IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NORTH CAROLINA
WESTERN DIVISION
Case No. 5:23-CV-00170-D

MARCUS C. PURDY AND AMANDA J. PURDY,	)
	)
Appellants,	)
v.	)
	)
MICHAEL BURNETT, TRUSTEE, AND BRIAN C. BEHR, BANKRUPTCY ADMINISTRATOR,	)
	)
Appellees.	)

ON APPEAL FROM THE UNITED STATES BANKRUPTCY COURT FOR THE EASTERN DISTRICT OF NORTH CAROLINA

BRIEF OF APPELLEES

This, the 21st day of July, 2023.

By:

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BRIEF OF THE CHAPTER 13 TRUSTEE AND U.S. BANKRUPTCY ADMINISTOR – APPELLEES

NOW COME Appellees, Michael B. Burnett, Chapter 13 Standing Trustee, and Brian C. Behr, U.S. Bankruptcy Administrator, and hereby file this brief in response to the Brief of Appellant, filed on behalf of Marcus and Amanda Purdy on May 31, 2023.

EXCLUSIONS PERMITTED BY FED. R. BANKR. P. 8014(b)

Pursuant to FED. R. BANKR. P. 8014(b), this Brief does not include a jurisdictional statement because the Appellees are satisfied with such statement as provided in the Brief of Appellant.

STATEMENT OF THE CASE

Marcus C. Purdy and Amanda J. Purdy (collectively "Debtors," individually "Male Debtor" and "Female Debtor") filed a petition seeking relief under chapter 13 of title 11 of the U.S. Code. In response to the Debtors' violation of Local Rules and bankruptcy court orders regarding the incurrence of post-petition debt, Michael B. Burnett, as Chapter 13 Trustee ("Trustee"), filed a motion on August 23, 2022, seeking dismissal of the case with prejudice. The bankruptcy court conducted a hearing on the motion and the Debtors' response thereto, at which it concluded, based upon the evidence before it, the Debtors acted in bad faith by forging a letter of support from the Trustee to satisfy the requirements of a mortgage lender during the process of incurring post-petition debt, thereby

circumventing previous court orders and a local rule of procedure regarding the incurrence of post-petition debt. An order was entered dismissing the Debtors' case with prejudice. The Debtors thereafter filed a notice of appeal to this Court.

STANDARD OF REVIEW

The standard of review for dismissal of a chapter 13 case is abuse of discretion. A "court abuses its discretion only where it has acted arbitrarily or irrationally, has failed to consider judicially recognized factors constraining its exercise of discretion, or when it has relied on erroneous factual or legal premises." *L.J. v. Wilbon*, 633 F.3d 297, 304 (4th Cir. 2011) (internal quotation marks, alternation, and ellipsis omitted). "Legal conclusions are reviewed *de novo*, but findings of fact will only be set aside if clearly erroneous." *Schlossberg v. Barney*, 380 F.3d 174, 178 (4th Cir. 2004).

STATEMENT OF THE ISSUE PRESENTED

Whether the bankruptcy court abused its discretion in dismissing the Debtors' bankruptcy case when they forged a letter and signature of the Chapter 13 Trustee to obtain mortgage loan financing, and in furtherance of their violation of court orders and a local rule of procedure.

STATEMENT OF FACTS

The Debtors filed a petition with the United States Bankruptcy Court for the Eastern District of North Carolina on October 7, 2019, seeking relief under chapter 13 of title 11 of the United States Code.[1] (D.E. 1).[2] John F. Logan was thereafter appointed to serve as trustee and fulfill the duties under § 1302. (D.E. 9). Michael B. Burnett was appointed successor trustee on January 3, 2023. (D.E. 102).

Brian C. Behr was appointed United States Bankruptcy Administrator ("Bankruptcy Administrator") for the Eastern District of North Carolina on May 4, 2022. "The Bankruptcy Administrator 'may raise and may appear and be heard on any issue in any case under title 11, United States Code, but may not file a plan pursuant to section 1121(c) of such title.' Judicial Improvements Act of 1990 § 317(b), Pub. L. No. 101-650, 104 Stat. 5089 (1990). The Bankruptcy Administrator acts to prevent fraud and abuse in bankruptcy proceedings. See 11 U.S.C. § 704(b); H.R. Rep. No. 95-595, at 88, reprinted in 1978 U.S.C.C.A.N. 5963, 6049." *Lynch v. Jackson*, 845 F.3d 147, 149 n.1 (4th Cir. 2017).

The bankruptcy court entered an Order and Notice to Debtor on September

[1] Hereinafter, title 11 of the United States Code will be referred to as "the Bankruptcy Code," or "the Code." All citations with only a § symbol refer to a section or subsection of the Bankruptcy Code, as indicated. References to chapter 13 mean 11 U.S.C. § 1301, *et. seq.*

[2] All references to "D.E." are to specific enumerated entries on the bankruptcy court docket which appears in its entirety as Document 8 with this Court on appeal.

20, 2019 ("Order/Notice"). (D.E. 9). Paragraph 4 of the Order/Notice read,

> Financial/Address Changes: You must notify your attorney and the trustee of any change of mailing address or employment. You must notify the court of any change in mailing address. You must also promptly notify your attorney and the trustee of any substantial changes in your financial circumstances, including substantial changes in your income, expenses, or property ownership. Examples of changes that would require you to give notice include, but are not limited to, if you (a) Get a raise or changes jobs and your income changes substantially; (b) Move and your housing or utility costs change substantially; (c) Win the lottery; (d) Become entitled to inherit property; (e) Become entitled to combined tax refunds of $2,000 or more for any tax year.
>
> These obligations continue throughout the complete term of your chapter 13 plan. Contact your attorney for advice on whether a change is substantial and must be reported.
>
> (emphasis in original).

Paragraph 11 of the Order/Notice read,

> Incurring Debt: You must not purchase additional property or incur additional debt in excess of $10,000.00 without prior approval of the court.

The Order/Notice was delivered to the Debtors via their respective email addresses by the Bankruptcy Noticing Center. (D.E. 11).

E.D.N.C. LBR 4002-1(g)(5) ("Local Rule") reads,

> POST-PETITION DEBT. After the filing of the petition and until the plan is completed, a debtor shall not incur additional debt of $10,000 or more without prior approval from the court. The debtor shall file an application to incur the debt with a fourteen-day notice to the chapter 13 trustee. If no objection is filed, the court may approve the application without a hearing.

The Debtors filed all required schedules and statements with the bankruptcy court, (D.E. 12), and filed an amended chapter 13 plan ("Plan") March 9, 2020.

(D.E. 39). Part 2.5 of the Plan identified the Debtors' applicable commitment period to be 60 months, and Part 2.1 of the Plan provided for monthly payments of $1,300.00 to be paid to the Trustee for a period of 60 months. *Id*. Part 7.2 of the Plan also contained a standard provision reading, "The use of property by the Debtor(s) remains subject to the requirements of 11 U.S.C. 363, all other provisions of the Bankruptcy Code, Bankruptcy Rules, and Local Rules. *Id*.

Allowed claims of general unsecured creditors totaled $124,675.40. Part 2.5 of the Plan indicated a dividend of no less than $3,877.20 was to be paid to unsecured creditors because of the disposable income test of § 1325(b)(1)(B), but no dividend was required by the best interests of creditors test under § 1325(a)(4). (D.E. 39).

Allowed secured claims consisted of three separate claims secured by three separate motor vehicles, and one claim secured by furniture. The Plan provided for allowed secured claims to be paid through Trustee disbursements. (D.E. 39). On April 10, 2020, the bankruptcy court entered an order confirming the Plan. (D.E. 43).

On December 8, 2021, the Debtors filed a motion to incur debt or, in the alternative, abrogate the bankruptcy court's local rule regarding incurring debt in which the Debtors sought court authority to incur debt for the purpose of purchasing a house. ("Motion to Incur"). (D.E. 66). A hearing on the Motion to Incur was

conducted January 5, 2022, at which the bankruptcy court orally denied the motion. A written order for the same was entered January 12, 2022. ("Denial Order"). (D.E. 71).

The Debtors filed a motion on January 13, 2022, seeking reconsideration of the bankruptcy court's ruling on the Motion to Incur. ("Motion to Reconsider"). (D.E. 72). A hearing on the Motion to Reconsider was conducted January 19, 2022, at which the bankruptcy court orally denied the motion because the Debtors failed to plead any relevant factors found in Rules 59 and 60 of the Federal Rules of Civil Procedure, as made applicable to the bankruptcy proceeding by Rules 9023 and 9024 of the Federal Rules of Bankruptcy Procedure. A written order for the same was entered February 23, 2022. (D.E. 79).

On April 28, 2022, the Trustee filed a motion requesting production of certain financial records from the Debtors pursuant to Rule 2004 of the Federal Rules of Bankruptcy Procedure. (D.E. 81). The bankruptcy court entered an order granting the motion, (D.E. 82), and the Debtors thereafter complied with that order. Upon review of the Debtors' financial records provided to the Trustee, he found cause to believe the Debtors incurred mortgage debt following the denial of their Motion to Incur and Motion to Reconsider.

On June 6, 2022, the Trustee filed a motion to compel the Debtors to appear before the Trustee for an examination pursuant to Rule 2004 of the Federal Rules

of Bankruptcy Procedure. (D.E. 84). The bankruptcy court entered an order granting the Trustee's motion, (D.E. 85), and the Debtors appeared and testified at that examination ("2004 Exam") on June 30, 2022. During the 2004 Exam, the Debtors admitted to incurring mortgage debt and purchasing real property located at 117 Amsterdam Drive, Clayton, North Carolina ("Property"), despite the bankruptcy court's orders denying the Debtors' previous requests to do so. The Trustee filed a motion on August 23, 2022, requesting dismissal of the case with prejudice. ("Motion to Dismiss"). (D.E. 91). A hearing on the Motion to Dismiss was conducted September 27, 2022, in Raleigh, N.C., at which the Debtors appeared. At that hearing the Female Debtor admitted she forged a letter from the Trustee just two days after the hearing on the Motion to Reconsider. *See*, eScribers, LLC transcript for hearing on Trustee's Motion to Dismiss Case with Prejudice ("Transcript"), page 40, lines 9-25; page 41, lines 1-20. According to the Female Debtor's testimony, the forged letter was submitted to the loan originator, Veterans United, following which financing for the purchase of the Property received final approval. Transcript, page 42, lines 15-23.

The bankruptcy court entered the Order Dismissing Case and Barring Future Petitions on March 21, 2023 ("Dismissal Order") (D.E. 119), and subsequently issued an opinion (D.E. 126) on the same on April 13, 2023. The Debtor filed a Notice of Appeal of the Dismissal Order on April 3, 2023. (D.E. 121).

SUMMARY OF THE ARGUMENT

This Court should affirm the Dismissal Order which dismissed this case with prejudice as to refiling. Section 1307 of the Bankruptcy Code allows a court to dismiss a case "for cause." Section 349(a) of the Bankruptcy Code permits the court, for cause, to dismiss a case with prejudice as to refiling for a set period of time. The Debtors forged a letter and signature of the Trustee to obtain a mortgage loan in pursuit of violating the procedures established in this District by local rule for incurring debt, and ignored the bankruptcy court's prior orders. The forged instrument and the Debtors' violation of the bankruptcy court's orders and Local Rule each provided independent cause for dismissal of the case with prejudice.

ARGUMENT

I. THE COURT ACTED JUSTLY AND WITHIN ITS AUTHORITY IN DISMISSING THE DEBTORS' BANKRUPTCY CASE WITH PREJUDICE.

The sole issue on appeal is whether the bankruptcy court abused its discretion in dismissing the Debtors' chapter 13 case after considering evidence the Debtors forged a letter and signature of the Trustee, and in the process circumventing and violating the bankruptcy court's prior orders and Local Rule. The validity of the Local Rule is not an issue on appeal, despite the Debtors' best efforts to make it so in their Brief.

The Trustee filed and properly noticed out the Motion to Dismiss through

which he requested dismissal of the case under § 1307(c). Section 1307(c) reads, in part,

> "…on request of a party in interest or the United States trustee and after notice and a hearing, the court may convert a case under this chapter to a case under chapter 7 of this title, or may dismiss a case under this chapter, whichever is in the best interests of creditors and the estate, for cause, …"

Section 1307 continues by enumerating ten specific circumstances in which a case may be dismissed but that list "is not exhaustive; the court is not limited by the specific circumstances specifically mentioned there." *In re Gonzalez-Ruiz*, 341 B.R. 371, 382 (B.A.P. 1st Cir. 2006). The court's authority to dismiss a case is expanded from those limited set of circumstances by the qualifier "for cause." It is well established that when a debtor's conduct in prosecuting their case falls sufficiently short of "good faith" that it becomes characterized as "bad faith," sufficient cause exists for a court to dismiss the case. *See, e.g., In re Sullivan*, 326 B.R. 204, 211 (B.A.P. 1st Cir. 2005); *In re Leavitt*, 171 F.3d 1219, 1224 (9th Cir. 1999); and *In re Love*, 957 F.2d 1350 (7th Cir. 1992). The Fourth Circuit has noted "[s]pecific provisions throughout the Code provide remedies for abuses in each of the types of bankruptcy proceedings," and "[i]n some Code provisions, enumerated circumstances of abuse are addressed. In others, general phrases such as 'for cause' provide broad coverage for unenumerated instances of misuse." *In re Kestell*, 99 F.3d 146, 148 (4th Cir. 1996). The "for cause" in Section 1307(c) includes

enumerated instances that authorize dismissal but also dismissal for cause includes "judicially construed ones such as bad faith." *Id.* (citing *In re Love*, 957 F.2d 1350 (7th Cir. 1992)). So, while 'bad faith' is not expressly listed as cause for dismissal in § 1307, "it is often the most cited basis for dismissal." Keith M. Lundin, Lundin on Chapter 13, § 152.4, at ¶ 5 LundinOnChapter13.com (last visited July 21, 2023). Regardless, "[e]very court of appeals that has considered the question has concluded that 'lack of good faith' or something like it is an included cause for dismissal of a Chapter 13 case." ***Id.***

Furthermore, a debtor is obligated to provide full disclosure of their financial affairs and assets, and failure to do so can also lead to a forfeiture of rights under the Bankruptcy Code. *See, e.g.*, *In re Criscuolo*, No. 09-14063-BFK, 2014 WL 1910078, at *3 (Bankr. E.D. Va. May 13, 2014) (citing, *Marrama v. Citizens Bank of Massachusetts*, 549 U.S. 365 (2007)). Whether to dismiss or convert a case upon cause shown lies within the discretion of the bankruptcy court. *In re Myers*, 491 F.3d 120, 127 (3d Cir. 2007).

A debtor's good faith, or lack thereof, is most often assessed by a court in the context of plan confirmation or modification as in the cases cited above, and the United States Court of Appeals for the Fourth Circuit[3] has previously held that

[3] The United States Court of Appeals for the Fourth Circuit will hereinafter be referred to as the "Fourth Circuit."

assessing the good faith of a debtor requires evaluating the "totality of circumstances" on a case-by-case basis. *Deans v. O'Donnell*, 692 F.2d 968, 972 (4th Cir. 1982), superseded by statute on other grounds. *See also*, *In re Lilley*, 91 F.3d 491, 496 (3d Cir. 1996). A bankruptcy court should not, however, be limited to reviewing a debtor's conduct only at the time of plan confirmation or modification. In this case, the facts giving rise to the bankruptcy court's review of the Debtors' egregious conduct were outside those singular moments in time but that does not mean such conduct was without redress. The Debtors forged a letter and signature of the Trustee post-confirmation of the Plan to satisfy a mortgage lender's request for approval of financing. The forgery also served to circumvent the established procedures set out in bankruptcy court orders – the Order/Notice and Denial Order – and the Local Rule regarding the incurrence of debt, orders which effectuated not only the provisions of the Code but also the provisions of the Plan itself. When attempting to employ those procedures failed to yield the result the Debtors wanted, they elected to ignore those procedures and court orders altogether and hijack the Trustee's authority and position. This conduct should not be immune from the bankruptcy court's review simply because it occurred at a time other than plan confirmation or modification. Because this conduct spoke to the prudence of allowing the Debtors to continue in their pursuit of a discharge of debt without payment in full, and while under the authority and protection of the bankruptcy

court, the court was within its authority to consider the Motion to Dismiss and rule as it did.

The bankruptcy court was also within its authority to dismiss the Debtors' case with prejudice as to refiling. "[S]o long as the dismissing court finds cause, a bankruptcy action may be dismissed with prejudice for 180 days, or more, without violating the terms of § 349(a) or, for that matter, § 109(g)." *Jolly v. Great Western Bank (In re Jolly)*, 143 B.R. 383, 387 (E.D. Va. 1992), *aff'd*, 45 F.3d 426 (4th Cir. 1994). Section 349 provides the bankruptcy court with authority "to impose a permanent bar to discharge that would have res judicata effect" and "seems to make clear that the court has the power to order such a sanction in circumstances other than those dealt with by new § 109[g]" and what "is equally clear is that it has become common bankruptcy practice to employ the phrase 'dismissed with prejudice' to refer to a temporary bar to filing another petition." *Colonial Auto Ctr. v. Tomlin (In re Tomlin)*, 105 F.3d 933, 938 (4th Cir. 1997).

In this case the bankruptcy court conducted a hearing at which the Female Debtor testified, and from which the bankruptcy court considered the totality of circumstances giving rise to the Motion to Dismiss brought by the Trustee. Denying the Motion to Dismiss would have been tantamount to condoning the Debtors' forgery and turning a blind eye to their blatant disregard for the bankruptcy court's orders and rules. The court was within its authority to uphold the integrity of the

bankruptcy process, its orders, and the Local Rule by dismissing this case with prejudice based upon the facts and evidence before it.

II. THE COURT FOUND CAUSE FOR DISMISSAL INDEPENDENT OF ANY LOCAL RULE ANALYSIS OR VIOLATION.

This Court need not review the validity or application of the Local Rule to find the bankruptcy court's dismissal of the case to be proper. The Debtors' act of forgery and disregard of the Order/Notice and Denial Order provided sufficient grounds to dismiss this case, independent of the implications of the Local Rule – grounds which the court described in its Dismissal Order as "actions of misconduct in the form of forgery and the blatant abuse of the provisions, purpose and spirit of the Bankruptcy Code." D.E. 126, page 9, ¶ 20. "Congress has made it clear within the Bankruptcy Code itself that misuse of the bankruptcy process should not be countenanced." *In re Kestell*, 99 F.3d 146, 148 (4th Cir. 1996).

A. Forging a Letter from the Standing Trustee is Cause for Dismissal

In seeking financing to purchase a house, the Debtors learned their mortgage lender required prior bankruptcy approval, and the lender presumably had little concern for the workings of the Local Rule. The Female Debtor testified at the Motion to Dismiss hearing that during the loan application process, she received an email from a Veterans United representative reading, "Items Required From Veteran: Chapter 13 BK Approval from BK trustee. You need a statement from

your bankruptcy trustee approving your purchase of the new home," and that she "was repeatedly told the only thing she needed was a trustee's letter and approval." Transcript, page 35, lines 14-17, and 23-25. So, while the Local Rule provided a procedure by which the Debtors could obtain court approval which would have presumably satisfied the lender's needs, they were unable to do so, of which the mortgage lender was aware. But, the Debtors' inability to obtain such an order did not authorize them to purloin the identity or authority of the Trustee.

The efficacy of the forged statement, "To Whom It May Concern: Our office fully supports Marcus and Amanda Purdy obtaining a mortgage," derived from its alleged source – the case trustee. Chapter 13 standing trustees exercise a broad range of responsibilities in the administration and effectuation of chapter 13 plans. *See, Matter of Maddox*, 15 F.3d 1347, 1355 (5th Cir. 1994). A chapter 13 trustee is, however, no mere administrator or disbursing agent. A trustee is statutorily responsible to fulfill the duties imposed by 11 U.S.C. § 1302, which incorporates many of a chapter 7 trustee's duties. A chapter 13 trustee, like bankruptcy trustees in general, bears a responsibility to the bankruptcy system and to maximize recoveries to creditors. The trustee is empowered to assert claims, avoid preferences, receive and account for payments from debtors, and examine and object to creditors' claim in furtherance of the congressional goal of distributing estate property to holders of allowed claims. *Id.* The trustee, in effect, represents the

interests of all creditors in a general nature by exercising various powers to ensure the collection of debtors' disposable income and disbursement of that income to creditors pursuant to a confirmed plan, in accord with the dictates of Congress as set forth in the Bankruptcy Code. *Id*. A chapter 13 trustee plays a role in ensuring a case moves forward to conclusion within a relatively short, clearly defined time, while participants (debtors and creditors alike) are to fulfill their duties in following the governing statutes and rules. Chapter 13 trustees, as the fiduciaries responsible for the administration of chapter 13 bankruptcy cases (at least to the extent creditor payments flow through their hands), are charged with preserving and promoting the bankruptcy system's integrity by, among other things, efficiently, expeditiously, and equitably administering cases in an organized and uniform manner.

The Debtors in this case commandeered the office of the Trustee for their own purposes. While they assert their forgery "had no impact on the bankruptcy case itself or the parties to the bankruptcy case" (Brief of Appellant, Doc. 17, Page 20), their conduct inherently violated the integrity of the Trustee and undermined the integrity of the bankruptcy system as a whole. To conclude otherwise is to condone forgery and give license to other debtors to manufacture whatever Trustee authorization they may require for whatever need they may have. If "no impact" has resulted from this conduct as the Debtors assert, then presumably no impact would result from the forging of signatures of creditors or other parties in this case,

or perhaps even forging an order of the bankruptcy court. But, it is difficult to reconcile a debtor producing counterfeit correspondence for the purpose of obtaining financial benefit with a system of financial reorganization predicated upon the "honest but unfortunate debtor." Such conduct is antithetical to the bankruptcy process. Tolerating the forgery of a letter and signature of another party, particularly a case trustee, in bankruptcy cases should not be condoned but instead met with robust repercussions.

The Debtors in this case obtained the debt they were seeking in the face of the debt they were attempting to discharge, notwithstanding the bankruptcy court's denial of the Motion to Incur brought under the Local Rule, and they did so through fraud. Such conduct carries no badge of good faith, and the bankruptcy court did not abuse its discretion in dismissing the case.

B. The Debtors' Willful Violation of the Bankruptcy Court's Orders, the Plan, and the Local Rule Justify Dismissal with Prejudice.

The Debtors were subject to the bankruptcy court's orders and Local Rule during the pendency of the Plan, but they intentionally chose not to abide by them. The Order/Notice expressly referenced the incurrence of debt in excess of $10,000.00, and the Plan included a provision reading, "[t]he use of property by the Debtor(s) remains subject to the requirements of 11 U.S.C. § 363, all other provisions of the Bankruptcy Code, Bankruptcy Rules, and Local Rules."

If the Debtors believed the denial of their Motion to Incur Debt was not justified, the proper course of action would have been to seek appellate review. The Debtors instead chose to disregard the Order/Notice and Denial Order, as those orders conflicted with their *own* desires and the alleged interests of non-parties to this case.[4] "To say more would be to paint the lily... [as] the debtor's repeated spurning of bankruptcy court orders without any legitimate reason amply supports the bankruptcy court's finding." *In re Francis*, 996 F.3d 10, 20 (1st Cir. 2021), cert. denied sub nom. *Francis v. Desmond*, 142 S. Ct. 1674 (2022). Courts have routinely held cause for dismissal arises when a debtor fails to comply with orders and rules of the court. *See, Howard v. Lexington Inv., Inc*., 284 F.3d 320 (1st Cir. 2002) (bankruptcy court did not abuse its discretion by dismissing petition when chapter 13 debtor failed to comply with court order to file state income tax returns.); *In re*

[4] The Female Debtor attempted to justify the forgery by arguing she and the Male Debtor were "about to cost innocent people $20,000," Transcript, page 37, lines 12-13, (which is allegedly the downpayment the sellers of the Property had paid toward the purchase of *their* next home), but there is no evidence the sellers could not have timely found a substitute buyer if the Debtors were to default on the purchase agreement. The Debtors further argue in their Brief they "could have faced legal consequences for their failure to comply with the contract from the sellers [of the Property] and the real estate agents." Appellant's Brief, page 27 of 52. It is worth noting the mortgage loan application process commenced prior to the hearing on the Motion to Incur, which may not be unreasonable. Transcript, page 27, line 1-6. But, regardless of whether the Debtors executed all final loan documents before or after adjudication of the Motion to Incur and Motion to Reconsider, obligating themselves to the terms of a contract before they received all approval documentation required by the lender does not justify their forgery of a letter and signature from the Trustee.

Maclean, 200 B.R. 417 (Bankr. M.D. Fla. 1996) (cause for dismissal with prejudice to refiling for 180 days where pro se debtor ignored bankruptcy court's "Duties Order," which required the filing of income tax returns.); *In re Tobias, 200 B.R. 412* (Bankr. M.D. Fla. 1996) (debtors' failure to file tax returns notwithstanding repeated court orders to do so is bad faith justifying dismissal for cause); *Badalyan v. Holub (In re Badalyan)*, 236 B.R. 633 (B.A.P. 6th Cir. 1999) (cause for dismissal of chapter 13 plan included the debtor's failure to comply with a court order to amend the plan and failure to file a memorandum in opposition to dismissal.); *In re Campbell*, 266 B.R. 709 (Bankr. W.D. Ark. 2001) (failure to comply with court order to file required documents in third chapter 13 petition within five months warrants dismissal with prejudice to refiling for 180 days.); and *In re Lin*, 499 B.R. 430, 436 (Bankr. S.D.N.Y. 2013) ("Courts have routinely held that dishonesty of a debtor is an indication of bad faith conduct and warrants dismissal"). *See also, In re Leavitt*, 171 F.3d 1219 (9th Cir.1999).

Of all the cases cited above, no facts are as egregious as those found in the case at bar. To obtain what they wanted, the Debtors took it upon themselves to intentionally ignore the orders and rules of the bankruptcy court, and such conduct does not harmonize with the nature of bankruptcy relief under the Code. The bankruptcy court did not abuse its discretion in dismissing the case under these facts.

III. THE LOCAL RULE IS A PROPER EXERCISE OF THE BANKRUPTCY COURT'S AUTHORITY, AND THE DEBTORS' VIOLATION OF THE LOCAL RULE AND DISREGARD OF THE BANKRUPTCY COURT'S ORDERS JUSTIFIES DISMISSAL WITH PREJUDICE.

The Debtors failed to appeal the bankruptcy court's orders denying the Motion to Incur and Motion to Reconsider, and they have employed arguments about the validity of the Local Rule to screen the egregiousness of their conduct following the outcome of those two motions. Their arguments are distracting and must ultimately fail as the validity of the Local Rule is not an issue on appeal. However, to the extent this Court must analyze the Local Rule to assess the bankruptcy court's discretion in dismissing the Debtors' case, the Local Rule is a proper exercise of the bankruptcy court's authority and has previously been analyzed by the United States District Court for the Eastern District of North Carolina in *Higgins v. Logan*, 635 B.R. 776 (E.D.N.C. 2021), as described *infra*.

The Local does not violate the Rules Enabling Act, is not substantive, and is not inconsistent or duplicative of the Bankruptcy Code and Federal Rules of Bankruptcy Procedure. Congress delegated rulemaking authority to the Supreme Court by way of the Rules Enabling Act of 1934, subsequently amended in 1988. The 1988 amendments incorporated 28 U.S.C. § 2075, a previously enacted statute (Pub. L. No. 88-623 (1964)), which reads, in part, "[t]he Supreme Court shall have the power to prescribe by general rules, the forms of process, writs, pleadings, and motions, and the practice and procedure in cases under title 11. Such rules shall

not abridge, enlarge, or modify any substantive right."

With this delegation, the Supreme Court promulgated FED. R. BANKR. P. 9029, and this Court entered its October 8, 1987, Order 87-PLR-3 delegating to the bankruptcy court the authority to make local rules of practice and procedure.

Congress did not define "substantive right" in the Rules Enabling Act, and the Act is otherwise silent as to any clear distinction between "substance" and "procedure," or when the inevitable overlap of the two through a rule becomes a violation. Congress' ability to delegate procedural rulemaking power to the courts has long been recognized, if that delegation does not include "powers which are strictly and exclusively legislative." *Wayman v. Southard*, 23 U.S. 1, 20 (1825). The prohibition in the Rules Enabling Act against affecting substantive rights recognizes a "substantive" right is one of such significance that it requires policy choices extrinsic to the business of the court and is subject to prospective regulation more appropriately suited to a democratically-elected legislature. But, without further legislation by Congress, determining the distinction between "substance" and "procedure" has been left to the courts.

The Supreme Court addressed the validity of a federal rule after passage of the Rules Enabling Act in *Sibbach v. Wilson & Co.*, 312 U.S. 1 (1941), in which the Court declared, "[i]s the phrase 'substantive rights' confined to the rights conferred by law to be protected and enforced in accordance with the adjective law

of judicial procedure? It certainly embraces such rights." *Id*., at 13. The Court held in Sibbach "[t]he test must be whether a rule really regulates procedure, – the judicial process for enforcing rights and duties recognized by substantive law and for justly administering remedy and redress for disregard or infraction of them." *Id*., at 14; *See* also *Associated Dry Goods Corp. v. E.E.O.C*., 720 F.2d 804, 809 (4th Cir. 1983) ("The courts look rather at the actual function and effect of the rule or regulation in question in resolving whether it is substantive or procedural").

In 2010, the Supreme Court again cited *Sibbach*, holding that the test, is not whether the rule affects a litigant's substantive rights; most procedural rules do. What matters is what the rule itself regulates: If it governs only "the manner and the means" by which the litigants' rights are "enforced," it is valid; if it alters "the rules of decision by which [the] court will adjudicate [those] rights," it is not. *Shady Grove Orthopedic Associates, P.A. v. Allstate Ins. Co*., 559 U.S. 393, 407 (2010).

The Local Rule's validity was previously reviewed by the United States District Court for the Eastern District of North Carolina in *Higgins v. Logan*, in which the Court noted, that "appellant fails to identify any provision of the Bankruptcy Code that provides a Chapter 13 debtor with an unfettered right to incur postpetition debt." *Higgins*, 635 B.R. 776, at 779. In fact, the Court appropriately noted that both §§ 1305(c) and 1328(d) "curtail a Debtor's ability to incur post-

petition debt." *Id.* While the "the Bankruptcy Code does not explicitly require a debtor to obtain court approval before incurring post-petition consumer debt" this Court and others have "concluded that the Bankruptcy Code may implicitly require court approval." *Id.* As one court further explained, under § 1303[5] a debtor may, other than in the ordinary course of business, and after notice a hearing, sell or lease property of the estate, and "if a chapter 13 debtor is going to buy a car postpetition and use the postpetition earnings to pay for it, isn't this a use of property of the estate outside the ordinary course of business that needs court approval?" *In re Ward* 546 B.R. 667, 677 (Bankr. N.D. Tex. 2016). "Other courts have found the court approval requirement to be intrinsic to the court's role as overseer of the plan confirmation." *Higgins*, 635 B.R. 776, at 780. For example, the bankruptcy court in *In re Brown* concluded, "As postpetition earnings are the backbone of funding for the confirmed plan, subsequent credit transactions are subject to scrutiny by the Trustee and the Court." 170 B.R. 362, 364-365 (Bankr S.D. Ohio 1994) ("If chapter 13 debtors are to be rehabilitated, they must be educated and encouraged to enter into transactions that are in both their long-term and short-tern best interests"). Stated differently, bankruptcy court oversite may prevent post-petition financial decisions from jeopardizing the successful completion of a debtor's plan of

[5] Section 1303 provides that "[s]ubject to any limitations on a trustee under this chapter, the debtor shall have exclusive of the trustee, the rights and powers of a trustee under section 363(b), 363(d), 363(e), 363(f) and 363(l)."

reorganization. And, to protect creditors' claims that are provided for in a confirmed plan, courts can maintain some supervision over a debtor's post-petition earnings.

The Local Rule in this case does not abridge or modify a substantive right; it governs a practice that is intrinsic to the business of the bankruptcy court and is consistent with the purposes of the Bankruptcy Code. The Supreme Court of the United States has noted,

> a central purpose of the Code is to provide a procedure by which certain insolvent debtors can reorder their affairs, make peace with their creditors, and enjoy 'a new opportunity in life with a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt.' But in the same breath that we invoke this 'fresh start' policy, we have been careful to explain that the Act limits the opportunity for a completely unencumbered new beginning to the 'honest but unfortunate debtor.'

Grogan v. Garner, 498 U.S. 279, 286 (1991), superseded by statute on other grounds. Debtors seeking relief under chapter 13 of the Bankruptcy Code do so voluntarily, requesting the bankruptcy court's protection from creditors while reorganizing their debts in pursuit of a discharge after maximizing payments to their creditors over time. Maximum payment to creditors is accomplished statutorily through various provisions of chapter 13, including: § 1325(b)(1)(B), which requires the contribution of projected disposable income during the applicable commitment period for payment to general unsecured creditors; § 1306(a)(1), which brings into the estate all property of the kind specified in § 541 acquired by a debtor

from the time the case is commenced until the case is closed, dismissed, or converted to another chapter; and § 1329, which allows modification of a confirmed plan to increase or reduce payments to creditors. The Local Rule is a recognition of these statutory provisions and allows the bankruptcy court to fulfill its responsibility to ensure the purposes and intent of the Code are accomplished in cases filed in this District. The Local Rule is consistent with the Supreme Court's explanation of the Bankruptcy Code's purpose in *Grogan v. Garner*, *supra*, and is consistent with similar rules or procedures in other districts across the country.[6] The Local Rule is a proper exercise of the bankruptcy court's authority.

CONCLUSION

The bankruptcy court did not abuse its discretion by dismissing this case with prejudice after considering the Debtors' conduct in forging a letter and signature of the case trustee to obtain mortgage financing, and for ignoring previous orders of the bankruptcy court and the procedure for incurring debt established through the Local Rule. This Court should affirm the bankruptcy court's order dismissing the Debtors' case with prejudice.

[6] There are no fewer than 22 federal judicial districts which employ a rule or plan provision regarding chapter 13 debtors' incurrence of post-petition debt which are similar to, and sometimes more restrictive than, the Local Rule discussed in this case. *See*, Appendix A, attached to this brief for a list of those districts with links to the applicable rule or plan.

Respectfully submitted this, the 21st day of July, 2023.

By:

Michael B. Burnett, Trustee
Michael B. Burnett,
Chapter 13 Trustee
N.C. State Bar No. 42719

By:

Brian C. Behr, Bankruptcy Administrator
Brian C. Behr, Bankruptcy Administrator
N.C. State Bar No. 36616

CERTIFICATE OF COMPLIANCE

I hereby do certify that this Brief of Appellees complies with FED. R. OF BANKR. P. 8015(a)(7)(B)(i), and that this Brief contains a total of 6,144 words on the enumerated pages through the Conclusion, and exclusive of those contained in Appendix A.

By: *Michael B. Burnett, Chapter 13 Trustee*
Michael B. Burnett, Chapter 13 Trustee
N.C. State Bar No. 42719

STATEMENT REGARDING ORAL ARGUMENT

The Appellees believe the facts and legal contentions are adequately presented in the materials before the Court, and therefore requests the Court dispense with oral argument.

CERTIFICATE OF SERVICE

I, Michael B. Burnett, do hereby certify I served the attached Brief of Appellees and Appendix A upon the parties listed below by mailing a copy thereof to said parties at the address indicated below with proper postage attached and deposited in an official depository under the exclusive care and custody of the United States Post Office in Raleigh, North Carolina, or by the ECF System as allowed by law.

Served via ECF:

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A hardcopy of this Brief and Appendix A will be mailed to:

Case Manager
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310 New Bern Avenue, Raleigh, N.C. 27601

I declare under penalty of perjury that the foregoing is true and correct.

Respectfully submitted this, the 21st day of July, 2023.

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