Team 39

No. 23-0115

IN THE

Supreme Court of the United States

IN RE EUGENE CLEGG, DEBTOR,

VERA LYNN FLOYD, CHAPTER 7 TRUSTEE, PETITIONER

V.

EUGENE CLEGG, RESPONDENT.

ON WRIT OF CERTIORARI FOR THE
UNITED STATES COURT OF APPEALS
FOR THE 13th CIRCUIT

BRIEF IN SUPPORT OF PETITIONER

QUESTIONS PRESENTED

I. Whether any post-petition, pre-conversion increase in equity in a debtor's property inures to the benefit of the bankruptcy estate upon conversion of a case from chapter 13 to chapter 7 where that property remained in the possession of or under the control of the debtor on the date of conversion, pursuant to 11 U.S.C 348(f)(1)(A).

II. When the chapter 7 trustee sold as property of the bankruptcy estate, the ability to avoid and recover transfers pursuant to 11 U.S.C. §§ 547 and 550, which enables the trustee to avoid preferential transfers made by the debtor before filing for bankruptcy and allows the trustee to recover transferred property in avoidance actions respectively, when she sold the preference cause of action to the largest creditor for fair market value?

TABLE OF CONTENTS

QUESTIONS PRESENTED i

TABLE OF CONTENTS ii

TABLE OF AUTHORITIES iii

STATEMENT OF JURISDICTION vi

STATUTORY PROVISIONS vi

STATEMENT OF FACTS 1

SUMMARY OF THE ARGUMENT 6

ARGUMENT 8

- **I. There Is a Split Amongst Circuits Whether Increased Value of Property Inures to the Estate Where Property Held at the Time of the Chapter 13 Petition Remains in the Possession or Is Under the Control of the Debtor on the Date of the Chapter 7 Conversion** 8
  - **A. The "*Goins* Approach"** 9
  - **B. The "*Cofer* Approach"** 10
  - **C. The Ninth's Circuits Proper Application of the Plain Meaning of Section 541(a) Results in the Increased Value of Property Inuring to the Estate** 11
  - **D. The Approach Taken by the Eighth and Tenth Circuit Is Flawed** 14
  - **E. Public Policy Favors the Property Value Inuring to the Estate** 15
- **II. Preference Actions Are Property of the Estate That Can Be Sold By the Trustee** .. 16
  - **A. The Chapter 7 Trustee is Permitted to Pursue an Avoidance Claim Against Pink Because the Avoidance Claim is Property of the Estate** 21
  - **B. The Avoidance Claims are Property, and as Such, Can and Must be Sold For the Benefit of the Estate** 22
  - **C. When the plain language of the Code is ambiguous, the court may consider public policy implications** 23

CONCLUSION 24

TABLE OF AUTHORITIES

Cases

BFP v. ADR Tr. Corp., 511 U.S. 531, 546 (1994)

Briggs v. Kent (In re Professional Investment Properties of America), 955 F.2d 623, 626 (9th Cir. 1992).

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Harris v. Viegelahn, 575 U.S. 510, 514 (2015)

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11 U.S.C. § 101(31)

11 U.S.C. § 101(31)(a)

11 U.S.C. § 101(31)(a)(i)

11 U.S.C. § 1327(b)

11 U.S.C. § 301

11 U.S.C. § 302

11 U.S.C. § 303

11 U.S.C. § 348(f)

11 U.S.C. § 348(f)(1)

11 U.S.C. § 348(f)(1)(A)

11 U.S.C. § 348(f)(2)

11 U.S.C. § 363

11 U.S.C. § 541(a)

11 U.S.C. § 541(a)(1)

11 U.S.C. § 541(a)(6)

11 U.S.C. § 544(b)

11 U.S.C. § 547(b)

11 U.S.C. § 547(b)(4)(B)

11 U.S.C. § 550

11 U.S.C. § 926(a)

Other Authorities

22 J. Bankr. L. & Prac. 3 Art. 1

House Report No. 95-595

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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.

STATEMENT OF FACTS

Facts

This case is on appeal from the 13th Circuit Court of Appeals. The facts have been stipulated by both parties. R. 5. n.2.

Eugene Clegg (the "Debtor") filed for Bankruptcy under chapter 13 on December 8, 2021 after experiencing financial hardships brought on by the COVID-19 pandemic. R. 4.

The Debtor retired in 2011. Less than one year later the Debtor's mother, Pink, transferred ownership of her movie theater, Final Cut, LLC ("Final Cut"), to the debtor. Final Cut was debt free at the time of the transfer and routinely turned a profit each year. By this time the Debtor's only source of income was his salary from Final Cut.

In 2016, the Debtor borrowed a loan in the amount of $850,000 (the "loan") from Eclipse Credit Union ("Eclipse") for the purposes of renovating Final Cut. R. 5. Per the loan agreement Eclipse was given first priority liens on Final Cut's real and personal property, and the Debtor agreed to an unconditional, unsecured personal guarantee in an unlimited amount. R. 5.

Final Cut was able to complete the renovations for less than the total amount of the loan. R. 5. The debtor then donated the remaining loan proceeds, approximately $75,000, to the local Veterans of Foreign Wars (the VFW) in 2017. R. 5. Eclipse did not learn of this donation until four years later at the meeting of the creditors. R. 5. and 7.

Final Cut reopened to the public in 2017 after the renovations were complete. R. 5 and 6. For three years Final Cut made a profit, but in March 2020 Moot's Governor declared a public health emergency and issued stay-at-home orders. R. 6. Final Cut closed its doors for approximately one year, leaving the Debtor with no income. On September 8th, 2020, the Debtor chose to borrow an unsecured loan in the amount of $50,000 from his mother, Pink. R. 6.

Final Cut reopened for the second time in February 2021, however the theater generated less business than it did before the public health emergency. R. 6. Eventually Final Cut landed in financial trouble. As a result, the Debtor chose to forgo his salary income and instead rely on credit cards. R. 6. Because of this, the Debtor took on sizable credit card debt and failed to make timely mortgage payments. R. 6. The Servicer of his mortgage payment, Another Brick in the Wall Financial Corporation, (the "Servicer"), initiated foreclosure proceedings after several consecutive missed payments.

The Debtor filed for chapter 13 bankruptcy after the Servicer commenced foreclosure proceedings R. 6. In his Schedule A/B the Debtor listed his home's value at $350,000 based on an appraisal done days before the petition date. R. 6. The Debtor's Schedule C listed the maximum homestead exemption for the State of Moot in the amount of $30,000. R. 7. Schedule D listed a $320,000 non-contingent, liquidated and undisputed debt to the Servicer. R. 6. Schedules E/F and H identified a contingent and unliquidated unsecured debt to Eclipse with an unknown value. R. 6. Finally, in the Debtor's Statement of Financial Affairs he listed payments to his mother, Pink, made within one year prior to the petition date totalling $20,000. R. 7.

Procedural Background - Chapter 13

The Debtor filed a proposed plan under chapter 13 of the Bankruptcy Code and agreed to make payments to creditors over a period of three years. R. 7. In the proposal, the Debtor agreed to pay back the missed mortgage payments and to continue to make monthly payments to the Servicer. R. 7. The proposal listed the value of the Debtor's home as $350,000, the same amount listed in Schedule A/B. R. 7. The proposal also stated that because of the secured indebtedness and the $30,000 homestead exemption, the Debtor has no equity in his home as of the petition date. R. 7. The Debtor planned to make payments with his earnings from Final Cut. R. 7.

As mentioned above, Eclipse did not learn of the Debtor's $75,000 donation to the VFW with loan proceeds until four years after it occurred. R. 5. and 7. Immediately upon learning of the donation at the meeting of the creditors, Eclipse initiated an adversary proceeding requesting the court to declare the Debtor's debt to Eclipse be non-dischargeable under 11 U.S.C. 523(a)(2)(A). R. 7.

Separately, the chapter 13 trustee objected to the Debtor's proposal for failing to satisfy 11 U.S.C. § 1325 (a)(4). R. 7. This section requires each creditor to receive no less under the proposal than it would otherwise receive under a hypothetical chapter 7 liquidation. 11 U.S.C. § 1325 (a)(4). The chapter 13 trustee argued that under a chapter 7 liquidation, the alleged $20,000 preferential payments to Pink would be recovered for the estate and subsequently distributed among the creditors. R. 7. In response, the Debtor agreed to amend the proposal and increase the payments to the creditors by $20,000 to reflect the alleged preferential payments. R. 7. This proposed amendment to the plan was stipulated to, and the chapter 13 trustee agreed to not pursue an avoidance claim to recover the alleged preferential payments to Pink. R. 8.

Eclipse objected to the plan, arguing that the proposal was not in good faith. R. 8. Weeks later the Debtor, Eclipse, and the chapter 13 trustee had reached an agreement where Eclipse would withdraw its objection to the plan in return for an estimated claim of $150,000, of which $25,000 would be deemed non-dischargeable even in the event of a chapter 7 conversion. R. 8.

The Debtor's plan was confirmed by the court on February 12, 2022, which included the settlement with the chapter 13 trustee and a statement providing that all property of the estate be vested in the debtor. R. 8.

Procedural Background - Conversion and Post-Conversion to Chapter 7

The Debtor adhered to the plan for eight months until he fell ill in September, 2022. R. 8.

The Debtor was unable to work and the following month Final Cut closed permanently. R. 8. Soon thereafter Eclipse initiated foreclosure proceedings against Final Cut. R. 8.

With Final Cut closed, the Debtor had no source of income and was unable to make the agreed to chapter 13 payments. R. 8. Rather than the chapter 13 case being dismissed and the creditors resuming collection efforts, the Debtor opted to convert his case to chapter 7. R. 8. The bankruptcy court then entered a standard order to that effect. R. 8. The chapter 13 trustee stated in her final report that $10,000 was distributed to the Servicer under the chapter 13 plan and that the funds held in reserve by Eclipse had been returned to the Debtor. R. 8 and 9.

Upon conversion to chapter 7, Vera Lynn Floyd ("the trustee") was appointed by the court as trustee. R. 9. In the Debtor's conversion schedules and other filings, he again listed his home's value at $350,000 and disclosed the alleged preferential payments to his mother, Pink. R. 9. The filings also stated that the Debtor owed Eclipse approximately $200,000 due to the deficiency of the loan guarantee after foreclosure, which was completed post-conversion. R. 9. The Debtor's statement of intention listed his plan to reaffirm the mortgage debt owed to the Servicer so that he could retain the house. R. 9.

The trustee's initial conclusion at the onset of the case was that the estate was largely void of assets. During the chapter 7 11 U.S.C. § 341 meeting of the creditors, the trustee had learned from the Debtor that homes in his neighborhood were selling at increased values compared to pre-pandemic levels. R. 9. In response, the trustee had the Debtor's home appraised again for the first time since the petition date. The appraisal revealed that the non-exempt equity in the home had increased by $100,000. R. 9.

The trustee, consistent with her duty under 11 U.S.C. § 704(a)(1) to "collect and reduce to money the property of the estate which such trustee serves" marked the home for sale. Eclipse offered to purchase both the home, and the alleged preference claim against the Debtor's mother Pink for $470,000. In accordance with her duty to maximize the value of the estate's assets for the benefit of the creditors, the trustee filed a motion ("the Sale motion") to the court seeking to sell the home and the alleged preferential payments claim to Eclipse under 11 U.S.C. § 363(b).

The Sale motion was objected to by the Debtor for two reasons. One, the Debtor argued that any post-petition, pre-conversion increase in the equity of his home should inure to his benefit. Furthermore, because there was no equity in the home for the estate at the petition date, the trustee lacked the ability to sell the home. Two, the Debtor argued that the Trustee's statutory ability to avoid and recover transferred under 11 U.S.C. § 547 and 11 U.S.C. § 550 cannot be sold.

The bankruptcy court ruled in favor of the Debtor on both objections and ultimately denied the Sale Motion. The trustee timely appealed the ruling, and upon request from the parties, the disputes were certified for direct appeal to this court under 28 U.S.C. § 158(d)(2)(A).

SUMMARY OF ARGUMENT

This case concerns a conflict regarding post-petition, pre-conversion appreciation in the value of a debtor's homestead and whether that appreciation belongs to the debtor or belongs to the debtor's estate upon conversion from a chapter 13 reorganization to a chapter 7 liquidation. Competing interpretations and applications of 11 U.S.C. § 348(f)(1) exists among the circuits.

The plain language of § 348(f)(1)(A) dictates that any property of the estate at the time of the original filing that is still in the debtor's possession at the time of conversion attaches to the debtor's estate. The "*Goins* Approach" (the appropriate approach) directs that any change in the value of such an asset is also part of the estate.

Under the "*Goins* Approach," courts have held that 11 U.S.C. § 348(f)(1) is not ambiguous, and therefore rely on the plain meaning of the language as being conclusive without consulting legislative history. Conversely, under the "*Cofer* Approach," courts have incorrectly reasoned that 11 U.S.C. § 348(f)(1) is ambiguous and instead relies on legislative history.

Because 11 U.S.C. § 348(f)(1)(A) language is unambiguous, it dictates that any property of the estate at the time of the original filing that is still in the debtor's possession at the time of conversion attaches to the debtor's estate. Consequently, the $100,000 increase in the value of Clegg's property from the time of the filing of the chapter 13 petition to the time of conversion to chapter 7 inures to the estate.

It is unfortunate when a debtor faces tough circumstances due to illness or unemployment. However, it is important to analyze their situation objectively and not subjectively to arrive at consistent, fair, and predictable outcomes. 11 U.S.C. § 348(f)(1) mandates that, upon conversion to chapter 7 from chapter 13, the post-petition appreciation in the value of property should inure to the bankruptcy estate in a consistent, fair, and predictable manner.

Separately, the court must consider whether to approve the sale of the preferential payments action to Pink. 11 U.S.C. § 547(b) of the bankruptcy code grants the trustee the power to avoid and recover certain payments made to creditors within a specific period before filing for bankruptcy. The alleged preferential payments in this case occurred within the time frame listed in 11 U.S.C. § 547(b)(4)(b), and therefore permitted the chapter 7 trustee to pursue these preferential payments.

The House Report on the bankruptcy code and the Supreme Court have previously classified causes of action, like the chapter 5 avoidance cause of action, as property of the estate. A trustee has a duty under 11 U.S.C. § 550 to maximize the value of the estate by selling the property to be distributed to the creditors on a pro rata basis. Furthermore, 11 U.S.C. § 363 requires the trustee to use articulable and sound business judgment when selling property of the estate. Because avoidance claims are considered property of the estate, it is the duty of the trustee to sell those claims for the benefit of the estate so long as there are valid business reasons for doing so. In this case, permitting Eclipse to purchase the avoidance action maximizes the value of the estate by immediately recovering the maximum recoverable amount from the claim, without any litigation costs or fees. Furthermore, the sale can be supported by sound business judgment for the reasons stated above, it ensures maximum recovery, it saves costs, and it disposes of the case quicker than it would otherwise.

ARGUMENT

I. There Is a Split Amongst Circuits Whether Increased Value of Property Inures to the Estate Where Property Held at the Time of the Chapter 13 Petition Remains in the Possession or Is Under the Control of the Debtor on the Date of the Chapter 7 Conversion.

There is a split amongst certain appellate courts regarding whether post-petition, pre-conversion appreciation in the value of a debtor's homestead belongs to the debtor or belongs to debtor's estate upon conversion from a chapter 13 reorganization to a chapter 7 liquidation. *Castleman v. Burman (In re Castleman)*, 75 F.4th 1058 (9th Cir. 2023). The split arises from competing interpretations and applications of provisions of 11 U.S.C. § 541 and 11 U.S.C. § 348(f)(1) at the time of conversion from chapter 13 to chapter 7.

At the onset of filing for bankruptcy, a debtor's assets are immediately transferred to a bankruptcy estate. 11 U.S.C. § 541(a). 11 U.S.C. § 541(a)(1) defines the property of the bankruptcy estate upon filing under either a chapter 13 or chapter 7.11 U.S.C. § 541(a)(1) mandates that the estate includes "all legal or equitable interests of the debtor in property as part of the commencement of the case." Further, 11 U.S.C. § 541(a)(6) provides that all "proceeds, product, offspring, rents, or profits of or from the property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case" constitutes property of the estate. 11 U.S.C. § 541(a)(6).

11 U.S.C. § 348 sets forth what property of a debtor, in the debtor's chapter 13 plan, is property of the chapter 7 estate upon conversion. 11 U.S.C. § 348 simplifies the determination of property available for a trustee to administer.

11 U.S.C. § 348 provides, in relevant part:

(a) Conversion of a case from a case under one chapter of this title to case under another chapter of this title constitutes an order of relief under the chapter to

> which the case is converted, but, except as provided in subsections (b) and (c) of this section, does not effect a change in the date of the filing of the petition, the commencement of the case, or the order for relief.

. . .

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

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

Two approaches exist for analyzing 11 U.S.C. § 348(f)(1) where there are changes in property value or equity from the date of a chapter 13 petition filing to a chapter 7 conversion: the "*Goins* Approach" and the "*Cofer* Approach." Under the "*Goins* Approach," courts have held that 11 U.S.C. § 348(f)(1) is not ambiguous, and therefore rely on the plain meaning of the language as being conclusive without consulting legislative history. Conversely, under the "*Cofer* Approach," courts have held that 11 U.S.C. § 348(f)(1) is ambiguous and instead rely on legislative history.

A. The "*Goins* Approach"

Under the "*Goins* Approach," courts find no ambiguity in 11 U.S.C. § 348(f)(1). In the case of *In re Goins*, 539 B.R. 510, 511-13 (Bankr. E.D. Va. 2015), the trustee sought to sell the debtor's real estate property after the case was converted from chapter 13 to chapter 7. The property had increased in value between the date of the petition and conversion, and the debtor had made payments reducing the debt secured by the property. The trustee contended that the chapter 7 estate was entitled to the appreciation in value, while the debtor would receive any increase in equity due to payments made during the chapter 13 case. The court decided that the chapter 7 estate was entitled to appreciation. Consequently, the debtor would be entitled to retain equity in the home resulting from principal payments but any appreciation in market value of the home would inure to the estate.

Similarly, the court in *In re Peter*, 309 B.R. 792, 795 (Bankr. D. Or. 2004), held that, even if the net value of an asset changes during the chapter 13 case due to the debtor's payments on secured debt, any increase in equity goes to the chapter 7 estate. The debtor had paid off his vehicle's secured debt before the conversion of his chapter 13 to chapter 7. The court concluded that, pursuant to 11 U.S.C. § 348(f)(1)(A), upon conversion, property of the chapter 7 estate consists of property of the estate as of the date of filing of the petition. The vehicle was property of the estate on the date of the petition, and the statute does not limit the subsequent chapter 7 estate to equity in property of the estate at the petition date.

Likewise, in *In re Castleman*, 75 F.4th 1052 (9th Cir. 2023), the circuit court held that any increase in the net value of the debtor's home during the time they were under chapter 13 and before a good faith conversion to chapter 7 belongs to the chapter 7 estate. Castleman was a debtor who filed for chapter 13 bankruptcy and entered into a restructuring plan. Health issues caused Castleman to discontinue working, and he converted his chapter 13 case to chapter 7. Castleman sought to claim the appreciated value of his home as debtor's property. The home's appreciated value had increased since the post-petition under chapter 13 and before pre-conversion to chapter 7. The Ninth Circuit denied Castleman's request to retain the value of his home's appreciation as debtor's property, stating any property of the estate at the time of the petition date becomes part of the bankruptcy estate upon conversion.

B. The "*Cofer* Approach"

The second approach the courts have adopted is the "*Cofer* Approach," which looks at legislative history. *In re Cofer*, 625 B.R. 194, 200-02 (Bankr. D. Idaho 2021), following a conversion from a chapter 13 to a chapter 7, the chapter 7 Trustee sought to limit the amount of the debtor's homestead to the value at the date of the petition, arguing that any post-petition appreciation in the value inured to the chapter 7 estate. In analyzing 11 U.S.C. § 348(f)(1), the court determined that the statute was ambiguous. Accordingly, the court looked to the statute's legislative history and held that the post-petition, pre-conversion appreciation in value of the chapter 13 debtor's home inured to the benefit of the debtor.

In *Rodriguez v. Barrera (In re Barrera*), 22 F.4th 1217, 1223 (10th Cir. 2022), the court determined that 11 U.S.C. § 348(f)(1) was ambiguous and that the statute should be interpreted in light of the legislative history of the 1994 Amendments. The court applied the *Cofer* Approach to conclude that any appreciation in value inures to the benefit of the debtor as that outcome follows the intention of Congress to encourage debtors to file under chapter 13. Therefore, the court held that "property" as defined by 11 U.S.C. § 348(f)(1)(A) does not include any of the appreciation in the value of the debtor's house that occurred from the filing of the chapter 13 petition to the filing of the chapter 7 conversion. That appreciated value is excluded from the chapter 7 estate upon conversion.

C. The Ninth's Circuits Proper Application of the Plain Meaning of 11 U.S.C. § 541(a) Results in the Increase Value of Property Inuring to the Estate.

The Ninth Circuit has ruled that, when a debtor in good faith converts to chapter 7, the increase in the value of the debtor's homestead that accrued during the pendency of chapter 13 belongs to the chapter 7 estate and is available for distribution to creditors. *Castleman v. Burman*, 75 F.4th 1052 (9th Cir. 2023). The appellate court correctly begins its analysis by looking to 11 U.S.C. § 541(a), which mandates that the estate includes "all legal or equitable interests of the debtor in property as part of the commencement of the case." Further, 11 U.S.C. § 541(a)(6) provides that all "proceeds, product, offspring, rents, or profits of or from the property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case" constitutes property of the estate. 11 U.S.C. § 541(a)(6).

When interpreting the meaning of a statute, a court should first look at the language of the statute itself. *United States v. Ron Pair Enterprises*, 489 U.S. 235, 241, 109 S. Ct. 1026, 1030 (1989). In interpreting the Bankruptcy Code, "the first step … is to determine whether the language [of a statute] has plain and unambiguous meaning with regard to the particular dispute." *Hawkins v. Franchise Tax Bd. of Cal.*, 769 F.3d 662, 666 (9th Cir. 2017). If the plain meaning is unambiguous, it controls. Id.

Interpretation of a statute begins with the statute's text, and all words must receive their plain, ordinary meaning unless Congress otherwise specifies. Canons of statutory construction, which represent "rules of thumb that help courts determine the meaning of legislation," should also be used to analyze a statute's text. *FDA v. Brown & Williamson Tobacco Corp.*, 529 U. S. 120 (2000). "Statutory construction … is a holistic endeavor. A provision that may seem ambiguous in isolation is often clarified by the remainder of the statutory scheme." *United Sav. Ass'n of Tex. v. Timbers of Inwood Forest Assoc., Ltd.*, 484 U.S. 365, 371 (1988). The plainness or ambiguity of statutory language is determined by reference to the language itself, the specific context in which that language is used, and the broader context of the statute as a whole and look to the other definitions of "property of the estate" set forth in other provisions of the Code itself. *Robinson v. Shell Oil Co.*, 519 U.S. 337, 340 (1997).

Under 11 U.S.C. § 541(a)(1), filing for bankruptcy creates an estate that includes "all equitable interests of the debtor in property as of the commencement of the case." The estate also includes all "proceeds, product, offspring, rents, or profits of or from property of the estate, except such as earnings from services performed by an individual debtor after the commencement of the case." 11 U.S.C. § 541(a)(6).

The *In re Goins* court found that, for any post-petition appreciation in assets of the estate, a trustee is entitled to "[t]he equity attributable to the post-petition appreciation of the property [that] is not separate, after-acquired property . . . [t]he equity is inseparable from the real estate, which was always property of the estate under 11 U.S.C. § 541(a)." 539 B.R. at 516; see also *In re Goetz*, 647 B.R. 416 (B.A.P. 8th Cir. 2023) (the broad definition of "property of the estate" in 11 U.S.C. § 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"). Other courts have held that any post-petition increase in the property's equity is the "proceeds, product, offspring, rents or profits" of the estate's original property under 11 U.S.C. § 541(a)(6), and so became part of the estate when the case commenced. See In re Potter, 228 B.R. at 424; In re Peter, 309 B.R. at 794-95.

In the instant case, Debtor Eugene Clegg filed for a chapter 13 bankruptcy, listing his home valued at $350,000, with a mortgage balance of $320,000. Clegg claimed a homestead exemption of $30,000.00 to cover the difference between the appraised value of his property and the balance owed on it. Notably, the homestead exemption of $30,000 is the maximum amount Clegg was allowed to exempt under state law. After failing to make payments, Clegg converted his case to a chapter 7. While Clegg was under his chapter 13 Plan for eight months, the value of his property had increased by $100,000.

11 U.S.C. § 348(f)(1)(A) is unambiguous. The statute is clear that, at the time a debtor files for a chapter 13 bankruptcy, any property still in the debtor's possession at the time of conversion to chapter 7 remains the property of the chapter 7 estate. The statute does not restrict

the converted chapter 7 to the value of the property at the onset of the filing of chapter 13. As a result, any increase in equity of Clegg's property is inured to the estate.

D. The Approach Taken by the Eighth and Tenth Circuits Is Flawed

The Eighth and the Tenth Circuits have reached different conclusions than the Ninth Circuit regarding post-petition changes in property value and have relied on various statements or examples in the legislative history surrounding 11 U.S.C. § 348(f). 11 U.S.C. § 348(f) was enacted to clarify whether new property acquired during chapter 13 proceedings becomes property of the converted estate. The focus of 11 U.S.C. § 348(f)(2) is whether the debtor was acting in good faith or bad faith. *Cofer*, 625 B.R. at 200-02. This focus is misplaced, however, because the language of 11 U.S.C. § 348(f), when read in conjunction with the remainder of the Bankruptcy Code, is not ambiguous. Therefore it is not necessary to look to the legislative history for guidance. *Robinson*, 519 U.S. at 341 ("Our inquiry must cease if the statutory language is unambiguous.").

Any reliance by the Eighth and Tenth Circuit's on good faith or bad faith as a factor in interpreting a proper allocation of property during a conversion from chapter 13 to chapter 7 is misplaced. 11 U.S.C. § 348(f)(2) sets forth that any property acquired after filing would not become part of an estate upon conversion regardless if the debtor had acted in good faith. Allocation of property to the estate under 11 U.S.C. § 348(f)(2) where the debtor converts in bad faith is a penalty and not a factor in determining whether property inures to the estate as a result of a conversion from chapter 13 to chapter 7.

Additionally, in support of their interpretation of the Bankruptcy Code, the Eighth and Tenth Circuits point to 11 U.S.C. § 1327(b), which states: "Except as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all property of the estate in the debtor." The Eighth and Tenth Circuits rely on this section to reason that the property of the estate should inure to the debtor. However, the legislative intent does not support the Eighth and Tenth Circuit's application of 11 U.S.C. § 1327(b) in the context of conversion from a chapter 13 to a chapter 7. Neither 11 U.S.C. § 541 nor 11 U.S.C. § 348 cross-reference 11 U.S.C. §1327(b), so Congress did not intend for an accounting or ever-evolving valuation process that would result from the Eighth and the Tenth Circuit's application of 11 U.S.C. § 1327(b) in this context. Where Congress intends to exclude assets or specific interests, it does so with specificity. For example, in 11 U.S.C. § 541(a)(6), Congress expressly excluded post-petition earnings by an individual in a chapter 7 case. If Congress intended to exclude any increase in equity of an asset of the estate that occurred from the time of filing to conversion, it would have explicitly designated that exclusion in 11 U.S.C. § 348(f).

The plain language of 11 U.S.C. § 348(f)(1)(A) dictates that any property of the estate at the time of the original filing that is still in the debtor's possession at the time of conversion attaches to the debtor's estate. The "*Goins* Approach" (the appropriate approach) directs that any change in the value of such an asset is also part of the estate. Consequently, the $100,000 increase in the value of Clegg's property from the time of the filing of the chapter 13 petition to the time of conversion to chapter 7 inures to the estate. This is not earned equity, such as payment of mortgage principal, it is simply a happenstance of market conditions, which sometimes will benefit the debtor and sometimes benefit the estate. *In re Castleman*, 75 F.4th 1058 (9th Cir. 2023). In other instances, property value may decline to the detriment of the estate.

E. Public Policy Favors the Property Value Inuring to the Estate

Bankruptcy has negative consequences for all parties involved. The debtors lose their assets and their aspirations, while creditors lose income from the debtor's repayments. Generally, assets of a debtor cannot be repossessed or resold, making fair compensation of everyone challenging. The purpose of the Bankruptcy Code is to balance the rights and obligations between a debtor and a creditor, but satisfying all interested parties is not always possible.

When a debtor files for chapter 13 bankruptcy, the debtor does so in the hopes of relieving some of the financial burden the debtor is experiencing. A chapter 13 plan allows for some flexibility to help facilitate a debtor to pay off debts owed. The harsh reality is that debtor's often struggle to keep up with a chapter 13 plan, which is why "Congress accorded debtors to a non waivable right to convert a chapter 13 to one under chapter 7 'at any time.'" *Harris v. Viegelahn*, 575 U.S. 540, 513-14 (2015).

Importantly, the bankruptcy court's objective is not to disincentivize debtors from trying to pay their creditors as much as they can through a chapter 13 plan. While a debtor's intentions may be genuine, it is necessary to objectively examine the laws. Although it is unfortunate when a debtor faces difficult circumstances due to illness or unemployment, it is important to remember that their circumstances should be analyzed objectively and not subjectively to reach consistent, fair, and predictable results. The plain language of 11 U.S.C. § 348(f)(1) achieves such results by mandating that, upon conversion to chapter 7 from chapter 13, the post-petition appreciation in the value of property, consistently, fairly, and predictably inures to the bankruptcy estate.

II. Preference Actions Are Property of the Estate That Can Be Sold By the Trustee.

11 U.S.C. § 547(b) of the Bankruptcy Code grants the trustee the power to avoid and recover certain payments and transfers made by the debtor to the creditors, within a specified period before filing for bankruptcy. 11 U.S.C. § 547(b). The purpose of 11 U.S.C. § 547 is two fold. First, allowing the trustee to avoid transfers by the debtors before filing for bankruptcy discourages creditors "from racing to the courthouse to dismember the debtor." *Union Bank v. Wolas*, 502 U.S. 151, 160-161 (1991). Second, the preference provisions of the Code "facilitate the prime bankruptcy policy of equality among the creditors" by ensuring equitable distribution of assets to the creditors. *Wolas*, 502 U.S. 151 at 161.

Whether avoidance actions can be pursued depends on time of the payment to the petition date. 11 U.S.C. § 547(b)(4)(B). These avoidance actions can be pursued when the alleged transfer was made "on or within ninety days" before the petition date. *Id*. However, the payment window prior to the petition date expands to "between ninety days and one year" of the petition date when the creditor recipient of the payment is an "insider" and the payment enables the creditor to receive more than they would have had the case been under chapter 7. *Id.*

Those considered to be "insiders" are defined in 11 U.S.C. § 101(31) and the common law. This section lists different types of insiders for different types of debtors. Here, the Debtor is an individual. 11 U.S.C. § 101(31)(a) lists those considered to be insiders for individual debtors, specifically, 11 U.S.C. § 101(31)(a)(i) states that "relative(s) of the debtor" are to be considered insiders. In the present case, the alleged preferential payments were made to Pink, the debtor's mother, and were done between ninety days and one year of the petition date. R. 7.

Once the trustee learns of an alleged avoidance claim, 11 U.S.C. § 550 provides that "to the extent that a transfer is avoided under 11 U.S.C. § 544, 545, 547, 548, 549, 553(b), or 724(a)

. . . the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property." The statute however, is silent as to what constitutes a recovery "for the benefit of the estate." 11 U.S.C. § 550.

For the trustee to sell an alleged avoidance action, it must first be considered property of the estate. What constitutes property of the estate is found under 11 U.S.C. § 541 and its seven subsections.

This statute states in its introduction that whenever a bankruptcy case begins under 11 U.S.C. § 301, 302, or 303, an estate is created. 11 U.S.C. §§§ 301, 302, 303. The following seven subsections specifically list what is and is not considered to be property of that estate. 11 U.S.C. § 541. This statute too, is silent as to whether avoidance actions are considered property of the estate or not. *Id.* Additionally, the bankruptcy Code is silent as to the definition of "property." *Id.* To understand what the statute means when it refers to "property" we look to the pen of the legislature.

House Report No. 95-595 on the Bankruptcy Code specifies what is considered to be "property" of the estate. Property of the estate "includes all interests, such as interests in real or personal property…choses in action, causes of action…" House Report No. 95-595. Here, we are concerned with the sale of an avoidance action, which according to the Supreme Court, is a cause of action: "[A] statutory cause of action, such as the right to recover a fraudulent conveyance…" *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33, 53 (1989). Even 11 U.S.C. § 926, which governs municipal bankruptcy, refers to other avoidance action sections of the Code as "causes of action." "If the debtor refuses to pursue a cause of action under 11 U.S.C. § 544, 545, 547, 548, 549(a), or 550…the court may appoint a trustee to pursue such cause of action." 11 U.S.C. §

926(a). With the exception of 11 U.S.C. § 550, these sections are all avoidance provisions. *In re AVI, Inc.*, 389 B.R. 721, 734 (B.A.P. 9th Cir. 2008).

According to multiple circuits, avoidance claims do represent an interest in property. The fifth circuit court of appeals has held that 11 U.S.C. § 544(b) considers state law fraudulent transfer actions to be property of the estate that can be sold. *In re Moore*, 608 F.3d 253, 262 (5th Cir. 2010). The seventh circuit held as well that avoidance actions are property of the estate. *National Tax Credit Partners, L.P. v. Havlik*, 20 F.3d 705, 708-09, (7th Cir. 1994). Finally, the 9th circuit too has held, albeit under a different section of the Code, that avoidance claims can be sold under 1234(b)(3)(b). Briggs v. Kent (*In re Professional Investment Properties of America)*, 955 F.2d 623, 626 (9th Cir. 1992).

Fraudulent conveyance actions are property of the estate that the trustees are permitted to sell to the creditors. In Moore, 608 F.3d at 256, James Moore filed for bankruptcy under chapter 7. In re Moore, 608 F.3d 253, at 256 (5th Cir. 2010). The estate was bereft of assets and the only way for creditors to receive payments was to pursue asset recovery litigation. Id. The largest creditor in the case, Cadle, funded the asset recovery litigation while under the control of the chapter 7 trustee. Id. Legal fees mounted with no resolution, leading to the creditor offering to purchase the claims for $10,000. The trustee declined the sale, but negotiations continued. Eventually, the trustee decided to change course and pursued a settlement with the defendants. Id. The trustee and the defendants entered into a proposed settlement agreement in the amount of $37,500. When Cadle learned of the settlement, they offered $50,000 for the claims. Id. The trustee's attorney agreed that the proposed offer was "substantially more than the proposed settlement" Id. The lower court ruled that the settlement was in the best interest of the estate, in part because it concluded that the avoidance claims could not be sold. Id, 257.

The court held that the fraudulent-transfer claims are considered to be property of the estate under § 541(a)(1), and therefore may be sold by the trustee under § 363(b). The court reasoned that the state fraudulent conveyance claims are considered property of the estate under § 541(a)(1), and therefore could be sold by the trustee like any other asset under § 544(b). Id. at 259 and 261. The court further added that permitting a trustee to sell causes of action is in accordance with the trustee's existing power, because it still requires notice, court approval, and is based on the trustee's articulable business justifications.

Dissenters to the view that avoidance powers are considered property of the estate assert that avoidance causes of action are instead statutory powers granted to the trustee that are not property of the estate. *In re McGuirk*, 414 B.R. 878, 879, (Bankr. N.D. Ga. 2009). However, his view is misguided.

Despite the code and legislative history occasionally referring to the avoidance provisions as "avoidance powers," there has yet to be an indication that Congress used this term for the purpose of preventing avoidance actions from being considered property of the estate. *Frost v. Viegelahn* (In re Frost), BANKRUPTCY CASE NO. 09-54674-RBK (W.D. Tex. Jul. 9, 2012).

After establishing that avoidance actions are considered to be property of the estate, it must now be established that the trustee has the ability to sell property of the estate pursuant to 363. *Moore*, 608 F.3d at 261.

11 U.S.C. § 363 governs the trustee's authority to use, sell, or lease property of the estate. It provides that the trustee may "sell…in the ordinary course of business, property of the estate." This section also provides that the sale of an estate asset "must be supported by an articulated business justification, good business judgment, or sound business reasons."11 U.S.C. § 363(b). To satisfy this standard, "the trustee must demonstrate that the proposed sale price is the highest

and best offer though a bankruptcy court may accept a lower bid in the presence of sound business reasons." *Moore*, 608 F.3d at 263. Factors the court considers in establishing if the trustee had a good business reason are as follows:

(1) a sound business reason;

(2) accurate and reasonable notice;

(3) adequacy of the price; and

(4) good faith.

Id. So long as the trustee's sale of the avoidance claim satisfies the rules and standards laid out above, it should be permitted.

This Court has considered public policy implications when the plain language of the Code is ambiguous. *BFP v. ADR Tr. Corp.*, 511 U.S. 531, 546 (1994). It is crucial to the efficiency of the courts, its practitioners, and all parties to a case whose outcome hinges on a question of statutory interpretation. Permitting the sale of avoidance claims allows a trustee to more efficiently convert assets into cash to be distributed to creditors pro rata. Glenn, 1 "Fraudulent Conveyances and Preferences" § 132 at 250. By permitting the sale of an avoidance claim, it also lessens the burden on the estate by transferring the recovery cost to the buyer of the claim. Post Reorganization control (Code § 1129(a)(5)), 6 Norton Bankr. L. & Prac. 3d § 112:12. Finally, the sale of an avoidance action is consistent with a trustee's requirement under chapter 7 to "maximize the value of the estate" for the highest distribution to the creditors. *Commodity §Futures Trading Commn. v. Weintraub,* 471 U.S. 343, 357 (1985).

Opponents of the view that the trustee should be permitted to sell avoidance actions frequently argue that allowing a creditor to purchase avoidance claims is unfair to other creditors. This is misguided. The creditor only receives a recovery of an avoidance action due to their status as a buyer, for which they gave consideration for the right to litigate and keep any resulting recoveries. 22 J. Bankr. L. & Prac. 3 Art. 1. Additionally, The proceeds from the purchased action and the creditor's claim against the estate have no bearing on one another. *Id.*

A. The Chapter 7 Trustee is Permitted to Pursue an Avoidance Claim Against Pink Because the Avoidance Claim is Property of the Estate.

As mentioned above, § 547 grants the trustee the power to avoid and recover certain payments and transfers made by the debtor to the creditor within a specified period before filing for bankruptcy. Here, the avoidance claim at issue is a preferential payment made by the Debtor, to his mother Pink, between ninety days and one year before the petition date. R. 7. The trustee has the authority under § 547(b) to "avoid any transfer of an interest of the debtor in property." § 547(b).

Whether property of the estate includes avoidance actions has already been answered by the House Report on the bankruptcy Code and the Supreme Court in *Granfinanciera*. Both sources conclude that property of the estate includes causes of action. Here, the preferential payment to Pink is an avoidance action under chapter 5 of the bankruptcy Code, and therefore is considered property of the estate.

B. The Avoidance Claims are Property, and as Such, Can and Must be Sold For the Benefit of the Estate.

It has been established that avoidance claims are property. Because they are property, the trustee must, pursuant to §§ 550 and 363, sell those avoidance claims for the maximum benefit of the estate. Under § 550, it is the statutory duty of a chapter 7 trustee to maximize the value of the estate. If avoidance actions are considered to be property of the estate, it is the duty of the trustee to maximize those claims either by pursuing and recovering their value on behalf of the estate, or by selling them to a creditor. Here, the trustee did just that. The trustee wisely chose to accept

Eclipse's offer for the house and alleged preference claims against Pink for $470,000. The value of the house was appraised to be $450,000 at the time of the offer, and the Debtor's preference payments to Pink amounted to $20,000. R. 9. Eclipse offered the maximum recoverable amount in the preference claim to the Estate. If the trustee were to pursue a preference claim, not only would the estate incur litigation and overhead costs, there is no guarantee that the estate would collect the full $20,000. This would be to the detriment of the creditors. By Eclipse offering the maximum recoverable amount, and saving the estate costs, the transaction would by definition "maximize the value of the estate" pursuant to 11 U.S.C. § 550. Furthermore, the creditors' purchase in this case does not yield them a disproportionate recovery due to the fact that the purchase price of the claim is the max amount its worth. This does not provide an unfair recovery because the creditor is giving, in our case, more than adequate consideration for the claim.

If the trustee elects to sell the avoidance actions, they must do so pursuant to 11 U.S.C. § 363, requiring the sale to be done with good, articulable, business justifications. As mentioned above, the good, articulable, business justifications for selling to avoidance claim to Eclipse include: (1) it saves the estate costs of litigation, (2) it ensures the maximum recovery of the claim, and (3) it disposes of the issue immediately, rather than drag it on and incur more costs.

C. When the plain language of the Code is ambiguous, the court may consider public policy implications.

In the case before the court, it would be good public policy to permit the sale of an avoidance action because doing so would maximize the value of the estate. As mentioned above, the maximum amount the estate could hope to get from the preferential payment action is $20,000. This is because the payments to Pink amounted to $20,000, and Eclipse would not be able to collect more than the $20,000. It is entirely possible however, that pursuing the preference claim would amount to a judgment in an amount less than $20,000. Not to mention the litigation costs of pursuing the claim. This is a risk to the trustee, and would be to the detriment of the creditors. Permitting the sale of the avoidance claims ensures the estate receives the maximum amount possible for the claim and suffers no costs related to the pursuit of the claim.

Additionally, permitting the sale of the avoidance claim in this case would contribute to a speedy and efficient resolution to the bankruptcy action, benefiting the creditors, the debtors, and the court. Allowing the sale of the action would dispose of the case much sooner by allowing Eclipse to pursue the action separately from the estate, and allowing the estate to more quickly distribute the proceeds of the action to the creditors. Moreover, permitting the sale contributes to efficient judicial economy by disposing of the case sooner than it would have had the sale been rejected.

Lastly, permitting the sale does not provide an unfair recovery to any of the creditors, because in our case Eclipse is paying fair market value of the claim, $20,000, and in fact taking a risk that the claim will fail or amount to less than the purchase price. It would be impossible for Eclipse to "come out on top" in the action, because the maximum recoverable amount in the claim is precisely what Eclipse paid for the claim, not to mention any costs or fees that they will incur in the pursuit of the claim.

CONCLUSION

For the reasons listed above, this Court should find in favor of the Petitioner, Vera Lynn Floyd, chapter 7 Trustee, and reverse the decisions of the bankruptcy court.