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The authors survey the significant developments in bankruptcy, with particular emphasis on decisions — both state and federal — important to the Florida practitioner. Areas of emphasis include exemptions, the rights of secured parties and lessors, procedure and discharges. Throughout the article the authors make reference to pertinent decisions involving Florida's Uniform Commercial Code.

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The authors wish to express their appreciation to the following bankruptcy judges for their amiable cooperation in providing the authors with many of their important decisions rendered during 1977: The Honorable Thomas C. Britton and the Honorable Paul G. Hyman of the Southern District of Florida, the Honorable Alexander Paskay and the Honorable George L. Proctor of the Middle District of Florida.

I. INTRODUCTION

Recent developments in the law of bankruptcy,[1] an area of exclusive federal legislation, can in a sense be studied on a state-by-state basis. While all true "bankruptcy law" is federal in nature,[2] important rights in bankruptcy are regularly determined by reference to the laws of the state in which the bankruptcy court sits.

Indeed, if the reported Florida bankruptcy decisions are an accurate indicator, rarely are the bankruptcy courts required to look to the laws of a state other than the one in which they sit. Accordingly, this article's focus upon the decisions rendered by the bankruptcy and district courts sitting in Florida should have utility for the Florida lawyer. Decisions of the United States Court of Appeals for the Fifth Circuit are also selectively reviewed. In order to retain relevance for the Florida lawyer, only those Fifth Circuit decisions which construed Florida law or involved generally significant issues of federal bankruptcy law are highlighted.

II. JURISDICTION OF THE BANKRUPTCY COURT

A. *Summary Jurisdiction over Public Utilities*

A bankruptcy court's summary jurisdiction is generally limited to the adjudication of rights and claims pertaining to property in the actual or constructive possession of the bankruptcy court.[3] When a controversy involves property in the actual or constructive posses-

1. For earlier developments, see Gilbert & Pass, *Bankruptcy, 1976 Developments in Florida Law*, 31 U. MIAMI L. REV. 791 (1977).

2. *See* Bankruptcy Act, 11 U.S.C. §§ 1-1103 (1970). The Bankruptcy Act is referred to in this article as the "Act," and all citations herein are to the Act. A cross reference table correlating references to the Act with the United States Code appears at 11 U.S.C.A. xiv (1973).

3. *See* Herbert v. Crawford, 228 U.S. 204 (1913). For a thorough discussion of summary jurisdiction, see Suskin & Swing, *Ownership as a Basis for Summary Jurisdiction in Chapter XI Arrangements*, 31 U. MIAMI L. REV. 307 (1977).

sion of a third person asserting a bona fide adverse claim, the bankruptcy court may not assert summary jurisdiction without the claimant's consent. Absent such consent, suit must be brought in a court of appropriate jurisdiction, not the bankruptcy court.[4] Unlike the federal district courts, subject matter jurisdiction may be conferred upon the bankruptcy court by the third party's consent or waiver.[5]

A recent development concerning the bankruptcy court's summary jurisdiction was presented in *In re Security Investment Properties, Inc.*[6] In this case, the Court of Appeals for the Fifth Circuit held that a bankruptcy court lacks summary jurisdiction to compel a public utility to render future service to delinquent customers without an adequate security deposit. The court reviewed an order of the bankruptcy court that restrained an electric utility from imposing any security requirement upon a chapter XI debtor as a precondition to future electric service. The district court had affirmed the bankruptcy court, interpreting *South Central Bell Telephone Co. v. Simon (In re Fontainebleau Hotel Corp.)*[7] as empowering the bankruptcy court to predicate summary jurisdiction over such a public utility on the debtor's "property right" in the utility service.

Distinguishing its landmark *Fontainebleau* holding, the Fifth Circuit disagreed. The court drew an important distinction between the "property right" involved in *Fontainebleau* and the alleged property right involved in the case before it.[8] In *Fontainebleau*, the court found that the debtor, a famous resort hotel, had obtained a "unique property interest" in its telephone number, which had become widely known and had appeared in guidebooks, billboards and other publicity items. The phone company in *Fontainebleau* argued that the bankruptcy court lacked summary jurisdiction to enjoin it from requiring the payment of a deposit as a precondition to continued service under the existing telephone numbers.

Thus, the question in *Fontainebleau* was whether the hotel debtor had actual or constructive "possession" of its telephone

4. Harrison v. Chamberlin, 271 U.S. 191 (1926); Jan C. Uiterwyk Co. v. Brock, 500 F.2d 390 (5th Cir. 1974).

5. 2 COLLIER ON BANKRUPTCY ¶ 23.08 (14th ed. 1975) [hereinafter cited as COLLIER].

6. 559 F.2d 1321 (5th Cir. 1977).

7. 508 F.2d 1056 (5th Cir. 1975).

8. The right to receive electricity, the court held, does not constitute a "property right" that can be within the actual or constructive possession of the court; therefore, the court lacked summary jurisdiction to order continuation of the service without the payment of a deposit.

numbers.[9] In holding that the hotel had such possession, which allowed the bankruptcy court to gain summary jurisdiction, *Fontainebleau* rejected the holdings of the Ninth and Second Circuits to the effect that there is no such property right.[10]

There is no comparison, at least according to the Fifth Circuit, between the "property right" obtained by Fontainebleau Hotel by advertising its unique telephone number, and the simple right to receive electrical service. The court concluded that, although "a demand for a deposit securing present utility services may threaten to send a Chapter XI debtor into bankruptcy . . . this possible hindrance . . . cannot bootstrap the bankruptcy court's summary jurisdiction to cover property rights . . . not in the actual or constructive possession of the debtor."[11]

B. *Jurisdiction to Declare Rights in Exempt Property*

A bankruptcy court is deprived of jurisdiction over property once it has been determined to be exempt.[12]

In *In re Louis Vernell, Jr.*,[13] where the bankrupt was married at the time of the filing of the petition (therefore making the property technically exempt as homestead), the bankruptcy court refused to retain jurisdiction over the property because a state court had previously ruled the property nonexempt and subject to levy in satisfaction of a claim against the bankrupt arising prior to the property's existence as homestead. The fact that exempt property is subject to equities, liens or judgments is of no concern to the bankruptcy court,[14] and a bankruptcy court, without jurisdiction, is unable to rule on a particular person's right to avoid the general homestead exemption.

III. EXEMPTIONS

Closely related to the determination of jurisdiction over exempt

9. 508 F.2d at 1058. The court observed that the utility "virtually conceded" that it had no purpose in changing the numbers other than to induce payment of the debt.

10. *See In re* Vest Re-Mfg. Co., 453 F.2d 848 (9th Cir. 1971), *cert. denied sub nom.* Roughman v. Pacific Tel. & Tel. Co., 406 U.S. 919 (1972); Slenderella Sys., Inc. v. Pacific Tel. & Tel. Co., 286 F.2d 488 (2d Cir. 1961). However, as the *Fontainebleau* decision noted, the First Circuit had appreciated, at least, the value of telephone numbers by preventing the bankrupt from conveying them to increase the value of the bankrupt's estate. Darman v. Metropolitan Alarm Co., 528 F.2d 908 (1st Cir. 1976).

11. 559 F.2d at 1326.

12. *See* May v. Fidelity & Deposit Co., 313 F.2d 23 (10th Cir. 1962); *In re* Powers, 339 F. Supp. 1068 (W.D. Ark. 1972); Wetzel v. Idaho State Bank, 366 F. Supp. 1213 (D. Idaho 1973).

13. 11 C.B.C. 162 (S.D. Fla. 1977).

14. *Id.* at 164.

property is a determination of the exemptions themselves. Since exempt property constitutes no part of the bankrupt's estate, the bankruptcy court's jurisdiction is limited to the power to preserve intact all exempt property for the bankrupt.[15] Exempt property does not pass to the trustee[16] and is not considered in determining insolvency.[17]

The Florida bankruptcy courts were more actively involved in the determination of the availability of exemptions in 1977 than in prior years. There were a number of notable decisions.

A. *Homestead*

1. SURVIVING SPOUSE

Judson v. Deboliac,[18] in an apparent departure from prior Florida judicial construction of the homestead exemption, held that homestead property passes to the surviving spouse and retains its homestead character, even though the surviving spouse is not the "head of a family." The bankrupt, a surviving spouse with no children, had previously owned homestead property in a tenancy by the entirety with her husband. After his death, she sought to claim the homestead, which she occupied, as exempt.[19] Regardless of whether she was in fact the head of the family, the district court affirmed the bankruptcy court by holding that the surviving spouse was entitled to a continuation of the homestead property's exempt status.[20] The trustee contended that a surviving spouse, living alone, was not entitled to the exemption and proffered a number of decisions which seemed to recognize that the Florida Constitution did not authorize

15. Bankruptcy Act §§ 2a(11), 70a, 11 U.S.C. §§ 11, 110 (1970). *See also* 1A COLLIER ¶ 605[1]. Section 6 of the Act, 11 U.S.C. § 24 (1970), provides that the Act

> shall not affect the allowance to bankrupts of the exemptions which are prescribed by the laws of the United States or by the State laws in force at the time of the filing of the petition in the State wherein they have had their domicile for the six months immediately preceding the filing of the petition.

16. Bankruptcy Act § 70a, 11 U.S.C. § 110(a) (1970).

17. *Id.* § 70d, 11 U.S.C. § 110(d) (1970).

18. 14 C.B.C. 66 (S.D. Fla. 1977).

19. FLA. CONST. art. X, § 4; FLA. STAT. § 222.19 (1977).

20. FLA. CONST. art. X, § 4 provides, in part:

> (a) There shall be exempt from forced sale . . . and no judgment shall be a lien [on] . . . the following property owned by the head of a family:
>
> (1) a homestead . . . upon which the exemption shall be limited to the residence of the owner or his family;
>
> . . . .
>
> (b) These exemptions shall inure to the surviving spouse or heirs of the owner.

The legislature apparently intended to make the homestead exemption available to a surviving spouse living alone. *See* FLA. STAT. § 222.19 (1977).

the continuation of exempt status for homestead property in the surviving spouse unless she also constituted the head of the family.[21]

The bankruptcy court cited *Jasper v. Mease Manor, Inc.*[22] for the proposition that the legislature is free to interpret the Florida Constitution in order to allow the surviving widow to be the "head of the family." In *Jasper*, the issue was whether the statute, exempting all homes meeting the established standards, was within the constitutional mandate that property tax exemptions shall not be granted except for charitable purposes. The court found that it was within the legislature's prerogative to include an old-age home in the constitution's protection regardless of the sources of the inmates' financial support.[23]

In sum, *Deboliac* appears eminently correct, despite decisions interpreting the constitutional homestead provisions to the contrary.[24]

2. "BUSINESS HOUSE"

In *In re The Back Porch*,[25] the bankruptcy court upheld the bankrupt's homestead exemption claim for a three-story dwelling, a large portion of which was constructed as rental apartments. The constitution provides that the homestead is "limited to the residence of the owner or his family."[26] The old constitution, however, provided that the homestead protection was not to "extend to more improvements or buildings than the residence *and business house* of the owner."[27]

Thus, the 1968 excision of the term "business house" from the original homestead exemption language, leaving the current exemptions "limited to the residence of the owner or his family," reasonably implies that the homestead exemption is now more narrow than before. Although the former constitution did not define "residence

21. In Bendl v. Bendl, 246 So. 2d 574, 577 (Fla. 3d Dist. 1971), it was held that upon the husband's death the homestead exemption ceases absent a showing that the widow is the head of the family. *Compare* Regero v. Daugherty, 69 So. 2d 178, 180 (Fla. 1954) *with* Menendez v. Rodriguez, 143 So. 223, 226 (Fla. 1932) (concurring opinion).

22. 208 So. 2d 821 (Fla. 1968).

23. "The test for measuring such legislation against the constitutional restraints must be that of reasonable relationship between the specifically described exemption and one of the purposes which the Constitution requires to be served." *Id.* at 825.

24. *See* note 21 *supra*. Prior to the 1968 constitutional revision, it was provided that the homestead exemption "shall inure to the widow . . . entitled to such exemption." FLA. CONST. art. X, § 2 (1964). The omission of the "entitled to" language strongly implies that the legislature's newest construction was written as intended in FLA. STAT. § 222.19 (1977).

25. No. 77-26 (M.D. Fla. May 18, 1977).

26. FLA. CONST. art. X, § 4.

27. FLA. CONST. art. X, § 1 (1964) (emphasis added).

and business house," it was broadly viewed as "the owner's actual residence . . . [and] improvements . . . being used as a means of making the owner's livelihood."[28] In any event, it has long been settled that the homestead exemption was to be "interpreted in the liberal and beneficent spirit in which [it was] . . . conceived and enacted in the interest of the family home."[29] Rental garages, apartments and paint shops attached to the actual residence of the owner were within the former constitution's exemptions.[30]

In *The Back Porch*,[31] although the claimed homestead was an apartment house, at the time the petition in bankruptcy was filed, the building was occupied exclusively by the bankrupt and the immediate members of his family, who paid no rent. The trustee argued that the absence of the "business house" reference in the new constitution meant that income-producing property, even if part of the residence, is not exempt. The bankruptcy court, however, upheld the exemption claim of the debtor, curiously holding that the constitution does not qualify the homestead exemption by its use, but by its size.

The court responded to the trustee's argument, as well as the Supreme Court of Florida's decision in *Weiss v. Stone*[32] (decided under the old constitution), by finding that where only part of the property is a dwelling house and part is used for business, "the extent of the exemption would depend on all surrounding facts, and circumstances, and if the examination of the property reveals that it is more than the 'residence and business house' of the owner, the nonoccupied portion should be removed from the homestead exemption."[33] The bankruptcy court conceded that it would be contrary to the constitution's intent to permit an exemption claim for commercial property which was completely detached from the actual dwelling.

28. Cowdery v. Herring, 143 So. 433, 435 (Fla. 1932), *quoted in* White v. Posick, 150 So. 2d 263, 265 (Fla. 2d Dist. 1963).

29. Marsh v. Hartly, 109 So. 2d 34, 38 (Fla. 2d Dist. 1959), *quoted in* White v. Posick, 150 So. 2d at 265-66.

30. *See* Heil Co. v. Lavieri, 205 So. 2d 21 (Fla. 2d Dist. 1967).

31. No. 77-26 (M.D. Fla. May 18, 1977).

32. 220 So. 2d 403 (Fla. 1969). In that case, the property for which the homestead exemption was claimed consisted of three contiguous lots of land and a one-story, five-unit apartment building, of which the defendant occupied one apartment. The trial court held that all the property except that actually occupied by the bankrupt was subject to the homestead exemption. The appellate court affirmed. *Weiss v. Stone*, however, was decided under the old constitution, which contained the "business house" language. No recorded decision has yet determined what effect, if any, the excision of the "business house" language has had upon the scope of the homestead exemption.

33. No. 77-26 (M.D. Fla. May 18, 1977).

The court found that, at all relevant times, none of the remaining units were rented and none were income-producing. In addition, because there was no way to separate the building, it was impossible to allocate exempt and nonexempt status among the units, even if some had been income-producing.[34]

While probably correct on its facts, the conclusion in *The Back Porch*, that the homestead exemption is dependent not on the *use* of the property but only upon its *size*, seems inconsistent with the implication of the constitutional change removing the "business house" language. The full implication of that change remains to be decided. So far, however, it appears that the bankruptcy court will be reluctant to read that change very broadly in derogation of the debtor's exemption.

B. *Tort Claims*

Tort claims for slander, libel or personal injuries, which can transform a bankrupt into a wealthy person overnight when reduced to judgment, continue to enjoy an effective "exempt" status, as illustrated by *In re Gavin*.[35] After bankruptcy, the bankrupt settled a tort claim that was pending at the time of filing the petition. The court first ordered the settlement check turned over to the trustee, but eventually exempted the proceeds of the suit on the ground that the Act prohibits the trustee from taking title to "rights of action ex delicto for libel, slander, [or] injuries to the person of the bankrupt . . . unless by the law of the State such actions are subject to attachment . . . ."[36] Under Florida law, tort claims are not subject to attachment or execution until they are liquidated into a sum certain.[37]

Of course, although the tort claim became certain and liqui-

34. *Id.*

35. No. 76-1431 (S.D. Fla. July 25, 1977).

36. Bankruptcy Act § 70a(5), 11 U.S.C. § 110(a)(5) (1970).

37. Although the court correctly held that a chose in action for a tort claim is generally not subject to attachment or garnishment in Florida, the court's rationale is nonetheless somewhat confused. Choses in action of *any* kind are immune from attachment under FLA. STAT. § 76.01 (1977), which only authorizes the attachment of "goods and chattels, lands and tenements." Choses in action for many torts are also not subject to garnishment because the writ reaches only a chose in action for a "debt due" the person holding the chose in action, and then only when the debt due is unconditional and liquidated in nature. *See* Cobb v. Walker, 198 So. 324 (1940); FLA. STAT. § 77.01 (1977). Although *Gavin* appeared to rely in part upon the generally unliquidated and contingent nature of a tort claim, it also relied on *Id.* § 77.02, which provides that a writ of garnishment will not issue upon a chose in action sounding in tort. This statute has nothing to do with the central issue in *Gavin*.

dated when reduced to judgment or settlement, it then escaped inclusion in the bankrupt estate as after-acquired property.[38]

C. *Property Taxes*

Article VII, section 3(a) of the 1968 Constitution of Florida exempts from taxation property "used predominately for educational, literary, scientific, religious or charitable purposes." The legislature has recently decided to grant a tax exemption to private hospitals under this section on the ground that they are "charitable" in nature.[39] The legislature defined the term "used predominately for . . . charitable purposes," as used in article VII, section 3(a), as meaning "property used for exempt purposes in excess of fifty percent but less than exclusive."[40]

The exempting statute also provides that, in determining the amount of exemption for hospitals, "portions of the property leased as parking lots or parking garages operated by private enterprise shall not be deemed to be serving an exempt purpose and shall not be exempt from taxation."[41]

In *Blake v. Cedars of Lebanon Hospital Tower, Inc. (In re Cedars of Lebanon Hospital Tower, Inc.)*,[42] the bankruptcy court considered the applicability of that exemption to a tax exempt hospital with a substantial parking facility operated by private enterprise. The actual use of the parking area, which contained 624 spaces and which was also available for use by persons visiting doctors' offices, a pharmacy and a convenience grocery housed therein, was found to be "negligible" for hospital purposes. The entire lot was *available* exclusively for hospital use, however.

The court considered all the parking spaces in the complex, regardless of who owned the underlying land. The bankruptcy court appeared to stress that the availability of parking spaces is less important than their actual use since it found that only one-half of the parking facilities were used for any purpose and that even fewer spaces were used exclusively for hospital purposes.

Cedars of Lebanon indicates that by simply building too many parking spaces, either to comply with local ordinances or to prepare

38. Generally, property obtained by the bankrupt after the filing of the petition in bankruptcy does not pass to the trustee, whose estate is determined at the time of "cleavage"—the time of the filing of the petition under section 70b. 11 U.S.C. § 110(b) (1970). *See generally* Stein v. Leibowitt (*In re* Leibowitt), 93 F.2d 333 (3d Cir. 1937).

39. FLA. STAT. § 196.197 (1977).

40. *Id.* § 196.012(3).

41. *Id.* § 196.197(2).

42. No. 74-180 (S.D. Fla. May 16, 1977).

for future needs, a hospital may forfeit its *entire* tax exemption. The court did not clearly state whether a parking garage which is used to less than half of its capacity, even though used for charitable purposes, will forfeit its tax exempt status. Such a broad reading may impose a substantial and unwarranted burden upon charitable hospitals.

D. *Disability Payments*

In *In re Witlin*,[43] a case of first impression, the court ruled that premature disability disbursements under a Keogh plan[44] are not exempt from passing to the trustee.[45] The court construed the plan as an annuity with an incidental right to premature withdrawal and held that the fact that every Keogh plan contains a spendthrift provision, precluding assignment or alienation,[46] does not render them exempt.[47]

In *In re Prestein*,[48] the issue was whether the bankrupt could exempt disability insurance payments and civil service commissions he had received and deposited in his bank account. The bankrupt argued that the disability payments were exempt under Florida law, which provides that disability payments are not liable to attachment, garnishment or legal process.[49] He argued that comparable federal law exempted the civil service commissions.[50]

The court was not persuaded. First, it appeared that the bankrupt, after segregating the funds, had taken a $25,000 European tour which rendered him bankrupt. The court refused to allow the debtor to execute a "premeditated and deliberate plan to resort to bankruptcy and to stand behind the exemption laws to defeat the claims of [his] creditors."[51]

The bankruptcy court's second ground for denying the exemptions is more troublesome. The court simply held that while disability insurance payments are exempt before they are paid to the bankrupt, they are not exempt once received. The court concluded that the purpose of disability income benefits was, in large part, to preserve for the bankrupt the right to receive future disability benefits,

43. No. 76-1124 (S.D. Fla. Feb. 8, 1977).

44. A Keogh plan, essentially a retirement plan for self-employed persons, defers income to a later date (though the money may be withdrawn prematurely as disability payments).

45. *See* 29 U.S.C. § 1056(d)(1) (1970); FLA. STAT. § 222.18 (1977).

46. 29 U.S.C. § 1056(d)(1).

47. *See also* RESTATEMENT (SECOND) OF TRUSTS § 156(1) (1957).

48. 11 C.B.C. 516 (S.D. Fla. 1977).

49. FLA. STAT. § 222.18 (1977).

50. *See* 5 U.S.C. § 8346 (Supp. V 1975).

51. 11 C.B.C. at 523.

replacing the wages he would have earned. Of course, if no disability benefits were owing, future earnings would not pass to the trustee, since they would be after-acquired property. The court viewed the exemption[52] as a legislative attempt to "achieve equality in treatment between future earnings and . . . disability benefits."[53] The bankrupt who accumulates wages in a savings account, according to the court, should be treated no differently than the bankrupt who accumulates disability payments in the same manner.

While this much makes sense, the court's analysis was unsatisfactory insofar as it limited discussion to persons who receive their disability benefits in lump-sum payments. In making this distinction, the court noted:

> When lump-sum disability settlement are [*sic*] paid to a beneficiary, that beneficiary thereafter has sole control over the total amount of the settlement. He can invest in property, exempt or otherwise, or he can pay his creditors and avoid bankruptcy altogether. The beneficiary of the periodic payments does not have control over future payments, much as a wage earner does not have the control over, nor may he spend, future unpaid wages. Lump-sum beneficiaries enjoy the immediate benefit of disposition of their lump-sum. In return for this benefit, they must risk losing their lump-sum if they choose to segregate it from their creditors and thereby precipitate bankruptcy.[54]

But the fact that a lump-sum beneficiary has immediate control over the full amount he will receive under the disability contract, while the periodic beneficiary does not, has no substantial relation to the Bankruptcy Act's recognition of this exemption.

When that bankrupt elects, for whatever reason, to take the benefits in a lump-sum, it makes little sense to penalize that election by holding the entire amount subject to transference to the trustee. Periodic beneficiaries receive the "fresh start" that the Act intends. Lump-sum beneficiaries who do not foresee bankruptcy, however, may not receive this "fresh start," thereby allowing their creditors to receive a windfall.

A more equitable accommodation of these competing interests would be attainable by determining, in each case, whether the debtor truly deserves the benefits of an exemption. Another possibility would be for the lump-sum beneficiary's payment to be prorated, making it correspond to the existing or accrued periodic pay-

52. FLA. STAT. § 222.18 (1977).
53. 11 C.B.C. at 519.
54. *Id.* at 520.

ment that the beneficiary would have received had he not elected lump-sum payment.

The principle invoked by the *Prestein* court to deny exemptions to dishonest debtors can always suffice to take care of the debtor who abuses lump-sum privileges, but its doctrinal extension of the rule to all cases seems unwarranted.

E. *"Luxury Items"*

In *In re Wilson*,[55] the bankruptcy court rejected a trustee's claim that a diamond ring worth $662 was not exempt because it was a "luxury item." The court disagreed, reluctantly, and held that the Constitution of Florida,[56] which allows heads of households a $1,000 personal property exemption, does not distinguish between luxury and nonluxury items. The court refused to follow the holding in *Rivas v. Noble*,[57] which suggested a contrary result.

F. *Personal Property*

In *In re Bowles*,[58] a bankrupt was held to be entitled to claim certain office furnishings and equipment as exempt personal property.[59] The bankrupt, a practicing attorney who worked in his home, used the furniture, on which he owed nothing, for both business and personal functions. The court rejected the trustee's argument that occasional business use should preclude the exemption.

G. *Effect of Fraud*

In *In re Jeter*,[60] a bankrupt's knowing and fraudulent concealment of an interest in real property[61] did not operate to deny the debtor's right to an exemption on other properties. As a result of the fraud, the bankrupt lost his right to a discharge.[62]

Of greater interest was that one of the bankrupt's creditors also moved to deny the bankrupt's state created exemption on other property, on "general principles of equity." The bankruptcy court

55. 3 BANKR. CT. DEC. (CRR) 816 (Aug. 23, 1977).

56. FLA. CONST. art. X, § 4(a)(2).

57. 241 F. 673 (5th Cir. 1917). In *Rivas*, a $650 diamond ring was held not exempt, and was ordered to be turned over to the trustee. The court stated it was unable to find any authority for an exemption of this item. *Id.* at 674.

58. 3 BANKR. CT. DEC. (CRR) 822 (Aug. 17, 1977).

59. FLA. CONST. art. X, § 4(a)(2) exempts "personal property to the value of one thousand dollars." *See also* FLA. STAT. § 222.06 (1977) for the method of exempting personal property.

60. 3 BANKR. CT. DEC. (CRR) 821 (Sept. 14, 1977).

61. *See* 18 U.S.C. § 152 (1970).

62. Bankruptcy Act § 14c(1), 11 U.S.C. § 32(c)(1) (1970).

noted that section 6 of the Act[63] specifically recognizes the availability of exemptions existing under state law. The court, however, found that there was no Florida authority under which a bankrupt's right to an exemption on certain property was denied on "general equitable principles" because of fraudulent conduct by the bankrupt not relating to that property.[64]

The court concluded that fraudulent concealment of some property from the bankruptcy court has no bearing upon the bankrupt's right to exemptions otherwise available under state law on other property.

IV. PREFERENCES

In *Howdeshell Plumbing, Inc. v. American States Insurance Co. (In re Howdeshell Plumbing, Inc.)*,[65] the bankrupt, a plumbing contractor, informed the defendants, its bonding companies, that it would be unable to perform its bonded contracts. Soon thereafter, defendants made a thorough one month investigation of the bankrupt's operations.

Five weeks after the notification, defendants filed indemnity agreements executed by the bankrupt in favor of the bonding companies. Later that day, defendants, as sureties, appropriated certain of the bankrupt's equipment. Two weeks after the filing of the indemnity agreement, a petition for an arrangement under chapter XI[66] was filed.

The trustee argued that the indemnity agreements were voidable preferences[67] under sections 57g[68] and 60[69] of the Act. The court found that reasonable cause existed for defendants to know of the bankrupt's insolvency because of defendants' extensive investiga-

63. 11 U.S.C. § 24 (1970).

64. Florida courts have denied a bankrupt's right to a homestead exemption where there was fraud directly relating to the homestead property. Jones v. Carpenter, 90 Fla. 407, 106 So. 127 (1925); Ryskind v. Robinson, 302 So. 2d 427 (Fla. 1st Dist. 1974).

65. 3 BANKR. CT. DEC. (CRR) 711 (July 27, 1977).

66. 11 U.S.C. §§ 701-99 (1970).

67. *See* 3 COLLIER ¶ 60.57.

68. 11 U.S.C. § 93 (1970).

69. *Id.* § 96. Section 60a(1) of the Act defines a preference as

> a transfer . . . of any property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt, made or suffered by such debtor while insolvent and within four months before the filing by or against him of the petition initiating a proceeding . . . the effect of which transfer will be to enable such creditor to obtain a greater percentage of his debt than some other creditor of the same class.

11 U.S.C. § 96(a)(1) (1970).

tion and concluded that the elements of a voidable preference were present.[70]

In *Gorman v. Atlas Mortgage and Insurance Co. (In re Hamach Utilities Construction, Inc.)*,[71] the bankrupt, while insolvent, delivered an insurance check to a creditor to satisfy an antecedent debt. At the time, the creditor held two promissory notes executed by the bankrupt, which were over five months delinquent. The bankrupt's business office had been closed, and all its vehicles were gone.

The creditor was held to have knowledge of the insolvency at the time of the transfer, and the preference was declared voidable. "It is sufficient that a state of facts has been brought to the creditor's attention concerning the affairs and financial condition of the Bankrupt which would lead a prudent businessman to the conclusion that the Bankrupt is insolvent."[72]

V. SECURED PARTIES AND LESSORS

A. *Creditors*

In *ITT Automotive Parts Distributors, Inc. v. Gorman (In re Nordic Enterprises, Inc.)*,[73] a proceeding to determine the validity and enforceability of a security interest in the bankrupt's inventory, the trustee argued that the creditor had disposed of the collateral in a "commercially unreasonable manner,"[74] thereby forfeiting its right to a deficiency and to the entire security interest.[75]

The creditor had obtained a state court judgment requiring the bankrupt to turn over its inventory to the creditor, who then notified the bankrupt that it would offer the inventory for sale on one week's notice.[76] On the day of notification, the voluntary petition in bankruptcy was filed. The creditor took possession of the collateral, making a bookkeeping entry crediting the bankrupt's open account, but the sale was never held. The trustee, meanwhile, did not subsequently assert any right of possession in the collateral.

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70. *See* note 69 *supra*. The indemnity agreement was for an antecedent debt since it was executed at an earlier date than it was filed. It does diminish the estate for unsecured creditors as a class, since it would withdraw the secured property from the estate available for later distribution.

71. 12 C.B.C. 646 (M.D. Fla. 1977).

72. *Id.* at 650. *See also* Judson v. Popular Bank (*In re* Decorators Unlimited, Inc.), No. 76-442 (S.D. Fla. Feb. 28, 1977) (suggesting that the creditor should have examined the debtor's business records, since the creditor, the bankrupt's bank, had been refused access to financial statements over one year prior to the preferential transfer).

73. No. 74-662 (M.D. Fla. June 14, 1977).

74. *See* FLA. STAT. § 679.504(3) (1977).

75. *Id.* § 679.507.

76. *Id.* § 679.504(3).

The court observed that because the creditor's interest on the date of filing was only a security interest, the automatic stay provision under Bankruptcy Rule 601[77] would be determinative of the validity of the transfer in question.

The trustee was thus entitled to restoration of the collateral as it existed on the date the petition was filed. In addition, section 9-504 of the Uniform Commercial Code,[78] relating to "commercial reasonableness," would not apply unless the secured party elected to liquidate the collateral. Since there was no equity in the property, the estate was not authorized to retain it.

B. *Reclamation Rights of Sellers and Consignors*

1. SELLERS

One of the major questions existing under the Uniform Commercial Code is whether the section 2-702[79] reclamation rights reflect a security interest or simply a right to undo the transaction.[80] The determination of whether the right to reclaim is a security interest could mean the difference between a creditor being treated as unsecured or secured in the bankruptcy court, and the question of how the secured interest is perfected could be of even greater importance in terms of priorities.

Substantial disagreement also exists over whether the seller's interest under section 2-702[81] is a statutory lien "which first becomes effective upon the insolvency," and is therefore invalidated by section 67c(1)(A) of the Act.[82] In Florida, because section 2-702 has not been amended to eliminate the superior position of the lien creditor over the defrauded seller, the trustee in bankruptcy becomes a supe-

77. Bankruptcy Act, Rule 601, 11 U.S.C. Rule 601 (Supp. III 1973).

78. FLA. STAT. § 679.504(3) (1977).

79. *Id.* § 672.702.

80. Section 672.702 provides in pertinent part:

> (2) where the seller discovers that the buyer has received goods on credit while insolvent he may reclaim the goods upon demand made within 10 days after the receipt, but if misrepresentation of solvency has been made to the particular seller in writing within 3 months before delivery the 10-day limitation does not apply . . . .
>
> (3) The seller's right to reclaim . . . is subject to the rights of a . . . lien creditor . . . . Successful reclamation of goods excludes all other remedies with respect to them.

81. *Id.*

82. 11 U.S.C. § 107(c)(1)(A). *Compare* Carnation Plastic Mfg. Co. v. Giltex, Inc. (*In re* Giltex, Inc.), 17 U.C.C. Rep. 887 (S.D.N.Y. 1975) (invalidating as statutory lien); *In re* Good Deal Supermarkets, Inc., 384 F. Supp. 887 (D. N.J. 1974) *and In re* Federals, Inc., 12 U.C.C. Rep. 1142 (E.D. Mich. 1973) (invalidating as to trustee) *with* Alfred M. Lewis, Inc. v. Holzman (*In re* Telemart Enterprises, Inc.), 524 F.2d 761 (9th Cir. 1975).

rior lien creditor under section 70c of the Act,[83] the "strong-arm" clause.

In *Marcrest Pacific Co. v. Celtic Corp. (In re Celtic Corp.)*,[84] a defrauded seller claimed that he was entitled to a general lien on all the debtor's assets because the debtor had disposed of property purchased from the creditor without payment. On the same day that the bankrupt filed under chapter XI, the creditor delivered steel beams to the debtor's plant. Four days later, the seller demanded return of the beams under 2-702(2) of the Uniform Commercial Code.[85] The bankrupt debtor refused the demand.

By the time the action was commenced, the bankrupt no longer possessed the beams. They had been used in the construction of mobile homes, which the bankrupt had sold. Under the Florida version of section 2-702, the seller's rights cannot be enforced against the trustee, who becomes a lienor under section 70c of the Act.[86]

2. CONSIGNORS

In *Gorman v. Penny (In re Trier's Kimball Piano and Organ Center, Inc.)*,[87] the bankrupt sold organs and pianos on a consignment basis, as consignee. None of the consignors had executed security agreements or filed financing statements, but when the consignee filed for bankruptcy, the consignors brought an action to reclaim their property.

Section 2-326 of the Uniform Commercial Code[88] provides that goods sold on a "sale or return" basis are subject to claims of the consignee's creditors while in the consignee's possession, unless the consignor establishes that the consignee's creditors are aware of the consignments.[89] A consignor may also protect his property by perfecting a security interest in the property under Article 9 of the Uniform Commercial Code.[90]

In this case, the court held that where a "majority" of the

83. Bankruptcy Act § 70c, 11 U.S.C. § 110(c) (1970).

84. 13 C.B.C. 478 (M.D. Fla. 1977).

85. *See* note 80 *supra*.

86. Bankruptcy Act § 70c, 11 U.S.C. § 110(c) (1970). The court also found it unnecessary to determine whether the § 2-702 reclamation right is a statutory lien, a disguised priority or a voidable preference, because the collateral was not in the debtor's possession and could not be traced. Marcrest Pac. Co. v. Celtic Corp. (*In re* Celtic Corp.), 13 C.B.C. at 482.

87. 3 BANKR. CT. DEC. (CRR) 1005 (July 18, 1977).

88. FLA. STAT. § 672.326 (1977).

89. *Id.* § 672.326(3). In the absence of such a statute, the consigned property is subject to the trustee's claim. *See* 4A COLLIER ¶ 70.18[5].

90. FLA. STAT. § 672.326(3)(c) (1977).

consignee's creditors knows that the consignee deals in the goods of others, the consignor will prevail as to all creditors.[91]

C. *"Cram-Downs"*

In *In re Georgetown Apartments*,[92] the bankruptcy court held, *inter alia*, that a chapter XII arrangement[93] could not be accepted by the vote of all unsecured creditors over the rejection of the plan by secured creditors, even though the secured creditors would be adequately protected under the Act's "cram-down" provisions.[94] The debtor, a partnership engaged in the management of apartment houses, had obtained the unanimous approval of its unsecured creditors of a plan of arrangement, and several alternative plans. All of the plans had been rejected by the secured creditors, who were mortgagees. The secured creditors moved to dismiss the case on the ground that the plan could not be confirmed over the unanimous opposition of the secured creditors. The debtor sought confirmation, in response, on the ground that the acceptance of the secured creditors was unnecessary, since the secured creditors were not "affected by the plan."[95] Even if the secured creditors were affected, the debtor claimed they were adequately protected by section 461(11)(d) of the Act.[96]

Under section 407 of the Act,[97] creditors are "affected" by an arrangement only if their interest shall be materially and adversely affected thereby. Under section 468,[98] an application for confirmation may be filed with the court after the plan is accepted by the affected creditors holding two-thirds of the debts; creditors who are either not affected or who are protected by section 461(11)[99] are not included in this computation.[100]

Section 461(11) of the Act, known as the "cram-down" provision, protects classes of creditors by the transfer or sale of property by the debtor, payment in cash or any other equitable method that

91. This is arguably consistent with the language of § 672.326(3)(b) that the consignee "is generally known by his creditors to be substantially engaged in selling the goods of others." *See also* Buchanan v. Mobile Home Guar. Co. (*In re* Int'l Mobile Homes), 14 U.C.C. Rep. 1150 (E.D. Tenn. 1974); *In re* Fabers, Inc., 12 U.C.C. Rep. 126 (D. Conn. 1972); Guardian Discount Co. v. Settles, 114 Va. App. 418, 151 S.E.2d 530 (1966).

92. 3 BANKR. CT. DEC. (CRR) 512 (July 12, 1977).

93. Bankruptcy Act ch. XII, 11 U.S.C. §§ 801-926 (1970).

94. *Id.* § 461(11), 11 U.S.C. § 861(11).

95. *See id.* § 407, 11 U.S.C. § 807.

96. 11 U.S.C. § 861(11)(d) (1970).

97. *Id.* § 807.

98. *Id.* § 868.

99. *Id.* § 861(11).

100. Marcrest Pac. Co. v. Celtic Corp., 13 C.B.C. 478, 505 (M.D. Fla. 1977).

will adequately protect the creditors.

In *Georgetown Apartments*, after determining that the total value of the debtor's property was greater than the secured debt,[101] the court held that the secured creditors would be "affected." The debtor, meanwhile, had argued that the secured creditors would not be "affected" since the proposed plan would have furnished the creditors the same as that which they would have received on foreclosure—net cash flow from the property.[102]

The court felt that this argument ignored the proper test to determine whether a creditor has been affected.

> If the effect of the arrangement is to impair the actual value of the creditor's claim *or to prejudice any of the legal incidents of the claim*, then . . . the interest of the creditor is materially and adversely affected. . . . But aside from general creditors who are being paid in full in cash, it seems that *any* creditor who is dealt with in the arrangement is materially and adversely affected thereby.[103]

The bankruptcy court held that the creditors were "affected" because they were deprived of some of the legal incidents of the debt—the right to immediate payment of the amount past due and the right to monthly payments under the mortgage. Moreover, the court felt that nothing less than full payment would provide "adequate protection" for the creditors, since the value of the property exceeded the amount of the debt.[104]

A vote of unsecured creditors, according to the court, may not compel acceptance of the plan over the unanimous rejection of the secured creditors. Just because the secured creditors are adequately protected does not authorize the bankruptcy court to force acceptance, if the creditors are unanimously opposed to the plan.[105]

The court further held that a plan extending a mortgage held by a creditor for five years, with the creditor to be paid all remaining

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101. In such situation, under the cram-down provision, the creditors may be forced to accept less than the value of the debt.

102. The debtor argued that the secured creditors would receive only the net cash flow on foreclosure because no third party would bid on the property at the foreclosure sale, with the result that the secured creditor would, in any event, be forced to operate the property. 13 C.B.C. at 505.

103. *In re* Georgetown Apartments, 3 BANKR. CT. DEC. (CRR) at 516 (quoting 8 COLLIER ¶ 243).

104. *See* Rader v. Boyd, 267 F.2d 911 (10th Cir. 1959); *In re* Nob Hill Apartments, 11 C.B.C. 101 (N.D. Ga. 1976).

105. *In re* Georgetown Apartments, 3 BANKR. CT. DEC. (CRR) at 519. *See* Meyer v. Rowen, 195 F.2d 263, 266 (10th Cir. 1952); Security Title Ins. Co. v. Alpine & Lake Tahoe Paradise, Ltd. (*In re* Alpine & Lake Tahoe Paradise, Ltd.), 7 C.B.C. 286 (S.D. Cal. 1975) (both cited with approval in *Georgetown Apartments*).

cash flow after satisfaction of property taxes and maintenance costs, was not "adequate protection."[106]

This conclusion, however, is contrary to the language of section 461(11) of the Act,[107] which seems sufficiently broad to encompass extended payment plans that eventually provide complete compensation of secured creditors. Furthermore, at least one recent case construing section 461(11) has sanctioned extended payment of a mortgage to meet the chapter XII goal of substituting arrangement for liquidation, when possible.[108]

The state of the law is not as clear as the court in *Georgetown Apartments* would make it appear. Section 461(11) was added in the 1938 Chandler Act[109] to eliminate the ability of secured creditors to foil a potentially successful plan of arrangement by foreclosing on the debtor's real property, often the primary asset of the bankruptcy estate. The amendment removed secured creditors as an impediment to a successful arrangement by eliminating the secured party's right to vote a plan of arrangement once adequate protection has been provided pursuant to section 461(11).[110]

The designed "cram-down" effect was endorsed further by a 1952 amendment[111] which removed the "fair and equitable" test

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106. *In re* Georgetown Apartments, 3 BANKR. CT. DEC. (CRR) at 519.

107. An arrangement—

. . . .

(11) shall provide for any class of creditors which is affected by and does not accept the arrangement by the two-thirds majority in amount required under this chapter, adequate protection for the realization by them of the value of their debts against the property dealt with by the arrangement and affected by such debts, either, as provided in the arrangement or in the order confirming the arrangement . . . (d) by such method as will, under and consistent with the circumstances of the particular case, equitably and fairly provide such protection

. . . .

Bankruptcy Act § 461, 11 U.S.C. § 861 (1970).

108. *In re* Triangle Inn Assocs., 3 BANKR. CT. DEC. (CRR) 716 (Sept. 15, 1977).

109. Chandler Act, ch. 575, § 461, 52 Stat. 921 (1938) (current version at 11 U.S.C. § 861 (1970)).

110. This is clear from the language of § 468:

If an arrangement has not been so accepted, an application for the confirmation of an arrangement may be filed with the court within such time as the court shall have fixed in the notice of such meeting, or at or after such meeting and after, but not before—

(1) it has been accepted in writing by the creditors of each class, holding two-thirds in amount of the debts of such class affected by the arrangement proved and allowed before the conclusion of the meeting, or before such other time as may be fixed by the court, exclusive of creditors or of any class of them who are not affected by the arrangement or for whom payment or protection has been provided as prescribed in paragraph (11) of section 461 . . . .

Bankruptcy Act § 468, 11 U.S.C. § 868 (1970).

111. Bankruptcy Act Amendments of 1952, Pub. L. No. 82-456, § 472, 66 Stat. 835.

from section 472.[112] The amendment was added to prevent secured creditors from impairing, if not actively making valueless, the relief provided by chapter XII, by claiming absolute priority to their collateral and disposing of the collateral before the unsecured creditors could approve a successful arrangement.

Several recent cases likewise support this view of section 461 (11).[113] It is clear, then, that this section poses what a district court in New York described as a "potent threat"[114] to the positions of secured creditors in chapter XII arrangements.

D. *Validity of Security Interests*

In *In re Coed Shop, Inc.*,[115] the court held that a lien filed under the Florida statute[116] permitting a lender to use, as collateral, a debtor's liquor license, does not constitute a central filing system that may supplant the filing provisions of Article 9 of the Uniform Commercial Code.[117] The bankrupt's creditor had taken first lien on the bankrupt's liquor license and thereafter filed the lien with the Division of Alcoholic Beverages and Tobacco;[118] he did not, however, file a financing statement under article 9.

Since the trustee, under section 70c of the Act,[119] succeeds to the status of a hypothetical lien creditor at the date of bankruptcy, a security interest or lien which does not attach or is not perfected until after the date of bankruptcy is inferior to the trustee's interest.[120]

The court also rejected the argument that the erroneous filing was salvaged by section 9-401(2) of the Uniform Commercial Code,[121] which preserves the effectiveness of a filing made in good faith but at an improper place or otherwise incorrectly. This section, the court noted, was designed to allow a filing to be effective if made in good faith, but only as against persons with actual knowledge of the existence of the security interest. A trustee in bankruptcy "is deemed to have complied with all applicable requirements of state

112. 11 U.S.C. § 872 (1970).

113. *See* Sumida v. Yumen, 409 F.2d 654 (9th Cir. 1969); *In re* Triangle Inn Assocs., 3 BANKR. CT. DEC. (CRR) 716 (Sept. 15, 1977); *In re* Hartsdale Assocs., 3 BANKR. CT. DEC. (CRR) 460 (June 16, 1977); *In re* Pine Gate Assocs., Ltd., 2 BANKR. CT. DEC. (CRR) 1478 (Oct. 14, 1976).

114. *In re* Hartsdale Assocs., 3 BANKR. CT. DEC. (CRR) at 464.

115. 435 F. Supp. 472 (N.D. Fla. 1977).

116. FLA. STAT. § 561.65(a) (1977).

117. *Id.* § 679.302(3)-(4).

118. *Id.* § 561.65(a).

119. 11 U.S.C. § 110(c) (1970).

120. *In re* Coed Shop, Inc., 435 F. Supp. at 474.

121. FLA. STAT. § 679.401(2) (1977).

law for a lien of legal or equitable process and he is *without notice.*"[122]

E. *Lessor's Termination Rights*

Section 70b of the Act[123] declares lease provisions which purport to terminate a lease upon bankruptcy enforceable. Even so, at least in reorganizations, the statute has not dispensed completely with the common law disfavor of forfeitures.[124]

In addition, the judiciary has generally been disinclined to enforce forfeiture provisions if enforcement would substantially impair the success of the rehabilitation of the debtor or would deprive the bankruptcy estate of its principal assets.[125]

The courts have also effectively circumvented the Act by using state law; for example, courts have concluded that a landlord had somehow waived his right to enforce the forfeiture clause,[126] and have otherwise interpreted state law regarding forfeitures in order to reach the desired result.[127]

Moreover, it is now recognized that chapter XI proceedings are a proper forum for the exercise of the bankruptcy judge's equitable discretion in preventing lease terminations under such default provisions.[128] Such equitable powers have been employed forcefully where the lessee is current in his payments and has not impaired the value of his leasehold,[129] where it would do little good for the creditor, and where termination would substantially harm the debtor.[130]

In *In re Thrift Oil Co.*,[131] a bankruptcy termination clause was enforced, even though the lessor had actual knowledge of the bankruptcy proceeding, and the lessor had waited four months past filing

122. 435 F. Supp. at 475. *See also* 4A COLLIER ¶ 70.53.

123. 11 U.S.C. § 110(b) (1970).

124. Such provisions are often weighed against the public's interest in successful reorganizations. *See* Smith v. Hoboken R.R., Warehouse & S.S. Connecting Co., 328 U.S. 123 (1946).

125. *See* Pennsylvania Real Estate Inv. Trust v. Fontainebleau Hotel Corp. (*In re* Fontainebleau Hotel Corp.), 515 F.2d 913 (5th Cir. 1975); Queens Blvd. Wine & Liquor Corp. v. Blum, 503 F.2d 202 (2d Cir. 1974); *In re* Fleetwood Motel Corp., 335 F.2d 857 (3d Cir. 1964).

126. *See, e.g.*, Larkins v. Sills, 377 F.2d 1 (5th Cir. 1967); *In re* Speare, 360 F.2d 882 (2d Cir. 1966); B.J.M. Realty Corp. v. Ruggieri, 338 F.2d 653 (2d Cir. 1964); Geraghty v. Kiamie Fifth Ave. Corp., 210 F.2d 95 (2d Cir. 1954).

127. *See, e.g., In re* Fontainebleau Hotel Corp., 515 F.2d 913 (5th Cir. 1975).

128. *See In re* M&M Transp. Co., 437 F. Supp. 821, 822 (S.D.N.Y. 1977); *In re* D.H. Overmyer Co., 383 F. Supp. 21 (S.D.N.Y. 1974), *aff'd*, 510 F.2d 329 (2d Cir. 1975).

129. Thus, the court precluded the "unclean hands" defense.

130. *See In re* M&M Transp. Co., 437 F. Supp. 821, 822-23 (S.D.N.Y. 1977).

131. Crowder v. Thrift Oil Co. (*In re* Thrift Oil Co.), 3 BANKR. CT. DEC. (CRR) 1052 (Dec. 2, 1977).

of the petition to invoke the provision. The court also held that although the lessor had accepted tardy rental payments, this did not constitute a waiver of the lessor's right to enforce the termination provision.[132] Distinguishing two major cases,[133] the court found that an unreasonable time period had not elapsed between knowledge and termination (four months), and that no aspect of public interest required continuation of the lease.

F. *Garnishments*

In 1966, the Supreme Court of the United States held in *Bank of Marin v. England*[134] that a bank which honored checks of a bankrupt drawn before its bankruptcy but presented for payment after the filing of the petition is *not liable* to the trustee for the amount of the check, so long as the bank had no knowledge of the bankruptcy.[135] Though oft-criticized, *Marin* has never been overruled.

In *In re Ed L. Thomas Co.*,[136] despite substantial criticism, the bankruptcy court extended *Marin* to absolve a garnishee bank from liability to the trustee when the bank, which had no knowledge of the proceedings, satisfied a state court garnishment writ after bankruptcy.[137]

The court here absolved the bank under the *Marin* rule, since the bank was required under Florida law to satisfy the writ. In that sense, its position was analogous to that of the bank in *Marin*, which was relieved through the invocation of equity.[138]

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132. *Id.* at 1053.

133. *In re* Fontainebleau Hotel Corp., 515 F.2d 913 (5th Cir. 1975); Queens Blvd. Wine & Liquor Corp. v. Blum, 503 F.2d 202 (2d Cir. 1974). These cases are especially significant because of their application of the bankruptcy court's equitable powers. 3 BANKR. CT. DEC. (CRR) at 1054.

134. 385 U.S. 99 (1966).

135. The Court held that mere filing of the bankruptcy petition is not per se enough to put the bank on notice. Using "equitable principles," the Court held that under § 70d(5) of the Act, 11 U.S.C. § 110(d)(5) (1970), "it would be inequitable to hold liable a drawee who pays checks of the bankrupt duly drawn but presented after bankruptcy, where no actual revocation of its authority had been made and it had no notice or knowledge of the bankruptcy." 385 U.S. at 103.

136. Raymos v. American Laundry Mach. (*In re* Ed L. Thomas Co.), 3 BANKR. CT. DEC. (CRR) 1142 (Dec. 8, 1977).

137. The court so held despite the garnishee bank's claim that it was protected by § 70d of the Act since, according to the court, that section applies "only to transfers made *after* the filing of the bankruptcy petition and *before* adjudication or before receiver takes possession of the property of the bankrupt, whichever first occurs." *Id.* at 1142. Adjudication had already occurred when the writ was satisfied; therefore, § 70d was inapplicable. *See also* 4A COLLIER ¶ 70.67.

138. *Marin* has come to stand for the principle that "bankruptcy courts are essentially courts of equity to be guided by equitable doctrines and principles." *In re* Smith, 436 F. Supp. 469, 480 (N.D. Ga. 1977). *See also In re* Peterson, 437 F. Supp. 1068, 1070 (D. Minn. 1977).

But the garnisher-creditor did not fare as well. *Marin* was silent on the creditor's fate, because there the bankrupt himself had withdrawn the funds. In *Ed L. Thomas Co.*, the court applied the literal language of section 70d(5) to require the creditor to remit to the trustee all funds gleaned by the writ of garnishment.[139]

Regardless of the wisdom of the decision in *Marin*, the extension of its rule in *Ed L. Thomas Co.* does little, if any, harm to the bankrupt's estate. Since *Marin* did not involve a third party creditor or payee, the Supreme Court of the United States had no opportunity or necessity to rule upon whether the same equitable principles that protected the bank would protect the payee-creditor. Since the bankruptcy court here found the presence or absence of good faith irrelevant, the trustee may still look to the garnisher as an alternate source of payment.

VI. LIENORS

A. *Retail Sales*

In *In re Kennedy & Cohen, Inc.*,[140] the bankrupt, because of liquidation, was unable to perform appliance maintenance contracts, under which it had accepted payment from customers for a two year period. The court refused to impose a constructive trust upon the funds so received; a contrary decision would have removed the funds from the court's jurisdiction. Without a showing of wrongdoing by the bankrupt, and without an allegation that the bankrupt knew prior to bankruptcy that the contracts could not be performed, a constructive trust was not warranted.[141]

B. *Priorities and Choateness*

In Florida, the personal property tax is established in two steps[142] that are conditions precedent to its choateness. If the county tax lien does not become choate before the date of a federal lien for administrative and wage claims,[143] the federal lien will prevail.[144] Under federal law, a lien is inchoate when the certainty of amount,

139. 3 BANKR. CT. DEC. at 1143.

140. Wisconsin v. Reese (*In re* Kennedy & Cohen, Inc.), No. 76-97 (S.D. Fla. May 5, 1977).

141. The court also found that a constructive trust could not be imposed without an identifiable trust res to which the trust could attach.

142. *See* FLA. STAT. §§ 194.011, 195.096(2), .200 (1977).

143. *See* Bankruptcy Act § 67c(1)(C)(3), 11 U.S.C. § 107(c)(1)(C)(3) (1970).

144. A federal tax lien is, in actuality, superior to *all* other liens not choate at the time the federal tax lien is filed. United States v. Pioneer Am. Ins. Co., 374 U.S. 84 (1963); United States v. Crittenden, 563 F.2d 678, 683-84 (5th Cir. 1977).

exact identity of the lienor and time of attachment must await future determination.[145]

In the Court of Appeals for the Fifth Circuit, the "first in time, first in right" rule of priorities has been held inapplicable, in *United States v. Crittenden*,[146] to a situation involving a prior federal mortgage lien and a state-created mechanic's lien. Though not a bankruptcy case, the decision is nonetheless important because of the status it grants to mechanic's liens.[147] A mechanic's lien, the Fifth Circuit also held, would be superior to the federally-created lien only so long as the mechanic remains in continuous possession of the collateral.[148]

In 1977, the Court of Appeals for the Fifth Circuit also held that since protection is provided for future advances secured by earlier security agreements under the Uniform Commercial Code,[149] the choateness doctrine would not be invoked to give priority to a federal mortgage claim over a secured creditor making a future advance.[150]

Taken together, these decisions seem to indicate that the Tax Lien Act[151] standards may serve as a benchmark for the determination of priorities of federal vis-à-vis state-created liens.

VII. Access to Bankruptcy Relief

A. *Entity Status*

In 1977, the Middle District of Florida refused to allow a corporate debtor, whose chapter XI petition was dismissed because of the absence of unsecured creditors, to convert the proceedings to chapter XII despite the debtor's contention that the corporate veil should

145. United States v. City of New Britain, 347 U.S. 81, 84 (1954); United States v. White, 325 F. Supp. 1133 (S.D. W. Va. 1971); Stein v. Moot, 297 F. Supp. 708, 711 (D. Del. 1969). A federal test of choateness is applied when at least one lien at issue is that of a federal entity. United States v. Oswald & Hess Co., 345 F.2d 886 (3d Cir. 1965). But where no federal interests are at stake, the validity, nature and effect of a state lien is still governed by state law. *See* Porter v. Searle, 228 F.2d 748 (10th Cir. 1955).

146. 563 F.2d 678 (5th Cir. 1977). See also Connecticut Mut. Life Ins. Co. v. Carter, 446 F.2d 136 (5th Cir.), *cert. denied*, 404 U.S. 857 (1971), which the Fifth Circuit construed to hold that "in light of the Tax Lien Act, the choateness doctrine would not be applied to determine the relative priority of a lien for attorney's fees contained in a first mortgage on farm property and a second mortgage lien held by" the Farmers Home Administration. 563 F.2d at 684-85.

147. *See* Fla. Stat. § 679.310 (1977).

148. 563 F.2d at 691.

149. *See* Fla. Stat. § 679.204 (1977).

150. Kimbell Foods, Inc. v. Republic Nat'l Bank, 557 F.2d 491 (5th Cir. 1977). For the Florida UCC provisions on priorities of security interests, see Fla. Stat. § 679.312 (1977).

151. I.R.C. §§ 6321-26.

be ignored.[152] Since the debtor had, four years prior to the filing of the petition, agreed to corporate status for the purpose of securing a loan, the fact that it had never issued stock, maintained a bank account or evinced other corporate attributes, did not preclude its recognition by the court as a corporation.[153]

The court distinguished this case from situations where the *trustee* seeks to pierce the corporate veil in order to prevent injustice to creditors, noting that its equitable powers may be used to provide such relief.[154]

B. *Civil Rights*

In a case of first impression, the Court of Appeals for the Fifth Circuit, in *McLellan v. Mississippi Power & Light Co.*,[155] held that an employer does not violate section 1985(3) of the Ku Klux Act of 1871[156] by firing an employee because he is adjudged bankrupt.

Basing its decision on an equal protection analysis,[157] the Fifth Circuit noted that if the defendant's actions would be legal *apart from* section 1985(3), "the conspiracy could not have deprived the plaintiff of the 'protection of the laws.'"[158] Since nothing in the Bankruptcy Act nor any law in Mississippi expressly prohibited an

152. *In re* Eastwood Properties, Inc., 3 BANKR. CT. DEC. (CRR) 1023 (Nov. 9, 1977).

153. Chapter XII proceedings are available only to noncorporate entities. Bankruptcy Act § 406(6), 11 U.S.C. § 806(6) (1970). Chapter XI proceedings, meanwhile, are available to both corporate and noncorporate entities.

154. 3 BANKR. CT. DEC. at 1025. *See also* Markow v. Alcock, 356 F.2d 194 (5th Cir. 1966); Mayo v. Pioneer Bank & Trust Co., 270 F.2d 823 (5th Cir. 1959).

155. 545 F.2d 919 (5th Cir. 1977) (en banc).

156. 42 U.S.C. § 1985(3) (1970). That section provides, in pertinent part:

> If two or more persons . . . conspire . . . for the purpose of depriving, either directly or indirectly, any person or class of persons of the equal protection of the laws or of equal privileges and immunities under the laws; . . . in any case of conspiracy set forth in this section, if one or more persons engaged therein do, or cause to be done, any act in furtherance of the object of such conspiracy, whereby another is injured in his person or property, or deprived of having or exercising any right or privilege of a citizen of the United States, the party so injured or deprived may have an action for the recovery of damages, occasioned by such injury or deprivation, against any one or more of the conspirators.

157. The court pointed out that four elements comprise a cause of action under § 1985 (3), as mandated by Griffin v. Breckenridge, 403 U.S. 88, 101 (1971):

> (1) the defendants must conspire
>
> (2) for the purpose of depriving, either directly or indirectly, any person or class of persons of the equal protection of the laws, or of equal privileges and immunities under the laws; and
>
> (3) the defendants must act in furtherance of the conspiracy whereby
>
> (4) one was (a) injured in his person or property or (b) deprived of having and exercising any right or privilege of a citizen of the United States.

545 F.2d at 923. The court focused on paragraph (2) above.

158. 545 F.2d at 925.

employer from firing a bankrupt employee, the court found for the defendants.[159]

Although criticized since its publication,[160] the *McLellan* "independent illegality" test has not been rejected by any other court. Until rejected by the Supreme Court or changed by statute, the test appears to fashion a reasonably clear standard for the Fifth Circuit.

VIII. Rejection of Executory Contracts

Section 70b of the Act[161] provides that the trustee must assume or reject an "executory contract" within sixty days of adjudication or within thirty days of his qualification, whichever is later. Any contract not assumed or rejected within the time is deemed rejected by operation of the statute. Under section 313(1) of the Act,[162] the court may permit rejection of any executory contract of the debtor upon notice to the other parties to the contract. The trustee's rejection is deemed a breach of contract as of the date of filing the original chapter XI petition.[163]

Under section 313 of the Act,[164] there is no limit on the bankruptcy court's authority to reject an executory contract so long as it is truly executory.[165] The executory contract may not be partly rejected; it must be completely rejected or assumed.[166]

Though not defined in the Act itself, the case law views an executory contract as one in which "there remains any part . . . unperformed."[167] To be remembered is that section 70b of the Act authorizes the trustee to apply for permission to reject a contract that is executory "in whole or in part."[168] If the contract is rejected with the court's permission, the breach resulting therefrom may

159. The court did point out, however, that both of the proposed new Bankruptcy Acts contain identical language that would prohibit discriminatory action against a person who has filed for bankruptcy. *Proposed Amendments to the Bankruptcy Act: Hearings on H.R. 31-32 Before the Subcomm. on Civil and Constitutional Rights of the Comm. on the Judiciary*, 94th Cong., 1st & 2d Sess. 357, app. (1975 & 1976).

Currently, there is no fundamental right to file in bankruptcy. United States v. Kras, 409 U.S. 434, 445 (1973).

160. *See* 90 Harv. L. Rev. 1721 (1977).

161. 11 U.S.C. § 110(b) (1970).

162. *Id.* § 713(1) (1970).

163. Bankruptcy Act § 63c, 11 U.S.C. § 103(c) (1970).

164. 11 U.S.C. § 713 (1970).

165. *See In re* Klaber Bros., Inc., 173 F. Supp. 83, 85 (S.D.N.Y. 1959); 8 Collier ¶ 3.15[1].

166. 8 Collier ¶ 3.15[7].

167. *See, e.g., In re* Philadelphia Penn Worsted Co., 278 F.2d 661, 664 (3d Cir. 1960).

168. 11 U.S.C. § 110(b) (1970).

transform the other party to the contract into a creditor of the estate.

In *In re Kassabay*,[169] the debtor entered into a series of interrelated agreements whereby a real estate developer would construct apartment projects on the debtor's land. An "agreement for deed" provided that if the construction agreement were not in default, the developer could himself acquire the real estate.

While in default, the developer attempted to sell his interest to a third corporation. An agreement reflecting that sale was recorded, thereby putting a cloud on the debtor's title. The court held that the "agreement for deed," since it was not intended to secure the payment of money, was technically not a mortgage and, therefore, could not properly be recorded.[170] Moreover, since agreements for deeds are executory contracts,[171] the developer was held to have no lien on the property and was relegated to the status of an unsecured creditor.

IX. Apparent Title

Section 726.09 of the Florida Statutes[172] operates to vest absolute title to chattels in one who receives them as a pretended loan for two years without a demand for their return.[173] This statute is used occasionally by the bankruptcy trustee to take title to property that has been "loaned" to the bankrupt for two years without a demand for its return.

Section 726.09 was held in 1975 not to apply to leases.[174] It has been recognized, however, that while the trustee may not hold a lien on property formally leased to the trustee, he nonetheless succeeds to the bankrupt's rights as lessee.[175]

X. Procedure

A. *Amended Claims*

The filing deadline for statements of claim under the Act is

169. No. 76-380 (S.D. Fla. Oct. 11, 1977).

170. *See* Fla. Stat. § 697.01 (1977).

171. First Mortgage Corp. v. deGive, 177 So. 2d 741 (Fla. 2d Dist. 1965).

172. Fla. Stat. § 726.09 (1977).

173. The statute has the same effect on loaned property which is "pretended" to have been tendered to another with a conditional reversion, remainder or similar interest remaining in the lender, unless the loan reservation or limitation is declared by a recorded document. *Id.*

174. American Indus. Leasing Co. v. Searles, 510 F.2d 996 (5th Cir. 1975).

175. American Indus. Leasing Co. v. Searles, 13 C.B.C. 230 (S.D. Fla. 1977), *on remand from* 510 F.2d 996 (5th Cir. 1975). Fla. Stat. § 726.09 (1977) is also inapplicable to mutual bailments. *See In re* Aircraft Casting, Inc., No. 76-899 (S.D. Fla. Feb. 28, 1977).

more than just a statute of limitations; it is absolute, as equity proof, and may not be extended by the bankruptcy court.[176] This principle was reinforced in 1977 when a creditor attempted to file a proof of claim eighteen months after a deadline; the motion was denied.[177]

Where, however, a creditor, prior to the expiration of the filing deadline, takes *some* action against the trustee from which the court may ascertain the nature and amount of the claim, the creditor may subsequently amend the claim after expiration of the filing period.[178]

B. *Discovery*

In *In re Dade County Dairies, Inc.*,[179] an involuntary proceeding, creditors sought an examination of the bankrupt's records pursuant to Bankruptcy Rule 205.[180]

The bankrupt first complained that the requested information was outside the scope of the transfer alleged in the petition. The court, in rejecting this objection, analogized to the Federal Rules of Civil Procedure[181] and, finding the requested information "relevant," held it discoverable.

The bankruptcy court, however, also found that the receiver, to whom the records had been surrendered involuntarily, unjustifiably granted the creditors full access without the bankrupt being afforded the opportunity to object and obtain a ruling.[182]

XI. FEES

Apparently prompted by the Court of Appeals for the Fifth Circuit's recent decision in *American Benefit Life Insurance Co. v.*

176. Section 57n of the Act provides, in part: "Except as otherwise provided in this title, all claims provable under this title, . . . shall be proved and filed in the manner provided in this section. Claims which are not filed within six months after the first date set for the first meeting of creditors shall not be allowed." Bankruptcy Act § 57n, 11 U.S.C. § 93(n) (1970).

177. *In re* Gallagher, No. 75-430 (S.D. Fla. Apr. 11, 1977). Judge Britton remarked, "It has not been suggested that any person would be prejudiced if this creditor is allowed now to file its claim. The motion is not opposed. If I had the lawful discretion to do so, I would grant the motion." *Id.*

178. *In re* Kilpatrick, No. 75-1798 (S.D. Fla. Aug. 10, 1977). The court also cited Fausett v. Murner, 402 F.2d 961 (5th Cir. 1968) and 3 COLLIER ¶ 57.11[3] for the proposition that so long as the existence, nature and amount of the claim is ascertained, and the parties would not be unduly prejudiced, an amendment would be allowed. The court "reluctantly" granted the motion to amend.

179. No. 77-841 (S.D. Fla. Aug. 12, 1977).

180. 11 U.S.C. Rule 205 (Supp. III 1973).

181. FED. R. CIV. P. 26.

182. The court distinguished this case from a voluntary proceeding, where the bankrupt's records are open to any creditor. No. 77-841.

Baddock (In re First Colonial Corp.),[183] the bankruptcy courts dealt more thoroughly and in greater detail with the questions raised by attorneys' fees. While most individual fee application decisions turn on their own facts and do not merit individual discussion, the already substantial and growing body of law concerning such awards is of the utmost importance to the practitioner.

A previously established twelve-part test for determining the reasonableness of attorneys' fees was applied to bankruptcy cases for the first time in *First Colonial*.[184] It requires consideration of:

> (1) The time and labor required; (2) The novelty and difficulty of the questions; (3) The skill requisite to perform; (4) The preclusion of other employment by the attorney due to acceptance of the case; (5) The customary fee; (6) Whether the fee is fixed or contingent; (7) Time limitations imposed by the client or other circumstances; (8) The amount involved and the results obtained; (9) The experience, reputation, and ability of the attorneys; (10) The "undesirability" of the case; (11) The nature and length of the professional relationship with the client; (12) Awards in similar cases.[185]

The district courts and bankruptcy judges are given broad discretion in determining attorneys' fees in connection with bankruptcy proceedings, and the determination will not be disturbed absent a showing of an abuse of discretion by the trial judge.[186] *First Colonial* does require that, in awarding attorneys' fees, the bankruptcy judge be "particularly diligent in setting forth the facts that support [the] conclusion."[187]

In addition to the twelve enumerated criteria for the determination of attorneys' fees, *First Colonial* requires that, because of the peculiar nature of bankruptcy proceedings, attorneys "should not expect to be compensated as generously for their services as they might be were they" otherwise employed.[188]

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183. 544 F.2d 1291 (5th Cir. 1977).

184. *See* Johnson v. Georgia Highway Express, Inc., 488 F.2d 714 (5th Cir. 1974). Section 64a(1) of the Bankruptcy Act, 11 U.S.C. § 104 (1970), provides that attorneys' fees must be reasonable.

185. 544 F.2d at 1298-99 (quoting Johnson v. Georgia Highway Express, Inc., 488 F.2d at 717-19).

186. *First Colonial*, 544 F.2d at 1298. *See* Morgan v. Walter E. Heller & Co. (*In re* Bemporad Carpet Mills, Inc.), 434 F.2d 988 (5th Cir. 1970); Massachusetts Mut. Life Ins. Co. v. Brock, 405 F.2d 429 (5th Cir. 1968).

187. 544 F.2d at 1298.

188. *Id.* at 1299. In determination of the actual amount of compensation, *First Colonial* mandates a three-step process: First, the court "must ascertain the nature and extent of the services supplied by the attorney" through a statement filed by the attorney, reciting the number of hours worked and a description of how the time was spent. *Id.* Second, the judge

Later in 1977, the Fifth Circuit also held that interim allowances must be set below any final fee.[189]

Attorneys' fees incurred in the rendering of services for the bankrupt are entitled to first priority as "administrative expenses" under section 64a(1) of the Act.[190] Compensable services are only those which "have aided in the *administration* of the estate, that is to say they must have assisted the bankrupt in performing his legal duties, not in exercising his legal privileges."[191] Any service volunteered or rendered without clear prior authorization is not compensable.[192] It is often said that the bankrupt's attorney is the "courts' favorite object in furthering economy."[193]

XII. DISCHARGES

A. *Debtors*

Section 14c(7) of the Act[194] provides that a discharge may be granted unless, *inter alia*, the bankrupt "has failed to explain satisfactorily any losses of assets or deficiency of assets to meet his liabilities." Normally, though, if the circumstances were "such that the normal person under like circumstances would not have kept books and records," the bankrupt will not be penalized for having failed to do so.[195]

1. BOOKS AND RECORDS

Thus, failure to keep books and records in a small (five automobiles) taxi cab business, where nearly all transactions were handled in cash, did not prevent a discharge.[196]

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sets the value of the services, under the twelve-part test. *Id.* at 1300. Third, the judge must explain his findings in detail. *Id.*

189. Machinery Rental, Inc. v. Herpel (*In re* Multiponics, Inc.), 551 F.2d 1049 (5th Cir. 1977). *See also* Lutheran Hosp. & Homes Soc'y v. Duecy, 422 F.2d 200 (9th Cir. 1970).

190. 11 U.S.C. § 104(a)(1) (1970). Section 62 of the Act, 11 U.S.C. § 102 (1970), authorizes the award of compensation from the bankrupt estate to attorneys for the trustee who assist in the administration of the estate. Section 64, meanwhile, gives priority to costs and expenses incurred in administration of the estate itself.

191. *In re* Rods & Guns, Inc., No. 76-1625 (S.D. Fla. Apr. 27, 1977).

192. *Id.*

193. 3A COLLIER ¶ 62.31[5].

In addition, Judge Britton has noted that through June 1975, trustees' and receivers' attorneys' fees nationwide averaged 6.7% of the total realized in bankruptcy cases. In the Southern District of Florida, for the same period, the fees averaged 10.9%. *See In re* Daryl Indus., Inc., No. 73-239 (S.D. Fla. Apr. 15, 1977). Based on this data, and the language of *First Colonial*, it is likely that the bankruptcy courts, in Florida at least, will subject attorneys' fees to strict scrutiny in the future.

194. 11 U.S.C. § 32(c)(7) (1970).

195. *In re* Weismann, 1 F. Supp. 723 (S.D.N.Y. 1932).

196. *In re* King, 13 C.B.C. 224 (S.D. Fla. 1977).

2. BURDEN OF PROOF

While Bankruptcy Rule 407 places the original burden of proof under section 14c of the Act on the creditor, it was pointed out in 1977 that there remains a de facto burden on the debtor to show his innocence.[197]

3. DEBTOR'S INTENT

It was also recognized during 1977 that a violation of section 14c(4)[198] cannot occur through a transfer of exempt homestead property, regardless of the transferee's intent.[199] Moreover, the reconveyance of fraudulently transferred property, even when the reconveyance occurs prior to filing of the petition, does not serve as a defense to section 14c(4).[200]

The Middle District of Florida recognized that so long as a debtor intends to transfer property in an effort to conceal the property from creditors, his motivation for so acting, even if highly altruistic (*e.g.*, to help pay for a sick relative's medical care), is not a valid defense in an action to bar a discharge.[201]

B. *Fraudulent Debts*

Section 17a of the Act[202] exempts from discharge any provable debt of the bankrupt created or obtained by fraud.[203] In *Oneida National Bank and Trust Co. v. Cote (In re Cote)*,[204] the secured

197. Appelberg v. Harrison (*In re* Harrison, Jr.), 12 C.B.C. 728 (M.D. Fla. 1977). *See also In re* Tucker, 399 F. Supp. 660, 660-61 (S.D. Fla. 1975).

198. Bankruptcy Act § 14c(4), 11 U.S.C. § 32(c)(4) (1970). This section precludes a discharge where the bankrupt, "at any time subsequent to the first day of the twelve months immediately preceding the filing of the petition in bankruptcy, transferred, removed, destroyed, or concealed, or permitted to be removed, destroyed, or concealed, any of his property with intent to hinder, delay, or defraud his creditors."

199. Bank of Miami v. Abaunza (*In re* Abaunza), No. 76-1611 (S.D. Fla. July 13, 1977).

200. *Id.*

201. McLeran v. Hobbs (*In re* Hobbs), 12 C.B.C. 663 (M.D. Fla. 1977).

202. Bankruptcy Act § 17a, 11 U.S.C. § 35(a) (1970).

203. Section 17a provides, in pertinent part:

> A discharge in bankruptcy shall release a bankrupt from all of his provable debts, whether allowable in full or in part, except such as . . . (2) are liabilities for obtaining money or property by false pretenses or false representations, or for obtaining money or property on credit or obtaining an extension or renewal of credit in reliance upon a materially false statement in writing respecting his financial condition made or published or caused to be made or published in any manner whatsoever with intent to deceive, or for willful and malicious conversion by another . . . [and except such as] (4) were created by his fraud, embezzlement, misappropriation, or defalcation while acting as an officer or in any fiduciary capacity.

11 U.S.C. § 35(a) (1970).

204. No. 76-425 (M.D. Fla. Feb. 8, 1977).

creditor argued that the debtor had violated section 17a(2) by disposing of the collateral without the creditor's consent.

The court first noted that in order to maintain an action for conversion at common law, the plaintiff must show a denial of a possessory right. Absent default by the debtor, however, the creditor has no such right. Next, the court addressed the issue of whether the creditor had been deprived of its lien through disposition of the collateral. Since the lien remains enforceable, as against subsequent transferees, the question was answered in the negative. Finally, without the requisite showing of malice and willfulness, the court held that a charge of conversion could not stand.[205]

In another case, the court held that under section 17a (2) of the Act,[206] the issuance of a worthless check is not sufficient to preclude the right to a discharge, absent affirmative proof of actual fraud.[207] A similar case found that where an agent of the creditor knows the debtor's check is worthless, such knowledge will not be imputed to the creditor himself.[208] This rule comports with accepted agency principles, which provide that knowledge of an agent is not imputed to the principal where the agent acts adversely to the principal's interest. According to the Middle District of Florida, knowing acceptance of a worthless check for the benefit of a principal by an agent is not a sufficient defense for a debtor in a section 17a action.

Section 17a(4) of the Act[209] also denies a discharge where a liability was created by the bankrupt's fraud while acting as an officer or in any other fiduciary capacity. However, where the trustee granted the bankrupt *permission* to dispose of assets, and so notified the creditor, who took no action, the court held the debt discharged as against the creditor.[210]

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205. *Id.* In Atlantic Bank v. Gilbert (*In re* Gilbert), No. 75-253 (M.D. Fla. Feb. 7, 1977), Judge Paskay pointed out that where a borrower promises to use the proceeds of a loan to satisfy an existing indebtedness, the debtor's representations of his financial condition and his promise will be relied upon by the creditor. If the borrower did not, in fact, intend to fulfill that promise, a finding of "willful and malicious conversion" may be warranted.

206. *See* note 203 *supra*.

207. A.G. Edwards & Sons, Inc. v. Marin (*In re* Marin), 12 C.B.C. 100 (M.D. Fla. 1977).

208. Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Kurant (*In re* Kurant), No. 77-00004 (M.D. Fla. Aug. 11, 1977).

209. *See* note 203 *supra*.

210. United States v. Park (*In re* Park), No. 75-1155 (M.D. Fla. May 16, 1977). The result was obtained even though the bankrupt, the corporation's president, had used the corporate assets for his own benefit. The court held that sale of the assets created a potential liability only in favor of the corporation, not the creditor, since the creditor's lien did not in fact cover the contested property. The court also noted, in dictum, that since the corporation had already been adjudicated bankrupt at the time the transaction occurred, the alleged debtor could not have been acting as an officer or in a fiduciary capacity, since the corporate affairs were being managed by the trustee.

C. *Effects of Discharge*

In *In re Crouse*,[211] the court drew a fundamental distinction between the bankrupt's personal liabilities and liens on its property: a discharge releases the bankrupt's personal liabilities; a valid lien which is not avoided pursuant to the Bankruptcy Act may still be enforced.[212]

The bankrupt also claimed that the security, household goods, was exempt from enforcement of the lien under the Constitution of Florida.[213] The court noted, in rejecting this argument, that "nothing in the Bankruptcy Act . . . invalidates an otherwise valid lien against exempt property merely because it relates to exempt property."[214] As pointed out elsewhere,[215] the bankruptcy court lacks jurisdiction to rule upon exempt property because such property is excluded from the bankrupt's estate.[216]

While the debtor can no longer be sued for the recovery of a money judgment against him on a discharged debt, it is possible for the debtor to "revive" this debt after discharge. When the debtor does so and then defaults on the revived debt, the proper procedure for the debtor who wishes to attempt to collect on the revived debt is to seek a request for relief from the injunction issued under section 14f(2) of the Act.[217]

However, it is not by implication or ambiguity that a debt discharged in bankruptcy will be revived. It is generally held that "'to be enforceable the new promise must be definite, express, distinct, and unambiguous. The debts covered by the new promise must be identified as those that were discharged in the bankruptcy

211. Nos. 76-1264, 76-1265 (S.D. Fla. Sept. 29, 1977).

212. A discharge in bankruptcy operates to "discharge the debt" and to enjoin creditors from "instituting . . . any action . . . to collect such debts as *personal liabilities of the bankrupt*." Binnick v. Avco Fin. Serv., 435 F. Supp. 359, 363 (D. Neb. 1977) (quoting, in part, § 14f(2) of the Act, 11 U.S.C. § 32(f)(2) (1970)) (emphasis added). *See generally In re* Thompson, 416 F. Supp. 991 (S.D. Tex. 1976); 1A COLLIER ¶¶ 14.69, 17.29.

213. FLA. CONST. art. X, § 4(a)(2).

214. Nos. 76-1264, 76-1265.

215. *See* note 12 *supra*.

216. Had *Crouse* involved a *money* judgment instead of a lien against property, the result would have been different since enforcement would require an in personam adjudication of the bankrupt's rights.

217. 11 U.S.C. § 32(f)(2) (1970). Section 14f provides that an order of discharge is to "(1) declare that any judgment theretofore or thereafter obtained in any court is null and void as a determination of the personal liability of the bankrupt" for any debts not accepted from the discharge under section 17; and (2) enjoin all creditors whose debts have been discharged from "thereafter instituting or continuing any action or employing any process to collect such debts as personal liabilities of the bankrupt." For the proper procedure in pursuing a revived debt that has fallen into default, see *In re* McCann, 387 F. Supp. 416, 417 (D. Kan. 1975).

proceeding.'"[218] It has also been held that a debt may be revived "only when by an unequivocal statement in writing the debtor expresses his present intention personally to obligate himself to pay the debt."[219]

In *Safeco Insurance Co. v. Andriesse (In re Andriesse)*,[220] the creditor sought relief from a stay in order to determine the full amount of an allegedly revived debt. The bankrupt's conduct in her employment had resulted in a loss to her employer of more than $10,000, which had been covered by the creditor's bond and paid by the creditor. Prior to filing the petition in bankruptcy, the state had brought criminal charges against the employee, in which the plaintiff played no part. The result of that criminal prosecution was probation, which required, among other things, that the bankrupt pay the creditor almost $4,000 in monthly installments of $200.

In compliance with the probation order the defendant made monthly installments. The creditor, claiming that the voluntary payments under the probation order had revived the debt, sought relief from the stay in order to litigate the amount still owed. This was granted. The court did not inquire into the creditor's ability to prove its allegation of revival, though the possibility would appear slim if the debt were truly barred, since the "promise" contained in the probation order did not run to more than $4,000 of the $10,000 debt.[221]

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218. Wichita City Teachers Credit Union v. Rider, 203 Kan. 552, 558, 456 P.2d 42, 48 (1969) (quoting 1 COLLIER ¶ 17.34).

219. Linzer v. Weitzen, 292 N.Y. 306, 309, 55 N.E.2d 42, 43 (1944).

220. No. 77-319 (M.D. Fla. Dec. 19, 1977).

221. Presumably, the creditor could not prevent the discharge of the debt under § 17 of the Act, 11 U.S.C. § 35 (1970), which only prevents the discharge of debts arising out of certain intentional criminal wrongdoings. Also, § 14f of the Act, 11 U.S.C. § 32 (f) (1970), does not bar a creditor from using otherwise lawful methods to persuade a debtor to revive or to pay a discharged debt so long as those efforts do not include any legal process. Girardier v. Webster College, 563 F.2d 1267 (8th Cir. 1977). It is generally improper for a creditor's attorney to threaten criminal prosecution in order to collect a debt. The ABA CODE OF PROFESSIONAL RESPONSIBILITY DR 7-105(a) states that "a lawyer shall not present, participate in presenting, or threaten to present criminal charges solely to obtain an advantage in a civil matter." *See also* ABA CANONS OF PROFESSIONAL ETHICS No. 7.