U.S.C. §§ 547 and 550.

APPENDIX A

11 U.S.C. § 105(a). Power of Court.

(a) The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title. No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.

11 U.S.C. § 348(f)(1). Effect of Conversion.

(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 pre-bankruptcy 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.

11 U.S.C. § 541(a). 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)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

(2) All interests of the debtor and the debtor's spouse in community property as of the commencement of the case that is—

(A) under the sole, equal, or joint management and control of the debtor; or

(B) liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable.

(3) Any interest in property that the trustee recovers under section 329(b), 363(n), 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.

(5) Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date—

(A) by bequest, devise, or inheritance;

(B) as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree; or

(C) as a beneficiary of a life insurance policy or of a death benefit plan.

(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. § 547(b) - 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(a). 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 initial transferee.