No. 14-400

IN THE

Supreme Court of the United States

CHARLES E. HARRIS, III,

Petitioner,

v.

MARY K. VIEGELAHN, CHAPTER 13 TRUSTEE,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court of Appeals For The Fifth Circuit

REPLY BRIEF FOR PETITIONER

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Respondent contends that the Fifth Circuit's decision is interlocutory, distinguishable, under-developed, and correct. It is none of the four.

1. The Fifth Circuit's decision finally and conclusively reversed the district court's final order. That order had affirmed the bankruptcy court's final order directing respondent to pay petitioner. There is nothing remotely "interlocutory" (Opp. 5) about the decision below. Nor does the Fifth Circuit's inclusion of boilerplate language indicating that, in addition to reversing, it was remanding "for further proceedings consistent with this opinion" (Pet. App. 28a) leave any doubt about the outcome on remand or undermine the finality of the Fifth Circuit's decision.[1]

2. Contrary to respondent's suggestion, this case is *not* distinguishable from the Third Circuit's decision in *In re Michael*, 699 F.3d 305 (2012). As the Fifth Circuit recognized, the Third Circuit "squarely answered" the purely legal question presented here and reached the opposite conclusion. Pet. App. 2a–3a & n.2.

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[1] Even in cases arising from the state courts, in which this Court's review is more closely circumscribed, a decision is "final and reviewable when it end[s] the litigation by fully determining the rights of the parties." *Dep't of Banking, State of Neb.* v. *Pink*, 317 U.S. 264, 267 (1942) (per curiam). Such finality occurs notwithstanding that a decision has been remanded for "the ministerial act of entering the judgment which the appellate court ha[s] directed." *Ibid.*

Respondent contends (Opp. 7–12), however, that a "significantly different" fact in the two cases makes all the difference: The plan and confirmation order in *Michael* re-vested the property of the estate in the debtor upon *plan confirmation* (699 F.3d at 309–10), whereas the plan and confirmation order in this case re-vested the property of the estate in petitioner upon his *conversion to Chapter 7* (Pet. App. 21a n.8). But that distinction has no bearing on the question presented here. Indeed, the Fifth Circuit expressly rejected respondent's "attempt[] to distinguish" the two cases on this basis. *Ibid.*

At bottom, the question in both cases is what should become of undistributed funds still held by the Chapter 13 trustee *after conversion* to Chapter 7. In this case—and in *Michael*—the "property of the estate" had re-vested in the debtor by the time, post-conversion, that the trustee disbursed funds to creditors. It is neither here nor there that the re-vesting happened *earlier* in *Michael* than it did in this case. What matters is that re-vesting happened in both cases before the trustee made the challenged distribution.

The Fifth and Third Circuits' disagreement about Section 1327(b) has nothing to do with that immaterial difference in timing. The Third Circuit held that the property of the estate that re-vests in a Chapter 13 debtor under Section 1327(b) *includes* post-petition wages that the debtor has paid to the trustee but that have not been distributed to creditors. *In re Michael*, 699 F.3d at 310. Regardless of when the re-vesting happens in a particular case, the Third Circuit concluded (*ibid.*) that the undistributed funds are "under the control of the

debtor on the date of conversion" for the purpose of determining the "property of the estate in the converted case" (11 U.S.C. § 348(f)(1)(A)). See also 699 F.3d at 313 ("Because § 1327(b) vests all property of the Chapter 13 estate in the debtor, including any post-petition property held by the Chapter 13 trustee *at the time of conversion* (such as funds transferred to the estate for eventual distribution to creditors), *on conversion* property of the Chapter 13 estate usually is 'under the control of the debtor.'") (emphasis added).

The Third Circuit's decision "ultimately turn-[ed]" (699 F.3d at 308), therefore, on Section 348(f)'s exclusion from the converted estate of post-petition property in the debtor's control "[e]xcept" where the conversion was done "in bad faith" (11 U.S.C. § 348(f)). "Overall," the court held, "a textual reading of § 348(f), particularly in light of its legislative history, leads us to conclude that undistributed plan payments held by a Chapter 13 trustee at the time of conversion must be returned to the debtor absent bad faith." *In re Michael*, 699 F.3d at 316.

The Fifth Circuit, by contrast, held that a debtor's payments to a trustee pursuant to a Chapter 13 plan *never* re-vest in a debtor under Section 1327(b)—not at confirmation, at conversion, or otherwise. Pet. App. 18a–21a. Section 1327(b)'s re-vesting applies "[e]xcept as otherwise provided in the plan or order confirming the plan," and the Fifth Circuit concluded that the Third Circuit "err[ed] by ignoring" this caveat. *Id.* at 19a. The Fifth Circuit held that payments a debtor makes to a Chapter 13 trustee pursuant to a confirmed plan are "otherwise

provided" for by the plan and confirmation order and "specifically divest[ed]" by the debtor. *Id.* at 19a–20a.

Those conflicting conclusions are agnostic as to *when* any re-vesting happens; the dispute is about *what* re-vests. Accordingly, the Fifth Circuit rejected respondent's "attempt[] to distinguish" *Michael* based on a difference in the timing of re-vesting. Pet. App. 21a n.8. In the Fifth Circuit's view of the law—in clear conflict with the Third Circuit's conclusion in *Michael*—"[b]y requiring [petitioner] to pay part of his wages to [respondent] for distribution to creditors, the [confirmation] order clearly did not contemplate that such payments would revest in [petitioner]." *Ibid.*

Tellingly, when respondent tries to defend the merits of the decision below, she is compelled to contend that "*Michael II*'s interpretation of 11 U.S.C. § 1327 * * * is incorrect" whereas "the court of appeals below was correct in its analysis of 11 U.S.C. § 1327(b)." Opp. 18. Even respondent ultimately cannot get around the acknowledged, clear division between the courts of appeals.[2]

3. Respondent does not dispute the Fifth Circuit's acknowledgement that this issue "has divided bankruptcy courts and district courts for 'thirty years.'" Opp. 11 (quoting Pet. App. 2a). Nor does respondent deny that the question presented

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[2] Similarly, respondent does not disagree that the Fifth Circuit's decision effectively conflicts with the Ninth Circuit's holding that undistributed funds must be returned to a debtor who converts from Chapter 12 to Chapter 7. Pet. 14 & n.2 (citing cases).

arises frequently in the "common circumstance" in which a Chapter 13 debtor converts to Chapter 7. *In re Michael*, 699 F.3d at 306; see also Pet. 28–30. Indeed, respondent does not deny that the post-conversion disposition of funds is a recurring and important issue in the roughly 60,000 annual conversions from Chapter 13 to Chapter 7. See Pet. 28–30. Those conversions operate in the shadow of this conflict, even if they do not necessarily result in litigated decisions.

In response to the pervasive confusion created by the patchwork of conflicting decisions in the lower courts, the Department of Justice, which has recognized that "[c]ourts are divided" on the question presented here, has instructed Chapter 13 trustees to "follow legal authority in the jurisdiction" in which each debtor's case is proceeding. U.S. Dep't of Justice, Exec. Office for U.S. Trustees, *Handbook for Chapter 13 Standing Trustees* 3-36 (Oct. 1, 2012). Delaying review would ensure only that perhaps tens of thousands of cases—directly affecting the lives and pocketbooks of thousands of real people—will be decided by the happenstance of where they reside. That is hardly the "uniform" rule of bankruptcy envisioned by the Constitution.

Respondent nevertheless contends that it would be "premature" for this Court to resolve the issue. Opp. 11. Respondent's principal complaint is that the Fifth Circuit cited "only" 20 lower-court decisions (split 12–8) addressing the issue. *Ibid.* According to respondent, those 20 decisions demonstrate an "infrequency of decisions" counseling against certiorari. *Ibid.* Not so. Twenty reported decisions, spanning three decades, are more than enough to

show that the issue routinely arises in converted cases and has been analyzed and re-analyzed by the lower courts.

What is more, respondent never addresses *petitioner's* cited decisions. See Pet. 17–18 nn. 3 & 4. Petitioner cited 25 lower-court decisions in which courts have squarely addressed (and disagreed over) the question presented. *Ibid.* In response to the Fifth Circuit's observation (Pet. App. 2a n.1) that some early decisions did not *expressly* resolve the ultimate disposition of funds that were not included in the converted Chapter 7 estate (doing so instead by implication), petitioner conservatively excluded such cases from his collected citations. If the Fifth Circuit's and petitioner's citations are combined, however, the result is a list of 32 decisions addressing the question presented that split 17–15. Likewise, by ignoring petitioner's citations entirely, respondent also ignores the five lower courts (excluding those in this case) that have decided the question presented in just the two years since the Third Circuit decided *Michael*. Those recent decisions likewise split 3–2. Pet. 18.

In short, more than enough ink has been spilled by the lower courts in trying—and failing—to resolve the legal issue presented for review in this case. Three decades of judicial consideration have left no stone unturned in analyzing this "pure question of law." *In re Michael*, 699 F.3d at 308. Nothing requires "further study" (Opp. 12) in the lower courts. And, as we explained in the petition (and respondent does not dispute), reported decisions are just the tip of a very large iceberg. The disputed sum in any given case—although incredibly meaningful to

the individual debtor who is seeking a fresh financial start—is routinely not large enough to justify bankruptcy-court litigation and three layers of appellate review. Pet. 18. This case thus provides an excellent vehicle to resolve a pure legal question that has long vexed the lower courts, but that debtors are rarely able to present for this Court's review.

4. Respondent devotes most of her brief to a misguided defense of the merits of the decision below. Indeed, her open embrace of the Fifth Circuit's most glaring error—*i.e.*, that court's conclusion that the statute should not be read "too literally"—only underscores the urgent need for this Court's review.

a. Respondent first argues that Section 348(f) allows a Chapter 13 trustee's payment of a debtor's undistributed wages to his creditors *after* he converts to Chapter 7 in good faith. Opp. 13–15. Section 348(f), however, provides that undistributed wages are off-limits to creditors post-conversion through the Chapter 7 estate, "[e]xcept" when a case has been converted in "bad faith." There is patent illogic to the Fifth Circuit's conclusion that those funds can nevertheless be paid out to the same creditors by the former Chapter 13 trustee even after a case has been converted *in good faith* (as it is undisputed happened here). See Pet. 19–21. "Except" means "except": there is no valid basis for courts to add exceptions to those expressly and exclusively identified by Congress in the text of a statute.

Therein lies the critical legal dispute between the Third and Fifth Circuits. In *Michael*, the Third Circuit held that "a textual reading of § 348(f), particularly in light of its legislative history, leads us

to conclude that undistributed plan payments held by a Chapter 13 trustee at the time of conversion must be returned to the debtor absent bad faith." 699 F.3d at 316. Its decision "ultimately turn[ed]" on that construction of Section 348(f). *Id.* at 308. The Fifth Circuit, by contrast, held that the Third Circuit's "argument fails to recognize" a competing understanding of Section 348(f). Pet. App. 21a. Tellingly, however, respondent does not actually defend the flawed "non-superfluity" reasoning on which the Fifth Circuit rejected the Third Circuit's reading of the statute. See Pet. 20–21 (citing Pet. App. 21a–22a).

b. Respondent (Opp. 15), like the Fifth Circuit (Pet. App. 10a), asks this Court not to take "too literally" Section 348(e)'s text, which terminates a Chapter 13 trustee's services upon conversion. But, as the Third Circuit recognized in *Michael* (699 F.3d at 310), Section 348(e) must be afforded its plain and ordinary meaning—as "literally" as possible. As the Third Circuit explained, when Section 348(e) "terminates the services" of the Chapter 13 trustee upon conversion, it "renders [the trustee] powerless to make payments to creditors under a Chapter 13 plan." *Ibid.*; see also Pet. 21–22.

In the Fifth Circuit's view, paying undistributed funds to creditors as though the Chapter 13 plan were still in force is simply part of the trustee's obligation to "wind[] up" the Chapter 13 estate. Opp. 17. That is a bridge too far. A Chapter 13 trustee's post-conversion ancillary duties are specific and narrow. See Federal Rule of Bankruptcy Procedure 1019(4) (requiring turnover of records and property of the estate to the Chapter 7 trustee), 1019(5)

(requiring a final report and schedule of post-petition debts). If Section 348(e) "terminates" the trustee's ability to do anything, then certainly it must terminate her authority to continue disbursing funds to a debtor's Chapter 13 creditors.

c. Respondent takes issue with our identification of two ways in which the Third Circuit's interpretation of Section 1327(b) is more consistent with other Code provisions than the Fifth Circuit's. See Pet. 23–24. The first way is that a trustee must refund undistributed funds to a debtor who converts his case *before* plan confirmation. 11 U.S.C. § 1326(a)(2). It stands to reason that Congress intended the same rule to apply in cases converted *after* plan confirmation. See Pet. 23. Respondent provides no justification for the Fifth Circuit's inconsistent treatment of the two scenarios; she simply (and non-responsively) observes that this case does not involve a pre-confirmation conversion. Opp. 19.

The second way the Third Circuit's rule aligns with other Bankruptcy Code provisions is that a case *converted* after confirmation should not be treated differently from a case *dismissed* after confirmation. See Pet. 23–24 (citing 11 U.S.C. § 349(b)(3)). As the Third and Ninth Circuits have concluded, it "elevate[s] form over substance" to hold otherwise. *In re Michael*, 699 F.3d at 313 n.6; *Arkison* v. *Plata (In re Plata)*, 958 F.2d 918, 922 (9th Cir. 1992). Respondent claims that this comparison "ignores" the dismissal statute's "exception" for cases where a court finds "cause" not to return property of the estate to the debtor upon dismissal. Opp. 20–21 & n.6. But that "exception" merely confirms the validity

of petitioner's comparison: to disburse undistributed funds to creditors after conversion or dismissal, a trustee must show "bad faith" or "cause," respectively. Compare 11 U.S.C. § 348(f) (conversion) with *id.* § 349(b) (dismissal). In the absence of such a showing, the default rule should be the same: the undistributed funds are refunded to the debtor.

d. Finally, Respondent disputes (without success) that the decision below, if permitted to stand, would create perverse incentives for debtors and negative consequences for creditors. For debtors already proceeding in Chapter 13, however, the Fifth Circuit's rule compels them to convert out of Chapter 13 quickly once their circumstances have changed. Pet. 26–27. Respondent purports to disagree, but provides no basis for her disagreement. Opp. 21–22. As for a debtor considering a Chapter 13 proceeding in which success is unsure, he must consider any risk that post-petition wages that would be off-limits to his creditors in Chapter 7 would still be disbursed to those creditors even after Chapter 13 has proven unsuccessful. Pet. 27–28. That risk, which the decision below creates, favors proceeding in Chapter 7 in the first instance. Respondent argues that no disincentives are established because Chapter 13 debtors are just "honor[ing] their obligation[s]" if such post-conversion distributions are allowed to occur, but that merely begs the question. Opp. 22–23.

Respondent also mistakenly contends that debtors such as petitioner would receive a "windfall" if they were to recover post-petition wages undistributed at conversion. Opp. 22–25. Such rhetoric is not premised on fact. In this case, for example, respondent held funds at conversion

because the plan required her to withhold payments earmarked for petitioner's mortgagor once it received relief from the stay to foreclose on petitioner's home. If petitioner's unsecured creditors had believed they were entitled to those funds *during* the proceedings, they could have moved to modify the plan. See 11 U.S.C. § 1329. No creditor did so. The notion that those creditors are nevertheless entitled to funds post-conversion as a *quid pro quo* is unfounded.[3]

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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[3] Respondent relies (Opp. 23) on the purported "Congressional intent behind the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA)." That statute, however, made no relevant change to Section 348, and respondent points to no other BAPCPA provision that relates to the question presented.