The Holy Grail: Recent Developments in Bankruptcy Discharge Issues

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The discharge – the release of personal liability for your debts – is one of the primary goals for people seeking relief through bankruptcy. What happens when a specific debt is challenged? Or even worse, what happens when the entire discharge is at risk? There are two statutes that govern the discharge in bankruptcy, 11 U.S.C. § 523 and 11 U.S.C. § 727. This article will provide a brief refresher on the debts excepted from discharge in 11 U.S.C. § 523 and how a debtor's entire discharge can be denied or revoked using 11 U.S.C. § 727.

11 U.S.C. § 523(a)[1]

Section 523(a) of the Code excludes various categories of debts from the discharge granted to individual debtors. The 21 types of debt excepted from discharge under **Chapters 7, 11, and 12** are:

11 U.S.C. § 523(a)(1)

Generally, tax debts arising from tax returns due within three years before a debtor's bankruptcy filing are excepted from discharge in bankruptcy. If a return was required and was filed or given more than three years before the bankruptcy petition was filed, the taxes *may* be discharged if the return was not fraudulent and there was no willful attempt to evade taxes.

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[1] The authors extend sincere gratitude to Kenneth C. Edstrom, who has generously allowed the use of his summaries of Section 523(a) debt categories from his previous publication, I TAKE EXCEPTION TO YOUR DISCHARGE: Current Developments in Dischargeability Actions, July 17, 2019, *available at* https://sapientialaw.com/wp-content/uploads/2019/07/I-Take-Exception-to-Your-Discharge-Notes.pdf (unless otherwise specified, all links in this article were last visited on January 31, 2023). The reader should refer to the Code provisions for a complete description of the debt categories.

NOTE: The tax deadline for 2019 income tax returns was extended to July 15, 2020.[2]

This generally means that 2019 income taxes will be dischargeable after July 17, 2023.

The tax deadlines for 2020 returns were also extended to May 17, 2021.[3]

- ***United States v. Clayton***, 468 B.R. 763, 770 (M.D.N.C. 2012) – An attorney with a "high-paying job" filed a summary judgment motion to the I.R.S.'s action that sought recovery of alleged unpaid taxes and penalties because he had received a Chapter 7 discharge. Mr. Clayton's motion was denied. In making this determination, the court, among other things, analyzed the debtor's conduct to determine if the debtor voluntarily and intentionally violated his duty to pay taxes, using "badges of fraud." Badges of fraud include: " '(1) the recurrence of the understatement of income for more than one tax year, (2) the understatement of income, (3) implausible or inconsistent explanations of behavior, (4) inadequate records, (5) transfer of assets to a family member, (6) transfer for inadequate consideration, (7) transfer that greatly reduced assets subject to I.R.S. execution, and (8) transfers made in the face of serious financial difficulties.' " *Hassan v. United States* (*In re Hassan*), 301 B.R. 614, 620 (S.D.Fla.2003) (quoting *In re Spiwak*, 285 B.R. 744, 751 (S.D.Fla.2002)). However, lavish spending coupled with the knowledge of tax debts further indicates that a debtor acts willfully to evade his tax obligations. *In re Hamm*, 356 B.R. at 285–86 (considering a debtor's significant expenditures when determining if a debtor's actions met the mental state requirement of section 523(a)(1)(C)). Indeed, "[a] typical case of non-dischargeable tax liability pursuant to § 523 of the Bankruptcy Code often involves debtors who ... live a lavish lifestyle they cannot afford ... while making no effort to satisfy their tax liability." *Hawkins*, 447 B.R. at 296 (alternations in original) (quoting *Rhodes v. United States* (*In re Rhodes*), 356 B.R. 229, 235 (Bankr.M.D.Fla.2006)). The court found that Mr. Clayton prioritized his discretionary spending over his income tax obligations by spending over $10,000 per month on a mortgage, collecting exotic animals, paying monthly funds to his ex-wife above their agreed-upon separation agreement, private school college tuition, purchasing luxury vehicles for himself and his children, etc. *Clayton*, 468 B.R. at 772.

- ***In re Hillsborough Holdings Corp***., 599 B.R. 193 (Bankr. M.D. Fla. March 29, 2019) – The Coal Act premiums are taxes and were not discharged in a prior bankruptcy case.

- ***In re Sienega***, 18 F.4th 1164 (9th Cir. December 6, 2021) – Formal tax returns must be filed for tax obligations to be discharged. "Informal" faxes not signed by the debtor did not constitute returns.

[2] Internal Revenue Service: Notice 2020-17, *available at* https://www.irs.gov/pub/irs-drop/n-20-17.pdf. *See also* https://www.irs.gov/newsroom/payment-deadline-extended-to-july-15-2020.
[3] Internal Revenue Service: Notice 2021-21, *available at* https://www.irs.gov/pub/irs-drop/n-21-21.pdf. *See also* https://www.irs.gov/newsroom/tax-day-for-individuals-extended-to-may-17-treasury-irs-extend-filing-and-payment-deadline.

11 U.S.C. § 523(a)(2)

Section 523(a)(2) excepts from discharge 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.

- ***In re Osborne***, 951 F.3d 691 (5th Cir. March 10, 2020) – A fraudulent statement by a debtor's partner or agent can be imputed to the debtor under section 523(a)(2)(B) of the Bankruptcy Code, making the debt nondischargeable.

- ***In re Wigley***, 620 B.R. 87 (B.A.P. 8th Cir. September 25, 2020) – Creditor Lariat obtained a state court judgment finding both Wigleys (married couple) jointly and severally liable for $795,000 in damages for fraudulent transfers. The wife filed a Chapter 11 petition, and Creditor Lariat filed a claim based on the fraudulent-transfer judgment. Lariat sought to except its debt from the wife's discharge under section 523(a)(2)(A) of the Bankruptcy Code that the transfers were actually fraudulent. The court concluded that actual fraud elements established by *Husky International Electric Inc. v. Ritz*, 136 S. Ct. 1581 (2016), were met.

- ***In re Gaddy***, 977 F.3d 1051 (11th Cir. September 29, 2020) – Court dismissed the creditor's adversary proceeding to exempt from discharge the lender's $9 million claim because the loans were not obtained by fraud.

- ***In re Fusion Connect, Inc***., 634 B.R. 22 (S.D.N.Y. September 2, 2021) – Chapter 11 Debtor, a telecommunications company (Fusion), received a $4.2 million penalty from the F.C.C. for misleading telemarketing calls. Fusion received a discharge, and F.C.C. challenged the dischargeability of the F.C.C. penalty. The District Court reversed the lower court's decision, declaring that the F.C.C. fine was exempt from discharge because U.S. Supreme Court in *Cohen v. de la Cruz,* 523 U.S. 213 (1998), interpreted section 523(a)(2)(A) broadly to except from discharge all debts arising from the debtor's acquisition of money or property through fraudulent conduct. The F.C.C. penalty occurred because of fraudulent conduct and was not dischargeable.

- ***Apollo MedFlight, L.L.C. v. Lowry***, 2021 Bankr. LEXIS 2768, 2021 WL 4558296 (Bankr. E.D.N.C. 2021): Insurer Blue Cross Blue Shield mailed a $47,565.00 check payable to the debtor covering the life flight bill along with an Explanation of Benefits providing that "B.C.B.S.N.C. makes payment directly to you for services render [sic] by nonparticipating providers. You are responsible for paying the nonparticipating provider bills." The debtor (surprisingly) did not pay for the medical helicopter and instead deposited the check into her bank account and used it for her personal expenses and purposes. Furthermore, the debtor's sister made numerous representations to BCBS and Apollo that facilitated the deposit. The court imputed all relevant statements and knowledge of the debtor’s sister to the debtor as the debtor's agent under North Carolina agency law. It held the debt nondischargeable under § 523(a)(2)(A). The court declined to hold it nondischargeable under (a)(4) as larceny or (a)(6) as willful and malicious injury to the property of another.

- ***Nationwide Judgment Recovery, Inc. v. Sheppard*** (In re Sheppard), 2022 Bankr. LEXIS 531, 2022 WL 58780 (Bankr. E.D.N.C. 2022): The Court dismissed the complaint under Rule 12(b)(6) that sought to except from discharge a fraudulent transfer judgment against “net winner” in a Ponzi scheme because there was no allegation that false pretenses, a false representation, or actual fraud led to the "winnings."

- ***O’Connor v. Burg*** (In re Burg), 641 B.R. 120, (Bankr. S.D. Tex. 2022): Attorney was a creditor who agreed to a contingency fee of 35% of reduction in indebtedness from successful challenges of mortgage debts of a former client, totaling $170,591.02. The attorney sought to collect the fee. As a result, the debtor broke off communications, took out a reverse mortgage on her house to reduce equity, and then filed for Chapter 7 petition. The court held that the debtor never had any intention to sell the home to pay the debt as initially represented or to otherwise pay the fee, held the attorney fee as nondischargeable, and awarded attorney fees to the attorney creditor.

- ***Bartenwerfer v. Buckley***, No. 21-908, 860 Fed. App’x. 544 (9th Cir. 2021), *cert. granted*, 142 S. Ct. 2675 (2022) – Supreme Court heard oral arguments on December 6, 2022, on whether a debtor may discharge in bankruptcy a debt for money obtained by her business partner’s fraud when the debtor herself did not know about the fraud. Here, a creditor challenged the dischargeablilty of an innocent partner’s judgment under 11 U.S.C. §523(a)(2)(A) because the money was obtained through fraud. The court determined that the innocent partner did not know about the partner's fraud. The Ninth Circuit reversed the lower court decisions holding that fraud could not be imputed to the innocent partner because she did not know of it, and her debt was therefore dischargeable. The Ninth Circuit held that a person could not escape liability of her business partner's fraud due to lack of knowledge under *Strang v. Bradner*, 114 U.S. 555, 561 (1885). The Ninth Circuit emphasized that under *Strang*, “…if, in the conduct of partnership business, . . . one partner makes false or fraudulent misrepresentations of fact to the injury of an innocent person, . . . his partners cannot escape pecuniary responsibility therefor upon the ground that such misrepresentations were made without their knowledge. This is especially so when . . . the partners, who were not themselves guilty of wrong, received and appropriated the fruits of the fraudulent conduct of their associate in business." The innocent partner argues that *Strang* has been misinterpreted.

11 U.S.C. § 523(a)(3)

This exception to discharge excepts debts that are not listed in the petition. The policy behind this exception is based on due process as an unscheduled debt would mean that the creditor does not receive notice and has no opportunity to participate in the case. This self-effectuating exception applies if the debt is not scheduled "in time to permit (A) if such debt is not of a kind specified in paragraph (2), (4), or (6) of this subsection, timely filing of a proof of claim, unless such creditor had notice or actual knowledge of the case in time for such timely filing; or (B) if such debt is of a kind specified in paragraph (2), (4), or (6) of this subsection, timely filing of a proof of claim and timely request for a determination of dischargeability." 11 U.S.C. § 523(a)(3) (emphasis added).

11 U.S.C. § 523(a)(4)

All bankruptcy claims based on "fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny" are non-dischargeable.

- **Spring Valley Produce, Inc. v. Forrest (In re Forrest)**, No. 21-12133, 2022 WL 3908803 at *1 (11th Cir. Aug. 31, 2022). The Eleventh Circuit recently enunciated the test for determining whether a debtor was acting in a "fiduciary capacity" for purposes of § 523(a)(4): "First, the fiduciary relationship must have (1) a trustee, who holds (2) an identifiable trust res, for the benefit of (3) an identifiable beneficiary or beneficiaries….Second, the fiduciary relationship must define sufficient trust like duties imposed on the trustee with respect to the trust res and beneficiaries to create a technical trust….Third the debtor must be acting in a fiduciary capacity before the act of fraud or defalcation creating the debt."

- ***In re Piercy***, 21 F.4th 909 (6th Cir. December 29, 2021) – Sixth Circuit reversed the district court's decision, holding that the debt was nondischarageable as there was no express or technical trust between the debtors and creditor. The Sixth Circuit stated that under Tennessee statutes, partners owe each other the fiduciary duties of loyalty and care and thus could be nondischargeable under § 523(a)(4). The case was remanded to the bankruptcy court.

- ***BRRRT Properties, LLC et al. v. Pfeiffer et al***., --- F.Supp.3d ----, 2022 WL 3444841 (E.D.N.C. July 13, 2022): The district court upheld a bankruptcy court's finding that $235,174.00 stemming from a failed property flipping business was not nondischargeable debt but focused its analysis on Section 523(a)(4) which provides no discharge "from any debt ... for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny.” 11 U.S.C. § 523(a)(4). Here, the debtor misused funds intended for other properties from the plaintiff. The bankruptcy court focused its decision to hold the amount nondischargeable on the debtor's actions. It ruled the debt nondischargeable under 11 U.S.C. § 523(a)(2) due to the debtor's misrepresentations during a real joint venture with the creditor. The debtor’s misrepresentations, which, among others, included walking the creditor through a property under construction while representing that he had purchased the property when in fact, he had not, presented a falsified HUD-1, and did not subsequently correct these representations.

11 U.S.C. § 523(a)(5)

This paragraph excepts from discharge any “domestic support obligation,” which is defined by 11 U.S.C. § 101(14A). All other obligations awarded to a spouse or child by a family court, such as property settlement, fall under 11 U.S.C. § 523(a)(15), which does not apply in chapter 13. Regardless of whether a family court order describes an obligation as domestic support or property settlement, the bankruptcy court may look at the characteristics of the agreement to determine if an obligation is a domestic support obligation under federal law without regard to state law.

11 U.S.C. § 523(a)(6)

Section 523(a)(6) of the Bankruptcy Code provides that a debt “for willful and malicious injury by the debtor to another” is not dischargeable. 11 U.S.C. § 523(a)(6).

- ***In re Gaddy***, 977 F.3d 1051 (11th Cir. September 29, 2020) – Actions taken by a debtor after a debt is incurred, even if taken to thwart a creditor’s collection efforts by fraudulently conveying assets, do not create a separate injury for the purposes of section 523(a)(6).

- ***In re Hill***, 957 F.3d 704 (6th Cir. May 4, 2020) – State court finding Debtor (Hill) liable for tortious interference claim tantamount to the elements of § 523(a)(6) and judgment is not dischargeable.

- ***In re Cleary Packaging, L.L.C.***, 36 F.4th 509 (4th Cir. June 7, 2022) – Fourth Circuit on a direct appeal held that section 1192(2) provides discharges to small business debtors, whether they are individuals or corporations, except regarding the 21 kinds of debts listed in section 523(a). Here, Vincent Cleary, one of several the principals of a family-run company (Creditor), left the family business and created a new company (the "Debtor") to operate in the same line of business, taking with him various employees subject to non-compete clauses, customer lists and other proprietary material of the creditor. The creditor sued the Debtor and Vincent in state court for various intentional business torts, winning a judgment of over $4 million. Vincent filed a Chapter 11 case for the Debtor under **Subchapter V**. The Creditor brought a timely action to object to the discharge of its claim under Code section 523(a)(6). Section 1192(2) excepts from discharge under a plan any debts "of the kind specified in section 523(a) of this title." Section 523(a)(6) prevents the discharge of any debt "for willful and malicious injury by the debtor to another entity or to the property of another entity." Granting the debtor's motion to dismiss the complaint, the Bankruptcy Court agreed with the debtor that because by its terms section 523(a), which is incorporated by section 1192(2), applies only to "an individual debtor" and it therefore, does not apply to entities such as the debtor. The Fourth Circuit, on a direct appeal, reversed. Every bankruptcy court to address the issue in a written opinion to date has ruled contrary to the Fourth Circuit. See ***Jennings v. Lapeer Aviation, Inc. (In re LaPeer Aviation, Inc.),*** Adv. No. 22-03002, 2022 WL 1110072 (Bankr. E.D. Mich. Apr. 13, 2022); ***Catt v. Rtech Fabrications, LLC (In re Rtech Fabrications LLC),*** 635 B.R. 559 (Bankr. D. Idaho 2021); ***Cantwell-Cleary Co., Inc., v. Cleary Packaging (In re Cleary Packaging, LLC),*** 630 B.R. 466 (Bankr. D. Md. 2021), *rev'd* 36 F.4th 509 (4th Cir. 2022); ***Gaske v. Satellite Rest., Inc. Crabcake Factory USA (In re Satellite Rest., Inc. Crabcake Factory USA),*** 626 B.R. 871 (Bankr. D. Md. 2021); ***Avion Funding, LLC v. GFS Industries, LLC (In re GFS Industries, LLC)***, Case No. 22-05052, 2022 WL 16858009 (Bankr. W.D. Tex. Nov. 10, 2022).

- ***In re Hulse***, 2022 WL 16826561 (B.A.P. 10th Cir. November 8, 2022) – Plaintiff purchased a dental practice from Hulse and later discovered questionable billing practices. Plaintiff sued Hulse and obtained an award in arbitration. Hulse filed bankruptcy, and the plaintiff filed an adversary proceeding seeking a determination that the arbitration award should be excepted from discharge under section 523(a)(6) of the Bankruptcy Code as a "willful and malicious injury by the debtor to another entity." The court granted the plaintiff's summary judgment motion, and Hulse appealed. The B.A.P. held that the Bankruptcy Court erred in granting summary judgment and that genuine issues of material fact remained on the plaintiff's 523(a)(6) claim because (1) For an injury to be "willful" under section 523(a)(6), there must be a deliberate or intentional injury, not merely a deliberate or intentional act that leads to injury; and (2) For an injury to be "malicious," evidence of the debtor's motives, including any claimed justification or excuse, must be examined to determine whether the requisite "malice' is present.

11 U.S.C. § 523(a)(7)

11 U.S.C. § 523(a)(7) requires three elements for debts to fall under its dischargeability exclusion: (1) The charges must be "for a fine, penalty, or forfeiture." The charges must be

"payable to and for the benefit of a governmental unit." Finally, (3) The charges must also "not [be] compensation for actual pecuniary loss."

- ***In re Albert-Sheridan***, 960 F.3d 1188 (B.A.P. 9th Cir. June 10, 2020) – Discovery sanctions owed to a private party but imposed by California statutes are dischargeable.

11 U.S.C. § 523(a)(8)

Unless the debt "would impose an undue hardship," this paragraph excepts from discharge two different categories of educational debt. The first category is "(i) an educational benefit overpayment or loan made, insured, or guaranteed by a governmental unit or nonprofit institution; or (ii) an obligation to repay funds received as an educational benefit, scholarship, or stipend." 11 U.S.C. § 523(a)(8)(A). The second category is "any other educational loan that is a qualified educational loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986, incurred by a debtor who is an individual." 11 U.S.C. § 523(a)(8)(B).

> **NOTE**: On November 17, 2022, the U.S. Department of Justice, with the U.S. Department of Education, announced a new process for handling cases in which individuals seek to discharge their federal student loans in bankruptcy. The goal of the new process is to help ensure consistent treatment of the discharge of federal student loans, reduce the burden on borrowers of pursuing such proceedings and make it easier to identify cases where discharge is appropriate.[4] The National Consumer Law Center (NCLC) has published a manual describing a ten-step process to assist debtors in discharging their student loan debt.[5]

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[4] U.S. Dept. of Justice, Press Release No. 22-1231, November 17, 2022, *available at* https://www.justice.gov/opa/pr/justice-department-and-department-education-announce-fairer-and-more-accessible-bankruptcy.

[5] NCLC Publication titled New Process to Discharge Student Loans in Bankruptcy describes the Guidance issued by the Department of Justice on how bankruptcy debtors can obtain discharges of their student loans using a ten-step process. John Rao, New Process to Discharge Student Loans in Bankruptcy, NCLC (December 12, 2022), *available at* https://library.nclc.org/article/new-process-discharge-student-loans-bankruptcy.

- ***Crocker v. Navient Solutions***, L.L.C., 941 F.3d 206 (5th Cir. October 21, 2019) – Private bar preparation loans are dischargeable.

- ***In re Rosenberg***, 610 B.R. 454 (Bankr. S.D.N.Y. January 7, 2020) – Lawyer Kevin J. Rosenberg filed bankruptcy seeking to discharge his student loans. The bankruptcy court ruled that Rosenberg's student debt could be discharged. Judge Cecelia G. Morris also criticized the harsh results commonly associated with the *Brunner* test, stating that debtors cannot discharge student loan debt in bankruptcy because of the misapplication of *Brunner*.

- ***In re McDaniel***, 973 F.3d 1083 (10th Cir. August 31, 2020) - Section 523(a)(8)(A)(ii) of the Bankruptcy Code does not apply to exempt from discharge certain private student loans.

- ***Homaidan v. Sallie Mae Inc.***, 3 F.4th 595 (2d Cir. July 15, 2021) – The Second Circuit affirmed the opinion of the U.S. Bankruptcy Court for the Eastern District of New York, which held that private student loans are not excepted from discharge under Section 523(a)(8)(A)(ii) of the Bankruptcy Code, which excepts from discharge "an obligation to repay funds received as an educational benefit, scholarship, or stipend." 11 U.S.C. § 523(a)(8)(A)(ii). The court held that a private loan is excepted from discharge under Section 523(a)(8)(B) only if it was "made to individuals attending eligible schools for certain qualified expenses."

- ***Mader v. Experian Info. Sols., Inc.***, Nos. 20-3073, 21-2171, 2023 U.S. App. LEXIS 79, at *11-17 (2d Cir. January 4, 2023) – Second Circuit held that if legal or factual disputes must be resolved before deciding whether a private student loan was excepted from discharge under Section 523(a)(8)(A)(i), there is no violation of the Fair Credit Reporting Act (F.C.R.A.) if the credit reporting agency shows the debt to be outstanding. This case has been interpreted to limit the *Homaidan* holding.

11 U.S.C. § 523(a)(9)

This paragraph excepts from discharge debts resulting from driving, boating, or flying while intoxicated.

11 U.S.C. § 523(a)(10)

This paragraph excepts from discharge any debt that was or could have been listed or scheduled in a prior case in which the debtor waived or was denied a discharge under § 727(a)(2), (3), (4), (5), (6), or (7). This exception is a codification of the principle of res judicata.

11 U.S.C. § 523(a)(11)

This paragraph excepts from discharge any debt resulting from fraud or defalcation in connection with a federal depository institution or insured credit union.

11 U.S.C. § 523(a)(12)

This paragraph excepts from discharge any debt resulting from failure to maintain commitments concerning the capital of a federal depository institution.

11 U.S.C. § 523(a)(13)

This paragraph excepts from discharge debts resulting from restitution orders under the federal criminal code.

11 U.S.C. § 523(a)(14)

This paragraph excepts from discharge debts for funds borrowed to pay nondischargeable taxes or to pay fines or penalties imposed under federal election law.

11 U.S.C. § 523(a)(15)

This paragraph excepts from discharge obligations owed to a spouse, former spouse, or child other than a domestic support obligation related to a divorce or separation. There are only two requirements to be excepted from discharge under this provision. First, the obligation must run from the debtor "to a spouse, former spouse, or child of the debtor." Second, the obligation must be a debt other than a domestic support obligation and "incurred by the debtor in the course of a divorce or separation or connection with a separation agreement, divorce decree or other order of a court of record."

11 U.S.C. § 523(a)(16)

This paragraph excepts from discharge post-petition homeowner association fees and assessments as long as the debtor or the trustee has a legal, equitable, or possessory interest.

11 U.S.C. § 523(a)(17)

This paragraph excepts from discharge court filing fees owed by prisoners.

11 U.S.C. § 523(a)(18)

This paragraph excepts from discharge obligations to pay back 401(k) loans and other retirement plan loans.

11 U.S.C. § 523(a)(19)

This paragraph excepts from discharge certain debts arising from violations of securities laws to the extent that the debt results from a pre-petition judgment, order, consent order, decree, or settlement agreement.

A more limited list of exceptions applies to cases under **Chapter 13**. The categories of debt excepted from discharge under Chapter 13 are:

- **11 U.S.C. § 523(a) (1)(B)** – Certain Tax Debts.

- **11 U.S.C. § 523 (a) (1)(C)** - Fraudulent return or willfully attempted in any manner to evade or defeat such tax debt.
- **11 U.S.C. § 523 (a) (2)** - Fraud claims.
- **11 U.S.C. § 523 (a) (3)** - Unlisted debts.
- **11 U.S.C. § 523 (a) (4)** - Theft, conversion, or breach of fiduciary duty.
- **11 U.S.C. § 523 (a) (5)** - Domestic support obligations.
- **11 U.S.C. § 523 (a) (8)** - Student loans.
- **11 U.S.C. § 523 (a) (9)** – Debts resulting from driving, boating, or flying while intoxicated.

11 U.S.C. § 1328(a)(2).

Only ***three*** exceptions to discharge require an objecting creditor to file an adversary proceeding to determine that the relevant debt is nondischargeable.

1. 11 U.S.C. § 523 (a)(2) – Fraud/misrepresentation;
2. 11 U.S.C. § 523 (a)(4) Fiduciary; and
3. 11 U.S.C. § 523and (a)(6) – Willful/malicious injury.

See 11 U.S.C. § 523(c) (requiring the filing of a complaint regarding debts falling under Sections 523(a)(2), (4), and (6)). These debts are only excluded from the discharge if their nondischargeable is raised and determined during the bankruptcy case. Bankruptcy Rule 4007 (c) requires that these exceptions to discharge be raised within 60 days of the first day set for the 341 meeting. State courts have concurrent jurisdiction over all grounds for nondischargeability under Code § 523(a) except for (a)(2), (a)(4) and (a)(6). *See* Fed. Bankr. Rule 4007(b) Advisory Committee's Note.

Under Bankruptcy Rule 4007(b), there is no time limit for adversary proceedings ***other*** than those outlined in Bankruptcy Rule 4007(c). Fed. Bankr. Rule 4007. Exceptions for debts outside of §§ 523(a)(2), (4), and (6) can be raised during or after the bankruptcy case. These debts are automatically excepted from discharge without an adversary proceeding.

The standard of proof for the dischargeability exceptions in 11 U.S.C. § 523(a) is the preponderance of the evidence.

Collateral estoppel principles apply in discharge proceedings under 11 U.S.C. § 523(a). The record in the prior proceeding and whether the court entered findings of fact determines a court's collateral estoppel analysis.

11 U.S.C. § 727

Section 727 denies the debtor his or her <u>entire discharge</u>, and he or she remains liable for ***all pre-petition debts***. Grounds for objections under Section 727(a)(2-6) are: misusing property of the estate, concealing or destroying property prior to bankruptcy, concealing or tampering with financial information or recording, lying in connection with the bankruptcy case, failing to explain the loss of assets, and refusing to obey court orders. 11 U.S.C. § 727.

Under Section 727, the debtor's discharge may be filed by a creditor, by the trustee in the case, or by the U.S. trustee. However, the objection to discharge must be filed in a Chapter 7 or Chapter 13 bankruptcy case within 60 days after the first date set for the meeting of creditors.

However, it can be extended for “good cause” by a motion filed prior to the expiration of the original deadline. Fed. Bankr. Rule 4004.

- ***Gasson v. Premier Capital, L.L.C***., 43 F.4th 37 (2nd Cir. July 29, 2022) – Anthony Gasson was part-owner of several accounting companies that failed in 2003, resulting in judgments against him for nearly $600,000. The debtor and his wife also operated a consulting business, Soroban Inc. Premier Capital attempted to collect a judgment, and Gasson filed a Chapter 7 bankruptcy and did not disclose his interest in Soroban, Inc. Premier filed an adversary complaint asking the court to deny Gasson a discharge under section 727(a)(2)(A) of the Bankruptcy Code. The bankruptcy court, the district court, and later, the Second Circuit denied the discharge under the “continuous concealment” doctrine because the debtor concealed his interest in Soroban and hindered creditors using by using Soroban funds for personal matters, denying receiving a salary from the company, and creating the company while the I.R.S. and creditors were pursuing collections.

- ***Seaport Capital Partners, L.L.C. v. Speer*** (In re Speer), 2018 WL 2283834 (Bankr. D. Conn. May 17, 2018) – Seaport Capital Partners L.L.C. (Seaport) filed an adversary complaint against debtor Speer, objecting to the discharge of Speer's debts. The debtor obtained insurance proceeds and rental income during a bankruptcy case that she did not disclose. In denying discharge, the court cited section 727(a)(2) of the Bankruptcy Code, which allows a bankruptcy court to deny discharge to a debtor who conceals property with the intent to defraud creditors or the bankruptcy trustee. Speer’s conduct to “hinder, delay and defraud creditors” and conceal estate property included: operating her business in cash, failing to file income taxes, failing to keep financial records, and failing to disclose limited liability interests and insurance proceeds.

- ***Lynch et al. v. Hollan***, Adv. Pro. No. 19-00162, (E.D.N.C. April 2, 2021) – Discharge denied where well-educated debtor withdrew, used, and failed to keep records of $270,000+ cash within the four years prior to the petition date (§ 727(a)(3) and failed to satisfactorily explain the spending of this cash and other income (§ 727(a)(5)). The Bankruptcy Administrator brought this action.

Other considerations when § 727 actions arise are ***ethical obligations***. For example, in North Carolina, an attorney who prepares the petition and related documents will often have a conflict of interest in defending a debtor in a § 727 action as the client may be materially limited by the personal interests of the lawyer. Rule 1.7 of the N.C. Rules of Professional Conduct.

- ***Worley v. Robinson*** (In re Worley), 15-2346 (4th Cir. February 28, 2017) – Fourth Circuit denied debtor’s (Worley) discharge under the false oath provision of 11 U.S.C. § 727(a)(4). Debtor – a sophisticated party with an M.B.A. from Emory University and

> over ten years of experience working as a financial advisor – valued his interest in real estate using a "capitalization of income method" that resulted in a significantly less value than other valuation methods. When challenged on this issue, the debtor claimed that he relied on the advice of counsel in using the lower value. The attorney that filed the Chapter 7 petition did not represent the debtor in the appeal to the U.S. District Court in the North Carolina Middle District or the appeal to the United States Court of Appeals for the Fourth Circuit.

A complete understanding of 11 U.S.C. § 523 and 11 U.S.C. § 727 will ensure you give your client's the fresh start the bankruptcy discharge provides.