MCLE Self-Study Article:

Bankruptcy Hijackings: Improper Use of the Automatic Stay in Consumer Bankruptcy Proceedings

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By Joshua Scheer and Spencer Scheer

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I. INTRODUCTION

The automatic stay set forth in 11 U.S.C. § 362 arises upon the filing of a bankruptcy petition and is one of the most fundamental protections afforded to a debtor in bankruptcy. It gives a debtor a breathing spell and protection from almost all creditor actions, until terminated by order of the court or operation of law. There is a growing tension, however, between the legitimate use of the bankruptcy process to protect debtors that need to liquidate or reorganize, and the abuse and fraudulent use of the process by debtors and third parties seeking to obtain serial automatic stays. This tension is not a new phenomenon, and legislatures and courts have found ways to tailor or limit bankruptcy protection and the automatic stay to prevent abuse. However, the response by enterprising debtors and third parties has been just as creative, and both the courts and creditors are now confronted with adaptive schemes that often thwart the law.

The purpose of this article is to give a brief history of (i) the limitations on the automatic stay that have been imposed by legislatures to curtail abuse by debtors and third parties, (ii) strategies employed by debtors to thwart such limitations, (iii) creditor responses to such strategies, and (iv) the current state of the law. This article primarily focuses on the use and misuse of a bankruptcy stay to prohibit foreclosures of residential real property.

II. THE AUTOMATIC STAY

A. History of the Automatic Stay

It may be surprising to some, but there was a time when there was no such thing as the broad automatic stay now taken for granted in bankruptcy proceedings. Prior to enactment of the Bankruptcy Reform Act of 1978 ("Bankruptcy Reform Act"),[1] there was no automatic stay and a stay would only be granted under limited circumstances (and often dependent on court approval).[2] Accordingly, in the absence of an automatic stay, debtors who sought to restrain or limit creditor rights (i.e., foreclosure) were often required to petition for restraining orders in state court. This process resulted in increased expense due to legal fees and bond costs and a lack of uniformity and predictability because decisions varied from jurisdiction to jurisdiction.

The imposition of the current automatic stay in bankruptcy proceedings was a wholesale rearrangement of debtor and creditor rights. For as little as $175.00[3] an individual debtor could immediately obtain a stay of almost any creditor action,[4] anywhere in the country, by filing a petition in bankruptcy. No consent was needed and no order had to be obtained. The ease with which debtors could impose a stay forced creditors ranging from "mom and pop" establishments to labor unions to national and regional banks to go to the bankruptcy courts to resolve their rights, and reposed significant power in a court that was previously thought of as either ineffective or irrelevant.

B. Violations of the Stay

The power in the automatic stay comes not only from its effect on creditor actions, but in the ability of a court to punish those who violate it. Actions taken in violation of the automatic stay are void, not just voidable.[5] Under 11 U.S.C. § 362(k)(1), an individual injured by any willful violation of a stay can recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may even recover punitive damages. A willful violation of the automatic stay does not require specific intent to violate the stay, only that the party knows of the stay and thereafter takes intentional actions.[6] While attorneys' fees are generally not allowed for actions taken *after* the stay violation has been remedied, a recent Ninth Circuit Court of Appeals decision ruled in favor of a debtor requesting such fees for its defense of a lender's appeal relating to a stay violation award of damages.[7] In short, the automatic stay is far reaching and potential violations should not be taken lightly.

C. Bankruptcy Filing Trends and Legislative Attempts to Address Bankruptcy Filing Abuse

The number of bankruptcy filings skyrocketed immediately following the passage of the Bankruptcy Reform Act and continued to climb in subsequent years. While many factors have contributed to the rise in the number of filings, clearly the availability of an automatic stay that would cheaply and effectively stop foreclosures anywhere in the nation was a significant factor.

Since enactment of the Bankruptcy Reform Act, there have been two significant revisions relating to the automatic stay. In 1984, Congress passed the Bankruptcy Amendments and Federal Judgeship Act of 1984 ("BAFJA")[8] and in 2005, Congress enacted the Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA").[9] The BAFJA reform was relatively ineffective in limiting the number of filings. Following the passage of BAPCPA, while there was a significant decrease in the number of bankruptcy filings in its first year, filings soon began to rise again[10] once debtors and their attorneys were able

to navigate around the new restrictions imposed by BAPCPA relating to the automatic stay.

1. BAFJA Reform

Instead of seeking to directly limit the automatic stay, Congress initially attempted to address serial filing abuse by limiting debtor eligibility for bankruptcy. Accordingly, debtors who either disobeyed orders of the court, or who voluntarily dismissed a case after a creditor filed a motion to terminate the automatic stay, could be prohibited from continuing with a serial bankruptcy.[11]

This Congressional effort was not effective, however, as the provisions were not self-executing. A debtor could thwart the restrictions by continuing to refile, requiring a creditor to obtain further orders allowing relief from stay despite a debtor's ineligibility. Even if a court wanted to stop abusive filings by issuing orders prospectively terminating the automatic stay on particular properties (*in rem* orders), the courts were often reluctant to do so because of concerns that such orders exceeded the court's jurisdiction or were a denial of due process requiring the initiation of an adversary proceeding in bankruptcy.[12] Conversely, debtors who may not have acted in bad faith by dismissing a case due to financial circumstances might face a bar in refiling because a creditor had a motion for relief from stay pending when the case was dismissed.[13] Clearly, the BAFJA reform did not go far enough.

2. BAPCPA Reform

The BAPCPA amendments were extensive and far ranging, considered by many practitioners to be a reaction against lenient bankruptcy laws allowing debtors to avoid payment to creditors. The belief was that the BAPCPA reforms, including the implementation of a "means test" requiring debtors to demonstrate an inability to pay in order to obtain a bankruptcy discharge,[14] would permanently reduce the number of filings. After an initial decline, however, filings began to rise again, approaching historical norms.[15] Nonetheless, BAPCPA clearly made significant changes to address repeat filings by changing the automatic stay provisions. While the revisions to the imposition and duration of the stay under BAPCPA are far ranging, the amendments discussed below in this Section II(C)(2) were the primary changes concerning the limitation of repeat filings in residential mortgage cases.

a. Limiting Serial Filings by Denying Eligibility in Abusive Cases

Using a "*one, two, three strikes you're out*" approach, Congress limited the automatic stay depending on the number of filings and the proximity of the filings to a prior dismissal. 11 U.S.C. § 362(c)(3) limits the duration of the automatic stay to thirty days when there is a second filing by the debtor in a single or joint case within one year of the dismissal of a preceding case.[16] 11 U.S.C. § 362(c)(4) does not allow the imposition of a stay when there is a third filing by the debtor in a single or joint case and that filing is within one year of the dismissal of a preceding case.[17] These limitations can be removed by a debtor who obtains a court order, but the "shoe is now on the other foot" as the debtor has the burden of extending or gaining the stay.

Unfortunately, courts seeking to protect debtors have found ways to effectively maintain stay protection. Such courts have found that, although the stay terminated against the debtor in question, the stay continued for the benefit of an appointed bankruptcy trustee, and the creditor may also need to obtain relief against the trustee (or the estate), even in Chapter 13 proceedings. There are differing opinions and court decisions as to whether this interpretation correctly evidences the intention of Congress and the expected result when BAPCPA was passed.[18]

b. Limiting Serial Filings by Enacting Statutory Authority to Impose *In Rem* Orders

Further protections against abusive filings in the residential mortgage context were added through the enactment of 11 U.S.C. § 362(d)(4) and 11 U.S.C. § 362(b)(20). These statutory provisions allow a bankruptcy court to order *in rem* relief from a stay (effective upon recordation of the order)[19] applicable to a particular property for a period of two years, upon a showing that a property was subject to multiple filings or unauthorized transfers designed to delay, hinder or[20] defraud the creditor.[21]

This provision is well considered and can be effective if action is implemented in a timely manner. However, it can be thwarted by debtors or unscrupulous vendors in ways likely not envisioned by Congress when the legislation was passed. A primary example is a debtor who will deed fractionalized property interests to other debtors who are either in bankruptcy, or who will file for bankruptcy shortly after a creditor gets relief from a stay. Often, the recipients of the fractionalized interest in the property do not even know they were granted the interest. Further, in some instances, the grant of a fractionalized interest will be to debtors in other states or to multiple debtors in multiple states, resulting in a creditor having to petition courts in every state where there has been a transfer to a debtor to obtain the requested relief.

This author has handled matters where there were fractionalized transfers to over twenty different debtors with hundreds of related bankruptcies. As discussed in Section IV below, there are methods to combat this abuse. However, these adaptive debtor strategies often limit the ability of a creditor to obtain an *in rem* order recorded on a property prior to the imposition of the next serial filing and can result in a potential limitation in the effectiveness of these statutory provisions.

Accordingly, while BAPCPA has given creditors and the courts better tools to stop abuse of the automatic stay, creditors and the courts need to continue to respond effectively to counter persistent abuse, unless and until Congress acts again. Section III below outlines some of the more recent scams and tools utilized to bolster abusive filings, as well as court and creditor responses to such scams.

III. BANKRUPTCY SCAMS

A. Husband and Wife Re-Filing and the Co-Debtor Stay

A common way to avoid the BAPCPA restrictions on repeat filings is for a husband and wife to file separate bankruptcies. A married individual will file a bankruptcy petition to obtain the benefit of the stay. Once the bankruptcy is dismissed, the debtor's spouse will immediately file another bankruptcy. This second filing invokes a separate automatic stay and potentially

circumvents the restrictions of 11 U.S.C. § 362(c) that were designed to limit the stay in situations where there have been multiple re-filings by individual consumer debtors, as discussed in Section II(C)(2)(a) above.

A benefit of shifting bankruptcies back and forth between two spouses in a Chapter 13 case is that the non-filing spouse also obtains the benefit of a "co-debtor" stay imposed under 11 U.S.C. § 1301. The automatic stay of actions against co-debtors was actually a product of the Bankruptcy Reform Act. It was intended to protect a debtor who filed bankruptcy in a Chapter 13 action from the indirect pressures resulting from a creditor seeking to collect against a co-signor or guarantor who was also obligated on a loan with the filing debtor.[22] The "co-debtor stay" prevents any creditor from pursuing an individual who is liable on the debt with the debtor in a Chapter 13 action.[23]

While there may be legitimate reasons to provide a stay for a non-filing debtor, debtors have found it a useful tool in multiplying stay protection even after the enactment of BAPCPA. The scam typically proceeds as follows: after both spouses have exhausted their eligibility to obtain individual stays, they continue to re-file Chapter 13 bankruptcies individually so that the other party can maintain the benefit of the co-debtor stay, which, according to some bankruptcy judges, is not subject to the limitations on serial filings under 11 U.S.C. § 362(c). Since the imposition of BAPCPA, bankruptcy courts have rendered decisions upholding a co-debtor's right to a stay despite multiple filings by the underlying debtor that would otherwise be prohibited under the law. For example, a Maryland bankruptcy court found that because BAPCPA did not address the applicability of the co-debtor stay, it would not do so either, and that the co-debtor stay would still continue even if the filing debtor was not entitled to a stay.[24]

Clearly, this type of logic thwarts the intention of BAPCPA and emboldens debtors to abuse the protections afforded legitimate debtors seeking to repay their obligations. However, some courts have at least *implied* that although a co-debtor stay may arise upon a second filing, no stay (including a co-debtor stay) arises upon the debtor's third filing, thereby upholding at least part of the apparent legislative intention of BAPCPA.[25] The only effective way to limit this tactic is to obtain an *in rem* order and have it recorded in the county where the property is located.

B. Bankruptcy "Hijacking" Cases

Unfortunately for lenders and debtors alike, a burgeoning industry in California is foreclosure avoidance. In response to California's foreclosure problem, in late 2009, the California legislature instituted restrictions on broker and attorney assistance with loan modifications by passing Senate Bill 94, which modified sections of the Business and Professions Code, the Financial Code, and the Civil Code relating to debtor assistance with loan modifications.[26] This law prohibits accepting fees up front for assistance with loan modifications and even provides for criminal penalties (up to one year in jail) for a violation.

The law was enacted to limit a common scenario where an attorney or other party would represent that they could obtain a loan modification for a struggling debtor, take substantial money from the debtor up front, and then achieve no beneficial result. Removing licensed attorneys from the process, however, has given rise to abuse from other groups, as many unlicensed vendors now promise debtors additional time to occupy their mortgaged property by unlawfully using the bankruptcy stay provisions to stall creditor rights.

These schemes have been termed "bankruptcy hijackings" by some courts and are an increasing problem, especially in California and specifically in the United States Bankruptcy Court of the Central District of California (the "Central District Bankruptcy Court"). In one 2012 case in that court, an attorney was disciplined for her participation in a scheme related to eighty-two fraudulent transfers and bankruptcy filings;[27] the court estimated that the number of "hijacked" or fraudulent cases in 2012 totaled over 2,000. The Los Angeles County District Attorney's Office, the Los Angeles County Sheriff's Office, the Santa Barbara County District Attorney's Office, and the FBI have all opened investigations relating to bankruptcy and foreclosure fraud stemming from this type of conduct.[28]

1. *Transfer of Fractional Interest to Debtor in Bankruptcy*

As discussed in Section II(C)(2)(b) above, transfers of fractionalized interests in a property to one or more individuals in bankruptcy or who will subsequently file bankruptcy are proliferating. Although fact patterns vary, the most common example of a bankruptcy "hijacking" is the issuance of a grant deed to a debtor who is already in bankruptcy. The grant deed is provided to the foreclosing lender (or its foreclosure trustee) immediately prior to the foreclosure sale, along with a concurrent demand to stop a foreclosure sale. It is usually accompanied by a reference to the automatic stay of 11 U.S.C. § 362 and threat of punitive damages for a violation. The grant deeds are sometimes recorded immediately prior to the sale. Other times the grant deeds are not recorded at all, or are "backdated" to imply that the transferee had title to the property prior to the bankruptcy filing. The properties are typically not listed in the transferee's bankruptcy filing, yet the transferor purports to retain the benefit of the stay by asserting that the debtor in bankruptcy has an interest in the transferor's property and that any foreclosure sale will violate the automatic stay. These tactics are used for the sole purpose of avoiding or delaying the foreclosure.

Despite the likelihood that such documents may not be authentic and a history that may indicate a scheme to unlawfully delay foreclosure, lenders, foreclosure trustees, and title companies are hesitant to act and generally refuse to proceed with a foreclosure sale that could be in violation of the stay. The fear of repercussions under 11 U.S.C. § 362(k), and the possible effect a void sale may have on the ability to transfer clear title, act as sufficient deterrents to completing the sale no matter how spurious the debtor's claim may be. The hesitation in proceeding with a sale under these circumstances is not necessarily misplaced. Bankruptcy courts will generally follow the letter of the law when it comes to potential stay violations, often deeming actions void despite obvious bad faith actions by a debtor or third party.[29] For example, in *Johnson v. TRE Holdings, LLC (In re Johnson)*, the Bankruptcy Appellate Panel in the Ninth Circuit Court of Appeals held that a sale in violation of the stay is void even if the case is later dismissed as a bad faith filing due to a potential bad faith transfer of a fractional interest.[30]

The *Johnson* court also analyzed and challenged the ability of bankruptcy judges to issue orders "*in rem*" or "binding on the property" based solely on their authority under 11 U.S.C. § 105 ("Section 105") and not based upon a particular statute.[31] Section 105 provides that a court may issue any order "that is necessary or appropriate to carry out the provisions of this title" and allows a judge to, "sua sponte tak[e] any action . . . necessary or appropriate to enforce or implement court orders or rules, or *to prevent an abuse of process*."[32] Prior to BAPCPA, Section 105 was used as the basis for issuing binding orders in a "bad faith" scenario. While some courts disagree with the reasoning in *Johnson*,[33] this limitation creates a significant hurdle for creditors seeking to limit bad faith transfers and multiple filings that do not fall squarely within the confines of a particular statute.

Even though a "fractional transfer" falls squarely under the new restrictions under 11 U.S.C. § 362(d)(4), debtors (or third parties) have sought to avoid its restrictions on a technicality. Debtors argue that the limitations on refiling are specifically limited to situations where the *filing of the petition* was part of a scheme to delay, hinder or defraud creditors. Accordingly, such parties contend that, when there is a transfer to a new debtor who was not aware of the transfer, there could be no intention by that debtor to delay, hinder or defraud creditors, and therefore the court has no authority to enter an order under 11 U.S.C. § 362(d)(4). Clearly, the term "chutzpah" comes to mind.

Several bankruptcy courts have addressed this potential loophole in an effort to prevent further debtor abuse. Most courts have reasoned that 11 U.S.C. § 362(d)(4) is written in the *passive* voice, and thus does not require any involvement of the debtor. There is no requirement to find bad faith *by the debtor* mentioned anywhere in the statute.[34] Courts also continue to include in their reasoning a reference to Section 105, which provides that interpretation of the statute in this manner is "necessary to protect the integrity of the bankruptcy system."[35] Courts have gone so far as to say that BAPCPA evidenced Congressional intent to further limit any type of abusive filing by debtors and provided additional power to bankruptcy judges under Section 105 to issue similar types of orders.[36]

2. *Granting a Junior Lien to a Debtor in Bankruptcy*

Other variations on the "hijacking" scenario occur when there is a transfer of a junior deed of trust on a property subject to foreclosure to a debtor that is in bankruptcy. A debtor, unwilling to give up even a fractional interest in its property to obtain a stay, will instead issue a beneficial interest in a deed of trust on that property to a debtor who is in bankruptcy (or who will immediately file for bankruptcy to obtain the benefit of the stay). The beneficiary under the deed of trust becomes a "lienholder" on the property, with an interest in the property under California law. As a result, the debtor is able to obtain a stay of foreclosure. In some cases, the deed of trust is given to a fictional lienholder with numerous open bankruptcies across the country, thereby creating an additional hurdle and expense to foreclosure.

3. *Timing of Transfers and Recording of Order*

As discussed in Section II(C)(2)(b) above, if a creditor can obtain an *in rem* order recorded on the property under 11 U.S.C. § 362(d)(4), it can insulate the property from future bankruptcy filings. However, an unscrupulous way around this protection is for a debtor to transfer the property to another party already in bankruptcy *immediately prior to the recording of the order*. Since the *in rem* order has not been recorded prior to the transfer of the interest to the new debtor, the question arises as to whether the recording of the *in rem* order is in violation of the stay and whether the new transferee's bankruptcy prevents or voids the recording of the order. This confusion forces a lender to make a decision as to whether to file an additional motion to proceed with the original *in rem* order, or ignore the fraudulent transfer altogether and proceed with a sale and then go back to the bankruptcy court to request annulment and validation of the sale after the fact (as discussed in Section IV(D) below, there are risks in taking the latter approach).

4. *Transfer to Parties in Different States*

Given the response by local bankruptcy courts in California in developing specific rules and procedures to combat bankruptcy "hijackings," as discussed in Section IV(A) below, debtors have begun to focus their attention on filings across the country. While this is primarily looked at as a "California problem," other states have seen glimpses of these schemes. This author has seen transfers of California property to debtors in Pennsylvania, West Virginia, New York, and various other states across the country. The additional time spent in retaining attorneys familiar with these hijacking scenarios and convincing judges to issue *in rem* orders on a property in California results in additional delay.

IV. CREDITOR AND COURT RESPONSES

A. Local Rules

California appears to have been hit the hardest by "bankruptcy hijackings." As a result of a large number of such cases clogging the docket, bankruptcy judges in the Central District Bankruptcy Court have developed local rules and procedures to allow for an expedited hearing where this type of bad faith conduct is present for the issuance of "*in rem*" orders under 11 U.S.C. § 362(d)(4). For example, one particular judge in that court permits a reduced notice period for motions for relief from a stay of five business days (instead of the standard twenty-one calendar days), where there have been "[p]ost-petition transfers of real property to the debtor" or "[p]re-petition transfers to the debtor either within 30 days of the debtor's petition date, or involving a fractionalized interest in real property."[37] Other judges in that court have similar procedures with varying notice periods and timing requirements, ranging from two to fourteen days, in each case designed to assist creditors subject to a "bankruptcy hijacking" or other unlawful transfer scenario.

B. "Super" *In Rem* Orders and Other Creditor Options

In obvious bad faith scenarios similar to those described in Section III above, this author has been able to obtain orders on shortened notice (due to their emergency nature) using each court's general procedures or a judge's special procedures outlined in Section IV(A) above. Bankruptcy judges familiar with bankruptcy "hijackings" are generally quick to remove

these filings from their docket and prevent this bad faith conduct from continuing.

However, a problem arises when a foreclosure trustee or title company will not accept even a recorded order under 11 U.S.C. § 362(d)(4) because it has been entered or recorded while another "transferee's" bankruptcy or bankruptcies is open. Usually, these additional third party bankruptcies are not discovered until after the entry or recording of the order. Often, such bankruptcies are in multiple jurisdictions and can span several states and hundreds of separate courts. The lender is then faced with various unattractive options at this point.

First, it can seek to obtain orders in each open bankruptcy that may affect the property. This approach is obviously a very costly and unappealing proposition for a lender seeking to foreclose, usually on an already over-encumbered property.

Second, it can file an adversary proceeding in the bankruptcy court naming all parties in every bankruptcy and request a temporary restraining order of transfers of the property and an order for relief under 11 U.S.C. § 362(d)(4) binding on every open bankruptcy. Again, this approach is another costly and time consuming option for a lender who has already been significantly delayed. Some courts have held that this strategy is the only avenue to obtain this type of "all encompassing" relief or special relief.[38]

Third, it can file a motion for relief, provide notice to all parties to any open bankruptcy, and request that the relief be binding on any bankruptcy "pending or impending" which relates to the property. In rare instances, courts have entered expansive orders (sometimes termed "super" *in rem* orders by creditors) under 11 U.S.C. § 362(d)(4) and the court's authority under Section 105 to combat blatant bad faith delay tactics of debtors. While this author has been able to obtain such orders, many courts are becoming increasingly hesitant to issue them based on a legitimate fear of overstepping their authority.[39] Accordingly, while this approach may be the most attractive option for a lender, it is becoming more difficult to achieve.

Finally, aggressive creditors may simply proceed with a sale after receiving a clearly fraudulent grant deed or junior deed of trust and thereafter seek to obtain annulment of the automatic stay to validate the sale and all actions surrounding the sale. This option is by far the riskiest proposition, but in some circumstances may be warranted. Annulment requirements are addressed in Section IV(D) below.

C. Title Insurance

Practically speaking, the decision of a title company to insure a future sale may be a primary factor in how a lender or foreclosure trustee decides to proceed in the face of fraudulent bankruptcy filings.[40] The fear of having to defend a potential stay violation action is real. It greatly limits a title company from committing to insure a subsequent sale after foreclosure where there has been a transfer to a party in bankruptcy or where there is the potential for any bankruptcy involvement whatsoever. This reluctance to insure is typical even when there is a clear scheme to delay or a blatantly "forged" document.

Despite this hesitation, title companies sometimes agree to take on this potential risk since most parties involved in falsifying documents or filing "fake" bankruptcies are also hesitant to bring suit disclosing their fraud (potentially subjecting themselves to criminal liability for their actions). Accordingly, at the outset, a foreclosing lender should check with a title company to see if the title company will insure a subsequent sale to help determine the effectiveness of an order obtained by a court and to analyze the potential for litigation.

D. Annulment of the Stay

Annulment is another powerful tool that can be used in certain circumstances by foreclosing lenders who have fallen victim to a "bankruptcy hijacking" or a "fraudulent deed" scenario. Bankruptcy courts clearly have the authority to retroactively annul the automatic stay.[41] However, their willingness to do so varies depending on the circumstances of the case.

It has generally been held that annulment of the stay is the exception rather than the rule and should be granted only in unique and compelling circumstances.[42] In the Ninth Circuit, several factors are used in determining whether there is sufficient "cause" to annul the stay. It is an equitable analysis in which the bankruptcy court considers whether the creditor was aware of the bankruptcy petition and automatic stay, and whether the debtor engaged in unreasonable or inequitable conduct. In making this determination, the court will look at the history of the matter and the "good faith" of the parties.[43]

Some courts have been quick to grant annulment in scenarios where a debtor is misusing or abusing the bankruptcy system. Courts have entered orders *sua sponte* "to eliminate any vestiges of the abuse of process" relating to the debtor's petition, making an equitable analysis and basing their reasoning on their authority "to prevent an abuse of process" under the Bankruptcy Code.[44] Other courts have been hesitant to use this power even in situations of perceived and sometimes obvious abuse.[45]

The varying opinions and potential repercussions of a stay violation make the prospect of annulment less attractive. However, in certain situations, annulment may be the best option. Foreclosing lenders should review the relevant facts and circumstances with counsel and make sure their actions will be viewed as being in "good faith" even if there is blatant "bad faith" by the debtor. Knowing your audience is important and finding competent counsel to advise the foreclosing lender is even more crucial. The wrong move could not only void a sale, but could subject a lender to monetary damages.

V. CONCLUSION

The pendulum has swung both ways. Congress enacted a broad and sweeping automatic stay in 1978, providing substantial protections to legitimate debtors seeking bankruptcy protection. Since that protection was granted, abusive schemes have proliferated and parties have used the automatic stay provisions to thwart Congressional intent and the rights of creditors, especially in residential real property cases.

Congress has responded on two separate occasions to address such abuse, with limited success. As a result, uncertainty is prevalent, and large loopholes exist that unscrupulous debtors and vendors have been able to exploit through various types of "bankruptcy hijackings," inter-spousal transfers, co-debtor stays, and serial filings that skirt the restrictions under BAFJA and BAPCPA.

Strengthening the laws to provide that even a single finding of an abusive transfer or filing under 11 U.S.C. § 362(d)(4) is effective to limit future filings *even before an order is recorded* may be a way to allow more certainty in the law. Additionally, requiring the original debtor and/or borrower under the loan to appear in court to explain an unauthorized transfer of property or otherwise be subject to monetary or criminal penalties may be another potential deterrent. However, these scenarios are unlikely to be accepted by courts or debtors seeking the most expansive stay protection available; consequently, legislation that is remedial and incrementally deters abusive filings is a more plausible path forward.

In the meantime, it will take effective action by both courts and creditor counsel to respond to this problem, and it is likely that more courts will act as the Central District Bankruptcy Court has done in allowing expedited creditor relief in certain bad faith scenarios.

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Joshua Scheer is a principal of Scheer Law Group, LLP. ("SLG"). He graduated from the University of California, Santa Barbara with a degree in Political Science and earned his Juris Doctor from Suffolk University Law School in Boston, MA. He manages the bankruptcy department at SLG. His focus is on all aspects of lender representation in state and federal courts, including: Chapter 13 and 11 plan review and litigation, fraud litigation, and real estate transactions.

Spencer Scheer is the Managing Partner of the Scheer Law Group, LLP. He has been rated AV (top lawyer rating) by Martindale-Hubbell from 2005 to the present. He has over 20 years of experience in real estate, creditor bankruptcy, and general business litigation and transactional matters. Mr. Scheer has extensive experience in state and federal courts, having handled over 200 jury and non-jury trials on a wide variety of matters.

ENDNOTES

1 Pub. L. No. 95–598, 92 Stat. 2549 (1978).

2 Prior to the enactment of this legislation in 1978, bankruptcy was governed by the Bankruptcy Act of 1898 (Nelson Act, ch. 541, 30 Stat. 544 (1898)). While there were statutory grants of injunctive power in the Bankruptcy Act, they were not self-executing and a trustee, receiver, or debtor was required to make a request for such relief. The Nelson Act was significantly amended by the Bankruptcy Act of 1938 (Chandler Act, Pub. L. No. 75-696, 52 Stat. 840, 841, 842 (1938)). Noteworthy changes in the Chandler Act included the addition of business reorganization chapters, and the imposition of automatic stays in limited instances. For example, Section 148 of the Chandler Act allowed a stay only after an order approving the bankruptcy petition was entered, which could lead to delay or the failure of the Court to enter the order, often resulting in disputes regarding the effectiveness of the stay and the ability of a debtor to reorganize.

3 The cost at the time the Bankruptcy Reform Act went into effect.

4 There are limited exceptions to the automatic stay. 11 U.S.C. § 362(b) provides twenty-eight exceptions to the § 362(a) stay (e.g., exclusion of prosecution of specified criminal actions and certain administrative determinations from the automatic stay). Under 11 U.S.C. § 549(c), some courts have considered the protections afforded to bona fide purchasers who unknowingly take actions in violation of the stay to be a further exception. Other courts, however, have rejected this view, holding that this statutory provision can be distinguished because it concerns avoidance actions by the trustee and is designed to protect bona fide purchasers from actions by the debtor (as opposed to stay violations, which are actions taken against the debtor and are void because of a violation of the automatic stay). *See, e.g.*, *40235 Wash. St. Corp. v. Lusardi*, 329 F.3d 1076, 1080–81 (9th Cir. 2003). Practically speaking, bona fide purchasers at a foreclosure sale who buy from a creditor that violates the stay may also raise 11 U.S.C. § 549(c) to support the right to proceed.

5 *See Schwartz v. United States (In re Schwartz)*, 954 F.2d 569 (9th Cir. 1992).

6 *See In re Bloom*, 875 F.2d 224 (9th Cir. 1989).

7 *See Schwartz-Tallard v. America's Servicing Co. (In re Schwartz-Tallard)*, 751 F.3d 966 (9th Cir. 2014).

8 *See* Pub. L. No. 98-353, 98 Stat. 333 (1984). It should also be noted that in 1994, Congress passed the Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, 108 Stat. 4106 (1994), which created other significant changes to the Code, which are not addressed in this article.

9 *See* Pub. L. No. 109-8, 119 Stat. 23 (2005).

10 *See Newsroom: Statistics*, Am. Bankr. Inst., http://news.abi.org/statistics (last visited Aug. 31, 2014).

11 *See* 11 U.S.C. § 109(f) (since revised to 11 U.S.C. § 109(g)). Section 109(f) was re-designated as 109(g) by the Bankruptcy Judges, United States Trustees, and Family Farmer Bankruptcy Act of 1986, which added Chapter 12 to the Bankruptcy Code, and also added a new Section 109(f) to establish the eligibility for that chapter:

Notwithstanding any other provision of this section, no individual or family farmer may be a debtor under this title who has been a debtor in a case pending under this title at any time in the preceding 180 days if—

(1) the case was dismissed by the court for willful failure of the debtor to abide by orders of the court, or to appear before the court in proper prosecution of the case; or

(2) the debtor requested and obtained the voluntary dismissal of the case following the filing of a request for relief from the automatic stay provided by section 362 of this title.

Id.

12 *See, e.g., In re Feldman*, 309 B.R. 422, 428 (Bankr. E.D.N.Y. 2004) (decision issued before the BAPCPA amendments).

13 *See, e.g., In re Payton*, 481 B.R. 460, 467 (Bankr. N.D. Ill. 2012), (recognizing the issue and refusing to enforce the prohibitions upon a debtor).

14 *See* 11 U.S.C. § 707(b).

15 See, for example, *Annual Business and Non-business Filings by Year (1980–2012)*, Am. Bankr. Inst., http://www.abiworld.org/AM/AMTemplate.cfm?Section=Home&TEMPLATE=/CM/ContentDisplay.cfm&CONTENTID=66471 (last visited Aug. 31, 2014), showing that bankruptcy filings peaked in 2006 at 2,039,214, just before the effective date of BAPCPA, as debtors sought to gain rights under the prior law, declined significantly to 597,965 in 2006, the first year of BAPCPA, and then rose again, hitting 1,536,799 in 2010. Clearly, the Great Recession is a substantial factor in these statistics.

16 *See* 11 U.S.C. § 362(c)(3).

17 *See id.* § 362(c)(4).

18 *See, e.g., Reswick v. Reswick (In re Reswick)*, 446 B.R. 362 (B.A.P. 9th Cir. 2011). This case was an action brought by a former wife of the debtor for wage garnishment relating to a state court judgment. The debtor did not file a motion to extend the automatic stay after thirty days expired from the date of his second petition. The prior petition was dismissed within one year of the most recent filing. The court held that the legislative history of 11 U.S.C. § 362(c)(3)(A) showed an intent to have the stay terminated *in its entirety* after the expiration of thirty days in this situation if it was not extended by the court upon motion of the debtor. This holding was the *minority* view across the country at the time of the decision; other courts held that the stay terminates only *as to the debtor*, not *as to the estate*, based upon the plain wording of the statute. The *Reswick* court recognized that the statute would be impractical if it only applied to the debtor (and not the estate) because nobody would actually pursue the debtor without getting relief from stay as to the estate. The court reasoned that the language "as to the debtor" was intended to differentiate between a "debtor" and "co-debtor" spouse, not a debtor and the estate. For a different interpretation, see *Rinard v. Positive Invs., Inc. (In re Rinard)*, 451 B.R. 12 (Bankr. C.D. Cal. 2011). The Central District Bankruptcy Court disagreed with the reasoning in *Reswick* and adopted the majority view, claiming that the stay terminated only *as to the debtor* thirty days after the second filing. Also, the *Rinard* Court detailed in its opinion that Bankruptcy Appellate Panel cases have no authoritative or precedential effect, and that it was not bound by the *Reswick* decision. This conclusion is due to the BAPCPA changes, which now allow for a direct appeal of a bankruptcy court order to a U.S. Court of Appeals. The *Rinard* Court reasoned that Article I judges have no authority to make precedential decisions.

19 Congress specifically made its effectiveness contingent on the recording of the order to address any due process concerns for claims by third parties that they were unaware of the entry of the order. The statute also allows the order to be undone for "good cause shown," after notice and a hearing, thus allowing an innocent third party due process in the event an order is inequitably or mistakenly entered.

20 "When section 362(d)(4) was first enacted in 2005, the words in the pertinent phrase of the provision had been "delay, hinder *and* defraud." Use of the conjunction "and" rather than "or" led some courts to conclude that the language was deliberately chosen by Congress to impose a more substantial burden of proof on secured creditors before an *in rem* order could issue. These courts often denied *in rem* relief on the basis that the creditor had failed to show a scheme to defraud. The Bankruptcy Technical Corrections Act of 2010 amended section 362(d)(4) by replacing the "and" with an "or," making the subsection consistent with other Bankruptcy Code provisions that use the phrase "hinder, delay or defraud," such as sections 548(a)(1) and 727(a)(2)." 3 Collier on Bankruptcy ch. 362.05 (16th ed. 2011).

21 11 U.S.C. § 362(4) ("[T]he court shall grant relief from the stay . . . with respect to a stay of an act against real property under subsection (a), by a creditor whose claim is secured by an interest in such real property, if the court finds that the filing of the petition was part of a scheme to delay, hinder, or defraud creditors that involved either—(A) transfer of all or part ownership of, or other interest in, such real property without the consent of the secured creditor or court approval; or (B) multiple bankruptcy filings affecting such real property. If recorded in compliance with applicable State laws governing notices of interests or liens in real property, an order entered under paragraph (4) shall be binding in any other case under this title purporting to affect such real property filed not later than 2 years after the date of the entry of such order by the court, except that a debtor in a subsequent case under this title may move for relief from such order based upon changed circumstances or for good cause shown, after notice and a hearing. Any Federal, State, or local governmental unit that accepts notices of interests or liens in real property shall accept any certified copy of an order described in this subsection for indexing and recording.")

22 *See* 8 Collier on Bankruptcy ch. 1301.01 (16th ed. 2011).

23 *See* 11 U.S.C. § 1301.

24 *See King v. Wells Fargo Bank, N.A. (In re King)*, 362 B.R. 226, 232 (Bankr. D. Md. 2007). *See also In re Lemma*, 393 B.R. 299 (Bankr. E.D.N.Y. 2008), which applied the same concept to a second filing and held the termination of the § 362(a) automatic stay upon relief sought by a creditor under 11 U.S.C § 362(d) does not result in the termination of the 11 U.S.C.S. § 1301 co-debtor stay. Just as the termination of the stay in 11 U.S.C § 362(a) will not terminate the co-debtor stay imposed by 11 U.S.C.S. § 1301, so too does the

new thirty day automatic termination of the stay under 11 U.S.C.S. § 362(c)(3)(A) not terminate the co-debtor stay imposed by 11 U.S.C § 1301. The language of 11 U.S.C.S. § 1301 sets forth the instances when the co-debtor stay applies as well as exceptions to those instances; the termination of the automatic stay under 11 U.S.C.S. § 362(c)(3) is not a listed or implied exception.

25 *See In re Hernandez*, 2012 Bankr. LEXIS 1914 (Bankr. C.D. Cal. Jan. 31, 2012).

26 *See* Cal. Bus. & Prof. Code § 10085.6; Cal. Civ. Code § 2944.7; Cal. Fin. Code § 22161 (prohibiting a broker and anyone else, including attorneys, from demanding or collecting fees for loan modification services until the broker/licensee or attorney has performed each and every service and has provided required notices to the debtor).

27 *See In re The Disciplinary Proceeding of Lynne Romano*, No. 2:12-mp-00104-TA (Bankr. C.D. Cal. July 2, 2012).

28 *See Access to Justice: Self-Represented Parties and the Court—Fraud and Abuse*, U.S. Bankr. Court, Cent. Dist. of Cal., http://ecf-ciao.cacb.uscourts.gov/Communications/prose/annualreport/2012/sectioniiif.htm (last visited Aug. 31, 2014).

29 As discussed in Section IV(D), these voided actions do not prevent a request for annulment, which may be granted under certain circumstances, including bad faith.

30 *See Johnson v. TRE Holdings, LLC (In re Johnson)*, 346 B.R. 190, 194 (B.A.P. 9th Cir. 2006). In this case, a creditor's foreclosure was deemed void due to the transfer of a one-half interest in real property to a debtor in bankruptcy *just one hour before* the foreclosure sale occurred. The court issued this holding despite the fact that there was an order granting relief from the stay entered in a prior bankruptcy that limited any future filings relating to the subject property. The court noted that while the debtor was "on thin ice" for participating in an unacceptable strategy of transferring fractional interests for the purpose of filing multiple bankruptcies and that its actions "may constitute a crime," such actions did not change the nature of the creditor's conduct. *Id.* at 193. The creditor had foreclosed despite knowledge of the transfer and notification of the bankruptcy, and such knowledge and notice, in and of itself, was a clear violation of the automatic stay, thereby resulting in a void sale. The Court also referenced the alleged creditor's conduct in sabotaging a refinance for the purpose of foreclosing; however, the Court specified that its task was to focus on the law, not the "unsympathetic" parties. *Id.*

31 The order in *Johnson* was not issued under 11 U.S.C. § 362(d)(4) as it was not in effect at the time the initial order was requested.

32 *See* 11 U.S.C. § 105 (emphasis added).

33 *See, e.g., In re 4th St. E. Investors, Inc.*, 474 B.R. 709 (Bankr. C.D. Cal. 2012).

34 *See In re Dorsey*, 476 B.R. 261, 267 (Bankr. C.D. Cal. 2012) (discussing and concurring with the analysis in *In re Duncan & Forbes Dev., Inc.*, 368 B.R. 27 (Bankr. C.D. Cal. 2007)).

35 *Id.* at 268; *see also In re 4th St. E. Investors, Inc.*, 474 B.R. 709.

36 *See Wells Fargo Bank, N.A. v. Traub (In re Traub)*, 2014 Bankr. LEXIS 2028 (Bankr. S.D. Ga. May 5, 2014).

37 *Judge Houle's Self-Calendaring Instructions*, U.S. Bankr. Court, Cent. Dist. of Cal., http://www.cacb.uscourts.gov/judges/self-calendaring/houle-m (effective July 30, 2013).

38 *See, e.g., In re Van Ness*, 399 B.R. 897 (Bankr. E.D. Cal. 2009).

39 The 2011 U.S. Supreme Court decision in *Stern v. Marshall*, 564 U.S. 2 (2011), held that bankruptcy courts did not have constitutional authority to enter certain final judgments or orders relating to state law given their status as Article I, as opposed to Article III, courts. There have been many cases since *Stern* interpreting the decision and the extent to which it limits a bankruptcy judge's authority, a topic which is beyond the scope of this article.

40 Some title insurance policies and products, such as a trustee's sale guarantee, may provide little or no insurance for specific claims and may only protect the trustee. Though beyond the scope of this article, these issues should be considered by lenders and trustees alike.

41 *See In re Nat'l Envtl. Waste Corp.*, 129 F.3d 1052, 1054 (9th Cir. 1997).

42 *See Mataya v. Kissinger (In re Kissinger)*, 72 F.3d 107, 109 (9th Cir. 1995) (citing *In re Gonzalez*, 456 B.R. 429, 443 (Bankr. C.D. Cal. 2011) (Ninth Circuit determining that retroactive annulment should be granted only in extreme circumstances)).

43 *See Mendaros v. JPMorgan Chase Bank, N.A. (In re Mendaros)*, 2013 Bankr. LEXIS 4286 (B.A.P. 9th Cir. Oct. 2, 2013) (citing *Fjeldsted v. Lien (In re Fjeldsted)*, 293 B.R. 12 (B.A.P. 9th Cir. 2003)). *Fjeldsted* lists twelve factors provided by the Bankruptcy Appellate Panel of the Ninth Circuit, specifically (1) number of filings; (2) whether, in a repeat filing case, the circumstances indicate an intention to delay and hinder creditors; (3) a weighing of the extent of prejudice to creditors or third parties if the stay relief is not made retroactive, including whether harm exists to a bona fide purchaser; (4) the debtor's overall good faith (totality of circumstances test); (5) whether creditors knew of the stay but nonetheless took action, thus compounding the problem; (6) whether the debtor has complied, and is otherwise complying, with the Bankruptcy Code and rules; (7) the relative ease of restoring parties to the status quo ante; (8) the costs of annulment to debtors and creditors; (9) how quickly creditors moved for annulment, or how quickly debtors moved to set aside the sale or violative conduct; (10) whether, after learning of the bankruptcy, creditors proceeded to take steps in continued violation of the stay, or whether they moved expeditiously to gain relief; (11) whether annulment of the stay will cause irreparable injury to the debtor; and (12) whether stay relief will promote judicial economy or other efficiencies. 293 B.R. at 25.

44 *See In re Tara Hills, Inc.*, 234 F. App'x 432, 433 (9th Cir. 2007).

45 *See, e.g., In re Grason*, 2013 Bankr. LEXIS 2903 (Bankr. C.D. Ill. July 18, 2013) (deeming a creditor's action in proceeding with a sale to be in violation of the stay and denying the creditor's annulment request even though the debtor was not eligible for a bankruptcy filing under Section 109(g)).