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## Whether the Equitable Power of the Bankruptcy Court Can Save the Tardy Filing of a Nondischargeability Complaint

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### Introduction & Background

Courts have long held that the Bankruptcy Code provides a discharge only to those “honest but unfortunate debtors.”<sup>1</sup> To that end, when a debt has been incurred under false pretenses, false representation, or outright fraud, the Bankruptcy Code allows the debtor’s creditors to file a nondischargeability complaint against the debtor.<sup>2</sup> However, in order for the creditor to challenge the dischargeability of a debt, the creditor must file his or her nondischargeability complaint in a timely manner.<sup>3</sup> A creditor who fails to file a timely complaint (or to seek a “for cause” extension) risks losing the right to challenge the discharge of the allegedly fraudulently acquired debt.<sup>4</sup>

<sup>1</sup> Cohen v. de la Cruz, 523 U.S. 213 (1998).

<sup>2</sup> 11 U.S.C. § 523(a)(2)(A) (2012) (“A discharge . . . does not discharge an individual debtor from any debt . . . for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by . . . false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor’s or an insider’s financial condition”).

<sup>3</sup> 11 U.S.C. § 523(c)(1) (2012) (“the debtor shall be discharged from a debt . . . unless, on request from the creditor to whom such debt is owed, and after notice and hearing, the court determines such a debt to be excepted from discharge”).

<sup>4</sup> *In re Kennerley*, 995 F.2d 145, 148 (9th Cir. 1993) (creditor forfeited the right to contest the dischargeability of an allegedly fraudulent debt because of an untimely filing).

Rule 4007(c) of the Federal Rules of Bankruptcy Procedure (“FRBP”) sets forth a strict sixty-day time limit in which such a nondischargeability complaint must be filed. Specifically, the rule provides:

Except as otherwise provided . . . a complaint to determine the dischargeability of a debt under § 523(c) shall be filed *no later than 60 days* after the first date set for the meeting of creditors under § 341(a). The court shall give all creditors no less than 30 days' notice of the time so fixed in the manner provided in Rule 2002. On motion of a party in interest, after hearing on notice, the court may for cause extend the time fixed under this subdivision. The motion shall be filed before the time has expired.<sup>5</sup>

Despite the apparent clarity of the rule, questions remain as to whether there may be any retroactive extensions granted for the filing of nondischargeability complaints outside of the sixty-day period. Some courts have reasoned that since the bankruptcy court is a court of equity, relief should be available to litigants under limited circumstances.<sup>6</sup> On the other hand, some courts refuse to extend the equitable power of the bankruptcy court when faced with a clear directive from the Bankruptcy Code or the Federal Rules of Bankruptcy Procedure.<sup>7</sup> The former view has been called the “procedural” view, while the latter has been called the “jurisdictional” view.

This Article will discuss under which circumstances, if any, might a bankruptcy court use its equitable power to save a creditor from the tardy filing of a nondischargeability complaint. Part I of this Article will discuss the recent case, *Anwar v. Johnson*, where the Ninth Circuit held that a bankruptcy court could not use equity to grant relief to creditors who filed their nondischargeability complaint after a strict deadline. Part II will discuss the divide between the so-called “jurisdictional” and “procedural” courts, and whether such distinctions actually matter

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<sup>5</sup> Fed R. Bankr. P. 4007(c) (emphasis added).

<sup>6</sup> See *Farouki v. Emirates Bank Int'l, Ltd.*, 14 F.3d 244, 248 (4th Cir. 1994) (finding that bankruptcy rules “[do] not preclude the bankruptcy court from exercising its equitable powers in extraordinary cases”).

<sup>7</sup> *Anwar v. Johnson*, 720 F.3d 1183 (9th Cir. 2013).

for litigants. Finally, Part III will discuss the implications for attorneys practicing in either jurisdiction, in light of the *Anwar* decision and other developments in the law

## I. The *Anwar v. Johnson* Decision

In *Anwar v. Johnson*, two creditors sought to file nondischargeability complaints against their former employers who had filed voluntary petitions for bankruptcy under chapter 7.<sup>8</sup> Unfortunately for the creditors in *Anwar*, their attorney did not comply with the strict deadline of Rule 4007(c).<sup>9</sup> In particular, in *Anwar*, the creditors' attorney waited until the eve of the deadline to begin the two-step electronic filing process, and computer-related difficulties caused the attorney to miss the deadline.<sup>10</sup> Upon motion by the debtors, the bankruptcy court dismissed the nondischargeability complaints as untimely.<sup>11</sup> The bankruptcy court determined that it could not grant the creditors an extension to file because the court found that it lacked the discretion to grant a retroactive extension under Rule 4007(c).<sup>12</sup> Upon a *de novo* review, the district court affirmed.<sup>13</sup>

The Ninth Circuit also upheld the dismissal of the complaints, opining that the Federal Rules of Bankruptcy Procedure did not afford the bankruptcy court the discretion to retroactively extend the deadline for the creditors to file their nondischargeability complaints.<sup>14</sup> The Ninth Circuit reasoned that granting an extension to allow the creditors additional time to file their

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<sup>8</sup> *Id.* (the debtors were the two founders, principal shareholders, and officers of the bankrupt Xperex Corporation. Amina Anwar and David McClanahan sought to file nondischargeability complaints for debts owed to them as employees).

<sup>9</sup> *Id.* at 1184.

<sup>10</sup> *Id.* at 1185 n.3 (the record showed that the legal secretary for Anwar's counsel, who was responsible for electronic filings encountered difficulties while converting the nondischargeability complaints and attachments into Portable Document Format ("PDF") files in accordance with local rules. Because of these difficulties the filings of both Anwar and McClanahan's complaints were not completed until after the midnight deadline).

<sup>11</sup> *Id.*

<sup>12</sup> *Id.* at 1184.

<sup>13</sup> *Id.* at 1186.

<sup>14</sup> *Id.*

complaints would directly conflict with the plain language of Rules 4007(c) and 9006(b)(3).<sup>15</sup>

The Ninth Circuit also noted, the strict deadline of Rule 4007(c) differs from other deadlines set by the bankruptcy rules where courts may extend deadlines at any time upon a showing of good cause or excusable neglect.<sup>16</sup>

The creditors had argued that the bankruptcy court should have provided them relief in equity because the filings were completed less than one hour after the deadline,<sup>17</sup> and the debtors would not be prejudiced by an extension.<sup>18</sup> However, the *Anwar* court confirmed that the equitable powers of bankruptcy courts could only be exercised within the confines of the Bankruptcy Code and the Federal Rules of Bankruptcy Procedure.<sup>19</sup> Limitations placed on the bankruptcy court's equitable powers means that courts cannot exercise their equitable powers out of "a vague sympathy for particular litigations" when faced with clear guidance from the Bankruptcy Code or the Federal Rules of Bankruptcy Procedure.<sup>20</sup>

## II. Are Nondischargeability Complaint Deadlines "Jurisdictional" or "Procedural"?

In the *Anwar* decision, the Ninth Circuit reaffirmed its commitment to what has been described as the "jurisdictional" view on the deadlines relating to the filing of

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<sup>15</sup> Rule 9006(b)(3) of the Federal Rule of Bankruptcy Procedure provides, in relevant part, for a discretionary extension of time for filing nondischargeability complaints but "only to the extent and under the conditions stated under [Rule 4007(c)]".

<sup>16</sup> *Anwar*, 720 F.3d 1183, 1187; see also, *In re Casey*, 198 B.R. 918, 921 (Bankr. S.D. Cal. 1996) (finding that good cause and excusable neglect extensions could be applied to bankruptcy rules governed by Rule 9006(b)(1)).

<sup>17</sup> *Id.* at 1186 (the filing of the complaints against one of the debtors was completed at 12:26 a.m. and against the other at 12:38 a.m. after the midnight deadline).

<sup>18</sup> Bankruptcy courts have been called courts of equity because "bankruptcy proceedings themselves are inherently equitable in nature" *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989). However, the equitable powers of the bankruptcy courts are granted by statute. Section 105(a) of the Bankruptcy Code authorizes the bankruptcy court to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of [the Bankruptcy Code]"; see also *In re Anwiler*, 958 F.2d at 925 (9th Cir. 1992).

<sup>19</sup> *Anwar*, 720 F.3d at 1187; *NorthwestBank Worthington v. Ahlers*, 485 U.S. 197, 206 (1988) ("whatever equitable powers remain the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code").

<sup>20</sup> *Baldwin Cnty. Welcome Ctr. v. Brown*, 466 U.S. 147, 152 (1984)

nondischargeability complaints.<sup>21</sup> “Jurisdictional” courts are unlikely grant relief to litigants in the face of a clear directive from the Bankruptcy Code or the Federal Rules of Bankruptcy Procedure, absent extraordinary circumstances.<sup>22</sup> In contrast to this strict or “jurisdictional” position, some courts view bankruptcy deadlines as merely “procedural.” These “procedural” courts are more likely to exercise equitable discretion to grant certain nondischargeability petitioners relief, even if a deadline has passed.<sup>23</sup> As the *Anwar* court noted, the split exists largely because “the U.S. Supreme Court has not expressly addressed whether [Rule] 4007(c)’s filing deadline admits of any equitable exceptions.”<sup>24</sup>

However, the Supreme Court, in *Kontrick v. Ryan*, did acknowledge the split.<sup>25</sup> The *Kontrick* case involved a nondischargeability complaint under the related Rule 4004 of the Federal Rule of Bankruptcy Procedure, and the issue of whether a debtor who waits until a judgment on the merits of an untimely nondischargeability complaint forfeits his or her untimeliness defense.<sup>26</sup> The Court took note of the important role that deadlines play under the Bankruptcy Code:

First, they inform the pleader, *i.e.*, the objecting creditor, of the time he has to file a complaint. Second, they instruct the court on the limits of its discretion to grant motions for complaint-filing-time enlargements. Third, they afford the debtor an affirmative defense to a complaint filed outside the Rules . . . limits.<sup>27</sup>

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<sup>21</sup> See, e.g., *In re Kennerley*, 995 F.2d 145, 147 (9th Cir. 1993) (finding that Rule 4007(c)’s “time limit cannot be extended unless a motion is made before the 60-day limit expires”).

<sup>22</sup> See *In re Barley*, 130 B.R. 66, 69 (Bankr. N.D. Ind. 1991) (“A timely complaint is a jurisdictional prerequisite to a creditor’s right to relief”); *In re Poskanzer*, 146 B.R. 125, 127 (D.N.J. 1992) (“A bankruptcy court possesses limited discretion . . . to permit filing beyond the bar date”); see also, *In re Tanner*, 77 B.R. 897 (Bankr. N.D. Ala. 1987) (finding that the bankruptcy court lacks jurisdiction over a complaint filed outside the sixty-day time limit).

<sup>23</sup> See *In re Begue*, 176 B.R. 801, 803 (Bankr. N.D. Ohio 1995) (treating Rule 4007(c)’s deadline like a statute of limitations subject to certain equitable principles like tolling).

<sup>24</sup> *Anwar*, 720 F.3d at 1188.

<sup>25</sup> 540 U.S. 443 (2004).

<sup>26</sup> *Id.* at 459 (holding against the debtor because a defense is lost if it is not included in the answer or amended answer under the bankruptcy rules).

<sup>27</sup> *Id.* at 456.

Ultimately, the Court concluded that the deadlines set by the Federal Rules of Bankruptcy do not implicate the Bankruptcy Court’s subject matter jurisdiction,<sup>28</sup> directly rejecting the debtor’s interpretation of the “jurisdictional” view.<sup>29</sup> However, the Court did not reach the issue of whether equitable tolling or any other equity-based exception could excuse the untimely filing of a complaint.<sup>30</sup> Following *Kontrick*, the remaining distinction between “jurisdictional” and “procedural” courts exists largely over this question.<sup>31</sup>

The importance of deadlines undermines the rationale of the stricter, “jurisdictional” courts, even when litigants would face harsh results. These courts further justify this approach by citing Congressional intent to “establish a system whereby certain types of nondischargeability claims would be automatically cut off . . . in order to prevent debtors from being harassed by creditors after their claims had been discharged in bankruptcy.”<sup>32</sup>

In contrast, the “procedural” courts may allow for certain equitable extensions of Rule 4007(c) and other bankruptcy deadlines in limited circumstances, where the jurisdictional courts would not.<sup>33</sup> These courts view the Federal Rules of Bankruptcy Procedure as distinct from the “the statutory law of bankruptcy.”<sup>34</sup> Thus, a “procedural” court would likely view Rule 4007(c)’s deadline as functioning like a statute of limitations, and as such: “subject to the defenses of

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<sup>28</sup>*Id.* at 454 (“In short, the filing deadlines prescribed in Bankruptcy Rules . . . are claim-processing rules that do not delineate what cases bankruptcy courts are competent to adjudicate”).

<sup>29</sup>*Id.* at 454 (explaining the “jurisdictional” misnomer by noting that “Courts, including this Court . . . have been less than meticulous” and have used “the term ‘jurisdictional’ to describe emphatic time prescriptions in rules of court”).

Courts, including this Court, it is true, have been less than meticulous in this regard; they have more than occasionally used the term “jurisdictional” to describe emphatic time prescriptions in rules of court.

<sup>30</sup>*Id.* at 457 (“Whether the Rules, despite their strict limitations, could be softened on equitable grounds is therefore a question we do not reach”).

<sup>31</sup>*Id.* at 458 n.11.

<sup>32</sup>*In re Benedict*, 90 F.3d 50, 54 (2d Cir. 1996); *see also Neeley v. Murchison*, 815 F.2d 345, 347 (5th Cir. 1987) (“Rule 4007 is designed to implement . . . a heavy burden on the creditor to protect his rights”).

<sup>33</sup> Even “jurisdictional” courts may be willing to consider extraordinary exceptions. *See, Anwar*, 720 F.3d at 1188 n. 6 (“We need not, and do not, reach the question of whether external forces that prevented any filings—such as emergency situations, the loss of the court’s own electronic filing capacity, or the court’s affirmative misleading of a party—would warrant such an exception”).

<sup>34</sup>*In re Welsh*, 138 B.R. 630, 631 (Bankr. M.D. Fla. 1992).

waiver, estoppel, and equitable tolling.”<sup>35</sup> However, even “procedural” courts are careful to ensure that any exercise of equitable discretion is “consistent with the plain language of the rules.”<sup>36</sup> Additionally, a “procedural” court will usually require a showing of good faith by the party seeking relief from its own untimely filing.<sup>37</sup>

Generally, when it is the court’s own error that causes a party to miss a filing deadline, a “procedural” court will permit an untimely filing.<sup>38</sup> Even traditional “jurisdictional” courts would likely excuse the late filing of a complaint when “unique circumstance[s]” present, such as if a party relied upon an incorrect or misleading deadline that was incorrectly set by the court itself.<sup>39</sup>

### III. Analysis

*Anwar* illustrates the danger of waiting until the last minute to file pleadings; whether the filing is done electronically or more traditionally.<sup>40</sup> Even within the “procedural” jurisdictions, where the court might be more open to equitable exceptions, it is good practice to ensure that there is ample time to meet the hard deadlines set forth in the Bankruptcy Code and the Federal Rules of Bankruptcy Procedure, especially those set under Rules 4004 and 4007. Additionally, absent a clear statement from a circuit court, it is often difficult to determine whether a particular jurisdiction ascribes to either the “jurisdictional” or “procedural” view on deadlines,<sup>41</sup> or if the

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<sup>35</sup> United States v. Locke, 471 U.S. 84, 94 (1985).

<sup>36</sup> *In re Santos*, 112 B.R. 1001, 1006 (B.A.P. 9th Cir. 1990).

<sup>37</sup> See *In re Hickey*, 58 B.R. 106, 109 (Bankr. S.D. Ohio 1986).

<sup>38</sup> See *In re Themy*, 6 F.3d 688, 690 (10th Cir. 1993) (permitting a filing outside of the 60-day window when the court stated deadline was incorrect because a “creditor should be entitled to rely on the court’s orders”).

<sup>39</sup> See *In re Kennerley*, 995 F.2d 145, 147-48 (9th Cir. 1993) (noting that the bankruptcy court’s power to correct its own errors also derives from 11 U.S.C. § 105[a]); see also *Slimick v. Silva*, 928 F.2d 304 (9th Cir. 1990) (holding that a party faced with a knowingly mistaken or ambiguous deadline still bears the burden of seeking a clarification from the court).

<sup>40</sup> See n. 10, *supra*.

<sup>41</sup> Compare *Farouki v. Emirates Bank Int’l, Ltd.*, 14 F.3d 244, 248 (4th Cir. 1994) (finding Rule 4004 to be subject to equitable defenses), with *In re Alton*, 837 F.2d 457, 459 (11th Cir. 1988) (finding Rule 4007 confers no discretion to grant an untimely motion to extend the time to object, even if the creditor lacked notice of the bar date).

distinction even matters.<sup>42</sup> Moreover, it is unlikely that even in a more forgiving “procedural” court that the mistake made by the *Anwar* creditors could have been remedied in equity.

It is important for practitioners to keep in mind that even though bankruptcy courts have been called courts of equity, they have also been described as “specialized court[s] of limited jurisdiction applying statutory law that embodies a particular, often changing, social objective.”<sup>43</sup> Unfortunately, for practitioners, that social objective does not include saving creditors from their attorney’s filing mistakes. The failure to adhere to a known deadline could expose a practitioner to malpractice claims.<sup>44</sup> Indeed, studies show that over twenty-one percent of all legal malpractice claims arise from lawyers missing deadlines.<sup>45</sup>

While computers in many ways have streamlined private practice and court filing procedure, but these systems are not guaranteed to make life any simpler for lawyers. The *Anwar* court noted that “[p]aper filing systems present their own unique opportunities for parties to miss their deadlines” and in that rules pertaining to deadlines will still apply to older, as well as emerging ways of filing.<sup>46</sup>

## Conclusion

Attorneys representing creditors seeking to file nondischargeability complaints, like all attorneys, must be aware of upcoming deadlines in court proceedings and must know ahead of time how the filing systems work. In today’s practice it is increasingly necessary for attorneys and

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<sup>42</sup> See generally, Kontrick, *supra*.

<sup>43</sup> Hon. Marcia S. Krieger, “the Bankruptcy Court Is A Court of Equity”: What Does That Mean?, 50 S.C. L. REV. 275, 310 (1999).

<sup>44</sup> Jessica Belskis, *Electronic Case Filing: Is Failure to Check Email Related to an Electronically Filed Case Malpractice?*, 2 SHIDLER J. L. COM. & TECH. 13 (2005); see also *The Top Ten Malpractice Traps & How to Avoid Them*, MONT. LAW., Jan. 2000, at 7 (Calendaring errors remain the leading cause of malpractice claims).

<sup>45</sup> Manuel R. Ramos, *Legal Malpractice: The Profession’s Dirty Little Secret*, 47 VAND. L. REV. 1657, n. 89 (1994).

<sup>46</sup> *Anwar*, 720 F.3d at 1188.

support staff to possess the proper computer skills to use these systems effectively.<sup>47</sup> If the court is using an electronic filing system, then the attorney should allow for extra time in case of unforeseeable computer errors that would otherwise cause him or her to miss a filing deadline. Even if an attorney is practicing in a more forgiving “procedural” court, there is still no guarantee that a bankruptcy could will be use what limited equitable power it retains to provide his or her client relief from a tardy filing.

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<sup>47</sup> See Alane A. Becket, *Back to Basics: ECF's Benefits Should Be Approached with Caution*, AM. BANKR. INST. J., February 2006, at 14 (“At this point, the vast majority of bankruptcy courts in the country have converted to CM/ECF. Almost every court that is CM/ECF operational also accepts electronic filings”).