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Bruce A. Markell

Indiana University School of Law

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Conspiracy, Literalism, and

An examination of bankruptcy cases decided from 1990 to 1993.

By Bruce A. Markell*

During the 1980s, bankruptcy cases accounted for approximately one percent of the Supreme Court's docket, or an average of one or two cases a year. In the three terms beginning with the October term of 1990, however, the Court accepted an average of six bankruptcy cases per year, boosting its average annual percentage of bankruptcy fare to approximately five percent.¹

*Bruce A. Markell is an associate professor of law at Indiana University-Bloomington. He is a contributing editor for *Bankruptcy Briefs*, the newsletter of the FBA's Bankruptcy Law Section. In that capacity, he regularly writes a column on the Supreme Court's bankruptcy opinions from which portions of this article were taken. Mr. Markell is a graduate of Pitzer College and the King Hall School of Law at the University of California, Davis, where he was editor-in-chief of the law review. He clerked for Judge (now Justice) Anthony Kennedy, then of the Ninth Circuit Court of Appeals. Before becoming a law professor, Mr. Markell was a partner with the Los Angeles office of Sidley & Austin, where he practiced bankruptcy law. The author would like to thank Douglass Boshkoff and Leah Lorber, each of whom read and gave helpful comments on earlier versions of this article. Errors which remain are the author's alone. © 1994, Bruce A. Markell.

Why? In this article, I will examine the eighteen cases decided from 1991 through 1993, to determine if there is a consistent thread linking them.² Although such synthesis is what articles like this are about, I warn the reader early: I have no definitive answers. At best I can provide only working hypotheses for future writers. And it is to that task that I now turn.

October Term 1990

The first term, 1990-91, produced six bankruptcy-related decisions. The first two, *Langenkamp v. Culp* and *Grogan v. Garner*, stand for simple propositions. *Langenkamp* holds that a creditor loses whatever right to jury trial it has with respect to preference actions if it files a proof of claim. *Grogan* deals with dischargeability issues; it holds that collateral estoppel (issue preclusion) applies in fraud dischargeability cases, and that the quantum of proof in such cases is a preponderance of the evidence. Although both decisions

can be reduced to simple holdings, each has broad implications for other similar cases.

Langenkamp's facts were straightforward. Consumers invested funds with the debtors, who were uninsured, non-bank financial companies. The debtors, in turn, issued "passbook savings certificates," representing the debtors' obligation to repay money invested. Within ninety days prior to their bankruptcy filing, the debtors paid some, but not all, of the funds owed to the consumers. After the debtors' bankruptcy filing, the consumers filed proofs of claim with respect to the unpaid amounts. The trustee responded with a suit to recover the amounts paid as preferences.

After a bench trial, the trustee prevailed. The district court affirmed, but the Tenth Circuit reversed. It believed that the consumers had a jury trial right on the preference issues. The Supreme Court reversed the Tenth Circuit in an 8-0 *per curiam* opinion, holding that the consumers were not entitled to a jury trial.

Ennui at the Supreme Court

The Court held that when a creditor files a proof of claim, it initiates a process "integral to the restructuring of the debtor-creditor relationship through the bankruptcy court's equity jurisdiction."³ Subsequent preference actions against that creditor are thus viewed as ancillary to that "restructuring."

The same preference action, however, filed without the benefit of a creditor's proof of claim, is "a legal action to recover a monetary transfer." In that case, apparently, the creditor has a jury trial right.

This mode of analysis is hauntingly anachronistic, harkening back to the days of summary or plenary jurisdiction based upon actual or implied consent. One result of *Langenkamp* is a schizophrenic treatment of preference actions: the preference defendant, through its decision to file a proof of claim, now controls where the action will be tried and who will hear it.

And if a creditor does not receive sound legal advice before filing its proof of claim or taking some other action in bankruptcy court? Jurisdiction by ambush is back.⁴

Grogan is less problematic. The Court there addressed a split in the circuits over the proper quantum of proof in fraud dischargeability cases. Some insisted that preponderance of the evidence governed; others required proof by clear and convincing evidence. The Supreme Court aligned with the former: creditors need only prove their cases by a preponderance of the evidence.

Grogan will have its greatest effect on those cases in which a tenacious creditor obtains a state court fraud

judgment. *Grogan* gives that judgment collateral estoppel (claim preclusive) effect. Previously, debtors could lose in state court, file bankruptcy, and restart the litigation. The morally pliable took full advantage of this fact. No more. As stated by the Court, "collateral estoppel principles do indeed apply in discharge exception proceedings pursuant to § 523(a)."⁵ Each debtor wishing to extend litigation must now file his or her bankruptcy petition before the state court enters a final judgment.

The Court preserved, however, important distinctions between collateral estoppel and *res judicata*. A state court fraud judgment does not, of itself, bar the debtor from contesting dischargeability. It only bars the debtor from relitigating issues actually, necessarily, and finally litigated in the state court action. Thus, default judgments are still suspect, as are any other actions not accorded collateral estoppel effect by courts in the state where the judgment is issued.⁶

The Court also held in limbo the effect of punitive damages. In a footnote, the Court stated that it did not consider whether 11 U.S.C. § 523(a)(2)(A) extends to noncompensatory damages, although it indicated that these also might be non-dischargeable under section 523(a)(6), as debts caused by the debtor's willful and malicious acts.⁷

The Court's next two cases involved the murky intersection of family law and bankruptcy. The two cases, *Farrey v. Sanderfoot* and *Owen v. Owen*, were both decided on the same day, and both cases involved the same core facts. Under property settlements in divorces, the debtors received the marital house. The divorce decrees,

however, encumbered each house with a lien securing the debtor's obligation to pay the other spouse sums necessary to make the overall property settlements equitable. Unable or unwilling to raise the cash necessary to satisfy these secured obligations, the debtors filed bankruptcy, and claimed homestead exemptions in their houses.

In both cases, the homestead exemption was affected by the ex-spouse's judicial lien from the divorce proceedings. Both debtors attempted to set aside these judicial liens through the use of section 522(f). Section 522(f) allows a debtor to avoid "the fixing of a [judicial] lien on an interest of the debtor in property to the extent that such lien impairs an exemption to which the debtor would have been entitled . . ."

The key case is *Farrey*. There, the Court held that section 522(f) could only be used to avoid the "fixing" of a lien which attached after the debtor had acquired the interest. According to the Court, grammar dictated this result: "[t]he gerund 'fixing' refers to a temporal event. That event—the fastening of a liability—presupposes an object onto which the liability can fasten."⁸

Questions as to when interests are acquired or as to when liens attach are determined by state law. In *Farrey*, the debtor gave away his case on this point by admitting that, under Wisconsin law (which is the same as the Uniform Marital Property Act), the divorce decree had the effect of extinguishing all prior interests in the marital property and creating new ones in their places. The Court believed that the debtor's admission

meant that, under state law, he never possessed the house free of the judicial lien. Or, using section 522(f)'s language, the debtor never had an interest in property prior to the time the judicial lien fixed.

As Justices Kennedy and Souter pointed out in a concurring opinion, this reasoning allows vagaries of state law to produce different results on the same facts.⁹ For example, if a debtor is a tenant in common prior to divorce, and the divorce decree simply transfers the other half interest to him, there could be an argument that the pre-existing tenancy in common was impaired by the judicial lien. The majority, in *dicta*, seems to dismiss this possibility, stating that the same result would obtain if state law did not extinguish interests in divorces, but merely "re-ordered them."¹⁰ Justice Scalia declined to join the majority opinion on this point.¹¹ Look for further litigation.

In *Owen*, timing was everything. Owen owed his spouse \$350,000 under a divorce decree. After the decree was entered, he purchased a condominium; under controlling Florida law, the divorce decree created a judicial lien on any real property acquired. At the time of the purchase, however, state law did not grant the debtor a homestead exemption. State law changed after the lien attached, but before the debtor filed for bankruptcy protection.

In bankruptcy, the debtor attempted to use section 522(f) to avoid the judicial lien on the condominium. The non-debtor prevailed below, arguing that because Florida law would not allow the debtor to use the exemption against her, neither should bankruptcy law.

The Court began with an analysis of section 522(f). That section allows the avoidance of judicial liens to the extent that such liens "impair[] an exemption to which the debtor would have been entitled under subsection (b)" The Court then acknowledged two possible readings of the required impairment: from the viewpoint of the debtor in a state collection proceeding absent bank-

ruptcy, when the lack of equity in encumbered property would mean there was nothing to protect; or, from a position in which the lien at issue would be avoided regardless of whether the debtor, outside of bankruptcy, would have any equity in the property. The Court adopted the latter reading.

The Court felt that the consistent construction of section 522(d)'s exemptions required this result. Those exemptions speak to only the debtor's interest.¹² If impairment were assessed as if the liens were valid against the debtor outside of bankruptcy, many times there would be no interest of the debtor left. To give section 522(f) independent vitality, the Court stated that the hypothetical language in section 522(f) is to be read as testing impairment without the lien at issue, regardless of whether that result would be permitted by state law.

The Court, however, could go no further. Unlike *Farrey*, the debtor had not conceded that he acquired the property subject to the ex-spouse's interest. The Court thus remanded the matter for a determination of Florida law on this point.¹³ The Court also suggested that the non-debtor could raise a constitutional takings issue on remand if, under state law, her lien attached subsequently to the debtor's acquisition of the condominium.

Farrey and *Owen* signal that the Court is prepared to defer significantly to secured creditors. Both are full of language stating that the secured creditor's "equitable" interest does not become property of the estate, and that, in many cases, the debtor possesses "only bare legal title." Recall, however, that both cases deal with involuntary judicial liens. Neither would have arisen had the disgruntled spouses obtained consensual liens during the course of the divorce proceedings. Against this background, one wonders about the appropriateness of this degree of deference when the Court is asked to construe the lien restructuring provisions of Chapters 11 and 13, or the sale free and clear provisions of section 363(f).

The Court closed October Term 1990 with two easy cases: *Johnson v. Home State Bank* and *Toibb v. Radloff*. In *Johnson*, the Court declined to construe the definition of "claim" found in 11 U.S.C. § 101(5) narrowly to halt serial bankruptcy filings; in *Toibb*, the Court declined to limit Chapter 11 to businesses.

Johnson involved a farmer who had filed a Chapter 7 case to discharge his liability for a deficiency on an under-collateralized loan. After the discharge, the bank sought to foreclose on its remaining lien. In response, the farmer filed a Chapter 13 case. His plan, which was confirmed, called for four easy annual payments, with a balloon payment of the balance at the end of the four year plan. The bank cried foul, and the Tenth Circuit held in its favor, holding that the remaining liability on the mortgage was not a claim capable of a Chapter 13 restructure.

The Court made fast work of the bank's claim. Both the definition of claim and the Code's interpretive provisions (section 101(2)) clearly anticipate that nonrecourse liability such as that at issue is a "claim." The Court even trotted out some impressive legislative history and substantive context to support its point. It concluded by stating that if Congress wanted to discourage serial filings, there were better and more straightforward ways of doing it.

In *Toibb*, the debtor had filed a Chapter 7 petition. Soon thereafter, he discovered that some stock he held was more valuable than he had thought. He then moved to convert his case to a Chapter 11, and filed a plan of reorganization. The bankruptcy court never considered the plan, dismissing the case on the grounds that *Toibb*, an individual not engaged in business, was not eligible for protection under Chapter 11. The district court and the court of appeals affirmed.

The Supreme Court reversed. In an 8-1 decision by Justice Blackmun, the Court held that nothing in section 109 excludes consumer debtors from

eligibility under Chapter 11. Indeed, the plain language of section 109 states that “[o]nly a person that may be a debtor under Chapter 7 . . . may be a debtor under Chapter 11” Because Toibb clearly qualified as a Chapter 7 debtor, the Court had no difficulty extending Chapter 11’s protection to him.

The pre-decision procedural wrangling signalled the outcome. The “Radloff” of the case name was Toibb’s Chapter 7 trustee; he declined to respond at any stage of the proceedings. The Court then asked the office of the United States Trustee to respond and defend the dismissal. It also declined, stating that it believed Toibb to be right. The Court had to take the unusual step of asking a private lawyer to appear *amicus curiae* to defend the judgment.

The opinion itself is sparse, and does not cite much authority beyond the Code and some legislative history. The Court dismissed arguments based upon the structure of Chapter 11 and on the policy of not subjecting consumers to involuntary proceedings with its plain language argument. Only Justice Stevens in dissent thought these arguments mattered.

The Court is probably right in its guess that *Toibb* will not cause a flood of consumer Chapter 11 cases. Chapter 11 is procedurally complex and costly, making it unwieldy for all but a few consumers. Moreover, as the Court notes, the bankruptcy court has sufficient discretion under section 1112(b) to act as a gatekeeper for appropriate Chapter 11 candidates. With all the other issues floating around in the bankruptcy courts, one wonders why this case was taken, or why it did not result in a *per curiam* reversal.

The most surprising omission from the list of cases to be heard during the 1990-91 term was *Insurance Co. of Pa. v. Ben Cooper Inc.*¹⁴ At the beginning of the term, the Court had granted *certiorari* in this case to determine the ability of a bankruptcy court to hold a jury trial on a post-petition claim. After *certiorari* had been granted, the solicitor general suggested a lack of appellate

jurisdiction, and the Court remanded to the Second Circuit. On remand, that court found that jurisdiction was present. When *certiorari* was requested after remand, the Court declined to hear the matter. This leaves a split among the circuits as to the issue raised.

October Term 1991

The Court’s bankruptcy docket in October Term 1991-92 was an all-time high of nine cases. But the decisions offer thin gruel for the bankruptcy practitioner. They seem to concentrate more on a policy of good grammar than on good bankruptcy policy; the reported decisions seem to require both the Code and an English language handbook.

Board of Governors of the Federal Reserve System v. MCorp. Financial, Inc., dealt with the intersection of federal banking regulations and the automatic stay of section 362 of the Code. In *MCorp.*, a Chapter 11 bank holding company debtor sought to enjoin the Federal Reserve Board from prosecuting administrative actions against it under the Board’s source of strength powers. These powers grant the Board the authority to order bank holding companies, such as *MCorp.*, to improve the bank’s financial position. *MCorp.* argued that these powers did not apply to it so long as it was protected by the automatic stay; its theory was that there was no practical difference between the type of result sought in the administrative proceeding and the result of a lawsuit seeking a money judgment. Both would require the debtor to pay money for the benefit of pre-petition creditors.

The Court ruled against *MCorp.*, and held that the administrative proceeding could continue. It first noted that the Financial Institutions Supervisory Act, applicable to the Board’s actions, contains an anti-injunction provision that was not specifically mentioned in section 362, the assumption being that only if such cross-reference had been made could

MCorp.’s argument have succeeded. Next, the Court noted that section 362(b)(4) expressly exempts proceedings to enforce a “governmental unit’s police or regulatory power” from the stay. Although regulatory proceedings are exempt, collection actions based upon those proceedings are not. The Court, however, noted that collection from the debtor’s estate was not at issue, because there was not yet a final order demanding money. “[I]f and when the Board’s proceedings culminate in a final order, and if and when judicial proceedings are commenced to enforce such an order, then it may well be proper for the Bankruptcy Court to exercise its concurrent jurisdiction.”

MCorp.’s main effect will be outside the banking regulatory area. Government agencies charged with protecting the environment will find much in this opinion to support their authority to continue to conduct extensive investigations of a debtor’s activities, in spite of the automatic stay. The opinion also may reinforce the investigatory muscle of state and federal securities agencies. Whether this is a good development will turn on the nature of the regulatory scheme. The Court’s opinion is consistent with the notion of regulate first, collect later. But what happens if a debtor declines, due to the press of the business of reorganizing, to participate in the agency’s action? Will it lose rights to contest the agency’s findings and conclusions? The Court’s opinion does not acknowledge this factor, nor does it note any difference between regulatory investigations of post-petition conditions and inquiries regarding pre-petition behavior.

Union Bank v. Wolas presents a more traditional bankruptcy issue. There, a debtor had paid a loan commitment fee and two interest payments on long-term debt within the ninety-day preference period of section 547 of the Code. The trustee sought to recover these payments as a preference, and the lender defended on the basis that the payments were protected by section 547(c)(2), which provides a

defense for transfers made in the ordinary course of business.

The trustee argued that section 547(c)(2) applied only to transfers in respect of short-term debt and trade debt. His contention was met with derision. The Court flatly stated that “the [statutory] text provides no support for respondent’s contention”¹⁵ Justice Scalia added, in a separate concurrence: “[i]t is regrettable that we have a legal culture in which such arguments have to be addressed . . . with respect to a statute utterly devoid of language that could remotely be thought to distinguish between long-term and short-term debt.”¹⁶

The Court correctly left open the question as to whether the bank had established the elements of the preference exception. Thus, on remand, open questions remain as to whether the loan was in the ordinary course of the debtor’s and the bank’s businesses, and whether the payments were made in the ordinary course and according to ordinary business terms.¹⁷ In short, all the Court did was to shift the analysis to a case by case situation. Counsel to lenders now are left with questions to answer regarding when a debtor can incur long-term debt in the ordinary course of its business. Can first-time loans ever qualify? Can loans for new expansion? The case may signal yet another reason that lenders will demand full security for any extension of credit.

Dewsnup v. Timm deals with a significant issue by conducting a grammatical and syntactical examination of section 506 of the Code. Ms. Dewsnup held property worth \$39,000 subject to a \$120,000 mortgage. After filing for protection under Chapter 7, she commenced an adversary proceeding seeking to invalidate the lien. Her statutory basis was section 506(d), which provides for avoiding a lien “to the extent that [it] secures a claim against the debtor that is not an allowed secured claim.”

Her argument was that under section 506(a), the allowed secured claim was only \$39,000, and thus the balance was disallowed, and could be “stripped”

away under section 506(d). The effect of such a ruling would be to allow Dewsnup to transform a recourse loan into a non-recourse loan simply by filing bankruptcy; if successful, her personal liability for the \$120,000 would be discharged, and she could redeem the property for \$39,000.

After *Union Bank*, it would seem surprising that the Court would construe the same words “allowed secured claim” differently in section 506(a) and in section 506(d). But it did. To reconcile the cases, the Court first found an ambiguity in usage of the “allowed secured claim” term, and then adopted what it believed to be the “better” construction. Lien stripping is not permitted.

Justice Scalia, joined by Justice Souter, did not permit the inconsistencies between *Dewsnup* and *Union Bank* to go unnoticed.¹⁸ In a long dissent, Justice Scalia deconstructed each of the Court’s attempts to find ambiguity. More interesting, however, is his concluding paragraph. After acknowledging that the Court’s result is “probably fairer from the standpoint of natural justice,” he points out that this observation is irrelevant, because “bankruptcy law has little to do with natural justice.”¹⁹ This comment, together with the Justice’s somewhat brittle view on statutory construction, does not bode well for debtors’ lawyers. After all, what section of the Code clearly states the “fresh start” purpose, and what section grants bankruptcy judges flexibility in reorganizing complex businesses?

In *United States v. Nordic Village, Inc.*, statutory construction achieved a new nadir. In that case, an officer of a debtor-in-possession dipped into estate funds and paid a personal tax obligation. When a trustee later was appointed, he sued the government as a transferee of an unauthorized transfer under section 549 of the Code. The government asserted sovereign immunity.

Justice Scalia upheld the government’s position. He read section 106 of the Code as providing for a waiver of sovereign immunity only in cases of

compulsory counterclaims and permissive counterclaims (capped at the amount of the government’s claim). Section 106(c) provides that “notwithstanding any assertion of sovereign immunity . . . a provision of this title that contains . . . ‘entity’ . . . applies to governmental units; and . . . a determination by the court of an issue arising under such a provision binds governmental units.” Here, section 550 allows recovery from any “entity” receiving a transfer voidable under section 549.

Justice Scalia, however, invoking past case law, found the construction chosen by Congress to be ambiguous, and not an “unequivocal expression” of waiver. He also followed his practice of not considering legislative history.

As a consequence, the government may now defend any avoiding powers action with a claim of sovereign immunity. Preferences, fraudulent transfers, and other benefits received are immune. The oddity here is that Congress has never expressly adopted sovereign immunity; it is judicially created law, albeit with a long pedigree. Thus, to strictly construe sovereign immunity against a judge-made standard deprives the opinion of much of its analytical force.

Another cipher of an opinion is *Holywell Corp. v. Smith*. There, a liquidating trustee of five Chapter 11 debtors (four corporations and one individual) failed to file tax returns related to income from estate property after confirmation of the plans. The court painstakingly parsed the provisions of the Internal Revenue Code and found that the trustee had a duty to file. The Court also rejected claims that provisions of the Chapter 11 plan which exempted the trustee from filing duties were binding on the government because it was not a “creditor,” bound under section 1141, as the obligations at issue in *Holywell* arose post-confirmation, and “creditor,” as defined by section 101(10), only applies to entities whose obligations arise pre-petition.

The Court picked up where it left off after *Dewsnup* with *Connecticut Nat’l*


Bank v. Germain. In *Connecticut Nat'l Bank*, the bankruptcy court had refused to strike a trustee's demand for a jury trial in a removed adversary proceeding. The creditor appealed to the district court and lost, and then attempted to appeal to the Second Circuit. For jurisdiction, the creditor relied upon 28 U.S.C. § 1292(b), the general federal jurisdiction statute for appeals from district court interlocutory orders, which normally applies to decisions of the district court sitting as a trial court, not, as here, as an appellate court.

The Second Circuit disagreed. It reasoned that 28 U.S.C. § 158(d) deprived it of jurisdiction over orders such as the one before it. Section 158(d), enacted with specific reference to bankruptcy matters in 1984, does not negate jurisdiction explicitly. With respect to orders entered by district courts sitting as appellate courts, however, it only grants jurisdiction to the court of appeals to hear final orders.

The Supreme Court disagreed with the Second Circuit. It held that 28 U.S.C. § 1292(b) gave the courts of appeals jurisdiction. As a result, litigants have a new avenue to seek review of interlocutory orders, which type comprise most of the orders issued in a bankruptcy case.

As to this holding, all justices agreed; not one dissented. Four members of the Court (Justices Stevens, O'Connor, White, and Blackmun), however, saw fit to concur on the topic of the use of legislative history. As noted by Justice O'Connor, the interpretation adopted by the Court "render[s] § 158(d) largely superfluous."²⁰ This reading, she and Justice Stevens thought, at least obligates the Court to explain what it is doing, and resorting to legislative history would be appropriate for this task.²¹

The majority, however, are not believers in the utility of legislative history. The opinion, written by Justice Thomas, states the issue quite simply: "[w]e have stated time and again that courts must presume that a legislature says in a statute what it means and means in a statute what it says



I offer the following for conspiracy buffs. The Court is using bankruptcy cases to build an impressive (at least in numbers) body of precedent to apply to some tough statutory cases it knows are coming, such as the Americans with Disabilities Act, the Civil Rights Act of 1991, or even President Clinton's federal health care plan. . . . In short, the Court is sacrificing a coherent bankruptcy policy to thwart expansive interpretation of congressional efforts in the social policy arena.

there. . . . When the words of a statute are unambiguous, then, this first canon is also the last: 'judicial inquiry is complete.'²²

Whew. Such a statement is as striking in its simplicity as it is broad in its application. And such statements should make all interpretation of the Bankruptcy Code a piece of cake. Take, for example, the pre-petition satisfaction of an unsecured debt with a check. What is the date of transfer? The Code, in section 101(54), states that a transfer "means every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property. . . ."²³ Given the breadth of this section, doesn't a transfer occur when a creditor delivers its check? After all, the delivery of the check suspends the creditor's right to sue on the underlying debt until the check is dishonored.²⁴

The Supreme Court disagrees. In *Barnhill v. Johnson*, Chief Justice Rehnquist held that a transfer occurs, for preference purposes, on the date that the debtor's bank honors the check. This decision seems at odds with *Connecticut Nat'l Bank*. After all, the definition of "transfer" does not appear ambiguous; on the contrary, it is incredibly expansive. The Court, however, held that no transfer of a property interest occurs until honor. In addition to the debtor's order for the bank to pay, the bank must honor that order. This seems odd; most of us write checks for deductible expenses at year end, post them by December 31st, and then take deductions relating to those checks for the year in which they were posted. As Justice Stevens stated in dissent, the statute speaks of "modes" of transferring property interests, and "[a] check is obviously a 'mode' through which the debtor may 'par[t] with property.'²⁵

Regardless, the Court has spoken. Start calculating preference periods from the date that the bank honors the check.

Taylor v. Freeland & Kronz is more consistent with Justice Thomas' analysis in *Connecticut Nat'l Bank*. *Taylor* involved section 522(1) of the Code,

which deals with exemption claims by debtors. Section 522(1) requires the debtor to file a statement of claimed exemptions. It then provides that "[u]nless a party in interest objects, the property claimed as exempt on such list is exempt." Bankruptcy Rule 4003(b) then gives parties in interest thirty days after the first meeting of creditors to object.

Before *Taylor*, some courts read section 522(1) to include a good faith exception; creditors had unlimited time to object if the debtor did not have a good faith basis for the claimed exemption. In *Taylor*, the debtor had listed the full amount of any recovery in a pending lawsuit as exempt; no more than a minuscule amount could legitimately be claimed. When the debtor received a favorable settlement (apparently somewhat unexpectedly) and received more than enough funds to pay all creditors in full, the trustee sued the debtor's law firm, which had acted as an escrow for the settlement proceeds of the lawsuit.

The Court, again speaking through Justice Thomas, ruled for the law firm. Because the statute does not mention good faith, and the trustee did not object within the thirty days provided by Bankruptcy Rule 4003(b), "[s]ection 522(1), therefore, ha[d] made the property exempt." Interestingly, Justice Thomas cited absolutely no authority for his reading of the statute, not even *Connecticut Nat'l Bank*. The fallout from the decision is distressingly predictable: increased activity from trustees seeking blanket extensions of Rule 4003(b)'s thirty-day limit.

The Court closed out its term with an examination of the murky intersection of pension law and bankruptcy. In *Patterson v. Shumate*, the lower court had ruled that an ERISA-qualified pension did not become property of the debtor's bankruptcy estate. It relied upon section 541(c)(2), which excludes assets not generally available to creditors under "applicable non-bankruptcy law," such as spendthrift trusts. Because all ERISA plans must

have the type of anti-alienation clause the lower court found determinative, other courts of appeals had held that section 541(c)(2)'s reference to applicable non-bankruptcy law had to be a reference to state law only. Thus, the circuits were split.

The Court resolved the split by finding that ERISA is "applicable non-bankruptcy law," just as is any other federal statute not found in Title 11. ERISA-qualified pension plans are thus not property of a debtor's estate, and may not be liquidated in a bankruptcy proceeding to pay the debtor's debts.

The Court, in an opinion by Justice Blackmun, used *Toibb* as its standard for statutory interpretation. Although some of section 541's legislative history suggests that Congress intended to exclude only state-law spendthrift trusts, Justice Blackmun found that "the clarity of the statutory language at issue in this case obviate[d] the need" to consult that history.²⁶ He buttressed this conclusion by citing *Butner v. United States*²⁷ for the broad proposition that "the treatment of pension benefits will not vary based on the beneficiary's bankruptcy status."

All nine justices agreed with this result. Justice Scalia, however, could not help but comment on the court's method of statutory interpretation. After dismissing the issue in *Shumate* as elementary, he noted that the Court would not have had to decide the case but for the Court's prior waffling on the proper method of statutory interpretation. As he saw it, "the phenomenon [of raising far-fetched interpretations of seemingly unambiguous text] calls into question whether our legal culture has so far departed from attention to text, or is so lacking in agreed-upon methodology for creating and interpreting text, that it any longer makes sense to talk of a 'government of laws, not of men.' . . . I trust that in our search for a neutral and rational interpretive methodology we have now come to rest, so that the symbol of our profession may remain the scales, not the see-saw."²⁸

After nine bankruptcy cases, the Court took a rest in 1992-93. The cases it did accept, however, did have more substance. Its first opinion in October Term 1992 was *Pioneer Inv. Serv. Co. v. Brunswick Assoc. Ltd. Ptnshp.* At issue in *Pioneer* was what conduct is "excusable" in filing a late proof of claim. In the case below, the Sixth Circuit had taken the factors listed in *In re Dix*²⁹ as non-binding guides to interpretation, rather than as an exhaustive list of criteria. A split in the circuits was thus claimed to exist.

The petitioners in *Pioneer* were creditors of the Chapter 11 debtor, and some of them were on the debtor's creditors' committee. Each of them had apparently been assured by their counsel not to worry about filing their proofs of claim on time. Their counsel, however, had neglected to read fully the "Notice for Meeting of Creditors," which, uncharacteristically for a Chapter 11 case, had set forth a bar date. The court below had found that the debtor had suffered no prejudice by the late filings, which were accomplished within three weeks of the bar date.

The Court here focused on the apparent lack of prejudice to the debtor, or the novelty of combining a section 341(a) notice with notice of a bar date in a Chapter 11 case. (There is no statutory requirement, or requirement in the Bankruptcy Rules, as to when the bar date must be set in a Chapter 11 case.) This was not accomplished, however, without some grammatical wrangling over whether "excusable neglect" was two concepts, neglect and excuse, or just one.

The Court closed the 1992-1993 term with two Chapter 13 cases. Both involved the permissible treatment of secured creditors in Chapter 13. *Nobelman v. American Savings Bank* dealt with section 1322(b)(2) of the Code. That section takes loans "secured only by a security interest in real property that is the debtor's principal resi-

dence" out of the broad modification powers otherwise contained in section 1322. The issue was one presaged in *Dewsnup*: if a loan is undersecured, does 1322(b)(2) apply only to the secured claim, as defined by section 506(b), or does it apply to the entire loan? After the result in *Dewsnup*, the Court's resolution should not seem strange. Justice Thomas held that section 1322(b)(2) applies to the whole loan, regardless of how section 506(b) might split it up for other reasons.

His reasoning on this point borders on the novel. After reaffirming that bankruptcy was not intended to disturb property interests such as liens, he interprets the language of section 1322(b) to apply, not to the "claims"—which would be the province of section 506(b)—but to the "rights" of a secured creditor.³⁰ As the Court put it, section 1322(b)(2) puts the focus on the "rights" of the holders of claims in bankruptcy. Because "rights," as such, are not defined in the Code, he investigates state law to determine what rights the secured creditor held and, not surprisingly, found that one such right included the ability not to have the mortgage lien bifurcated.

The "rights" analysis is bound to give rise to new claims by secured parties. One of the purposes of sections such as 1322 and 1129 is to modify the rights that secured creditors have under non-bankruptcy law. To focus on the survival of such "rights" is bound to lead to odd arguments about what "modify" means, especially if the Court is committed to not modifying state law "rights."

Rake v. Wade rounds out the survey. There, an oversecured creditor failed to provide for post-default interest in its documentation, providing only for a five dollar charge for late payments. When the debtor filed for protection under Chapter 13 and attempted to cure and reinstate the loan, the lender claimed that post-petition, pre-cure interest, as well as post-confirmation interest, was a component of reinstatement. Because there was no entitlement to such interest in the

original loan documents, the Court had to look to bankruptcy law to fill the gap.

The Court filled the gap with section 506(b), which it held required payment of interest on the arrearages. It rejected the debtor's argument that a "cure" eliminated a default and placed the creditor where it would have been under state law. "[N]othing in [section 1322(b)(5)] dictates the terms of the cure." Because payment of interest could be part of a cure, and because the Court was loathe to ignore Section 506(b), it required the payment of interest.

Part of the weakness of *Rake* is that it leaves open the issue as to what is the effective rate of interest; at least if an effective rate was provided by state law, there would be some certainty. Almost immediately after the *Rake* opinion was issued, Congress amended the pending bankruptcy reform legislation to overrule *Rake*.³¹ Until such legislation is passed, however, the payment of interest will be part of any Chapter 13 cure and reinstatement.

Possible Explanations

I would like to explain that the Court increased its bankruptcy docket because it has realized the importance of a sound, consistent bankruptcy law to the nation's economy, or that it found that the consideration of bankruptcy issues presented a unique blend of intellectual rigor, pragmatism, and policy. However, I cannot and remain honest. Rather than eighteen pieces of a single puzzle, the Court's bankruptcy cases from 1990 to 1993 appear more like eighteen separate puzzles.

Still, can one engage in a mild, but constructive, cynicism and cull some transcendent similarities? Perhaps these cases are testing grounds for other, presumably more important or interesting statutes. They may simply be the latest vehicles in the Court's continuing effort to apply "plain meaning" to the interpretation of federal statutes. Alternatively, these cases with

so little of substance in common may reflect no more than the products of circuit splits natural with respect to a pervasive federal code entering the second decade of its existence. I opt for a mild, and not very informative, version of the last explanation.

Conspiracy

One could examine the eighteen cases and wonder: how could the Court decide so many bankruptcy cases in a three-year period without developing more of an interrelationship among them? Rarely do any of the eighteen decisions cite one another, and, even then, citation usually is only to the last case decided. Yet the statutory construction message is relatively clear: plain meaning, whatever that may be, is the preferred method of construction for the Bankruptcy Code.

One is tempted to expand that last statement. Plain meaning is the method of construction for all federal statutes. But, why do such intense and dogmatic discussions of plain meaning occur in bankruptcy cases?

I offer the following for conspiracy buffs. The Court is using bankruptcy cases to build an impressive (at least in numbers) body of precedent to apply to some tough statutory cases it knows are coming, such as the Americans with Disabilities Act, the Civil Rights Act of 1991, or even President Clinton's federal health care plan. The dark side of this theory is that the justices do not like such statutes, preferring Jefferson's agrarian and individualistic vision of the relationship between Congress and the people it governs. Anyone who has glanced at the text of these recent examples of social legislation can only cringe at the prospect of applying the literalism of, say, *Connecticut National Bank v. Germain* to such statutes. In short, the Court is sacrificing a coherent bankruptcy policy to thwart expansive interpretation of congressional efforts in the social policy arena.

As with most conspiracy theories, however, this one collapses of its own

weight. *Dewsnup v. Timm*, *Barnhill v. Johnson*, and *Pioneer Services*, at least, present gaps in the monolithic vision required by this theory.³² More importantly, the collective *animus* necessary for this theory is likely not present. My perhaps naive belief in the essential decency of the justices precludes any notion that the justices consistently and pervasively utilize this kind of tententious approach to the cases before them. Also, the lack of citation in non-bankruptcy cases to the analysis contained in the eighteen cases reviewed above tends to rule out an active campaign for their advancement as the new vanguard of statutory construction.

Literalism

So why the continued recitation of plain meaning? Perhaps it is because many of the justices sincerely believe in it. The affirmative case for such literalism is that, in our system of government, Congress legislates and the Court merely interprets. Unlike federal agencies such as the Environmental Protection Agency or the Federal Reserve Board, courts do not exist to fill in gaps in legislation consistent with an overall congressional purpose. And the lack of any such agency to administer the Bankruptcy Code has forced the issue in bankruptcy in ways which would not exist in other areas of federal legislation.

In short, under this view, a sincere belief in separation of powers meets one of the few pervasive and controversial federal statutes which goes directly from Congress to the courts without any intermediate interpretation. Tax statutes, by contrast, are just as (or more) complex, but they are mediated by IRS regulations which affect their construction, and, more importantly, the process for litigating their interpretation in ways not experienced in bankruptcy. A similar mediation occurs with environmental and banking statutes. In bankruptcy, however, the Court is often presented with cases of arguably ambiguous statutory text (likely the product of congressional compromise), and the

only guides as to its meaning are the decisions of the courts below. Missing is interpretation by an entity whose purpose is to interpret a federal code consistently.

This is the most benign statement of this proposition that I can muster. Noting a lack of a leavening force may be an explanation of the fractured nature of the eighteen cases, but it is not a justification. After all, the common law studied in the first year of law school is probably a better example of the attempt to weave a consistent body of law of general applicability without the benefit of a federal agency's interpretation. And some courts manage to get that right.

This theory then gets turned on itself. Failure to interpret the Bankruptcy Code consistently then becomes an abdication of judicial responsibility, not a vindication of it. But even this is an overstatement. As Robert Rasmussen has noted recently, the Court's plain meaning approach has not affected the outcome of many of the decided cases.³³ For the most part, the Court's decisions definitively settle some common issues. After *Barnhill*, for example, there should not be much question as to when a check constitutes a transfer; after *Dewsnup*, there can be little doubt that lien stripdown is not available.

But, as of yet, this piecemeal response to the question of the moment has left many of us unsatisfied that the Court is doing right by the Bankruptcy Code. We long for the days of (dare I say it) Justice William O. Douglas, who actively participated in shaping the contours of the Chandler Act of 1938 (*Case v. Los Angeles Lumber* was his third written opinion) and bankruptcy policy thereafter. It is safe to say that no one fills his shoes now.

Ennui

This leads me to my final and pedestrian point. Perhaps the best explanation of the eighteen cases is simply that, one decade after its enactment, the Bankruptcy Code has matured to a point where many of its terms are now the subject of disparate treatment at

the circuit level. Enough cases have arisen and been appealed that only now are we seeing significant splits among the circuits on various interpretations of the Bankruptcy Code. And because the Court does view one of its functions as correcting such circuit splits, these cases naturally present themselves to the Court, and to its clerks, as likely candidates for *certiorari*.

How else to explain cases like *Toibb*, in which the Court had to appoint counsel for one of the parties? Or *Union Bank*, in which Justice Scalia excoriates counsel and some courts as follows: "[i]t is regrettable that we have a legal culture in which such arguments have to be addressed (and are indeed credited by a Court of Appeals), with respect to a statute utterly devoid of language that could remotely be thought to distinguish between long-term and short-term debt. Because there was here no contention of a 'scrivener's error' producing an absurd result, the plain text of the statute should have made this litigation unnecessary and unmaintainable."³⁴ Or the high number of 9-0, or 8-1 opinions?

Another facet of this explanation may be the role of Justice Thomas. After he was appointed, he authored five of the nine subsequent bankruptcy decisions. I do not think the reason for this is that he is a bankruptcy buff. Rather, the Court's practice of allowing the senior justice in the majority (or the chief justice if he is in the majority) to assign the opinion may account for it. It is not a fanciful view to envision a conference in which all eyes turn to Justice Thomas, the new guy, to resolve a circuit split over what must appear to the rest as a relatively arcane bankruptcy point. Watch to see if Justice Ginsburg writes the next wave of bankruptcy opinions.

Of course, those of us who focus upon the Bankruptcy Code as part of our daily work rightly wince at this prospect. But the Bankruptcy Code is resilient, and it will take more than a motley collection of interpretations to deprive it of its place in commercial law. We can at least count our bless-

ings that the Court, for whatever reason, has avoided subjecting significant bankruptcy issues to analysis over this period. The Court has not spoken definitively on jury trial rights,³⁵ on the proper scope of the absolute priority rule,³⁶ or on a host of other issues central to the smooth and efficient operation of the bankruptcy sys-

tem. Maybe that is why these cases are so unsatisfying: the Court has not been pressed by the issues presented to consider the whole.

So, I end as I began, without any sure-fire, snappy explanation or justification linking the eighteen bankruptcy cases decided during October Terms 1990-1993. I think we will con-

tinue to see bankruptcy cases decided at a higher rate than the historic one or two cases a year, but certainly at a lesser rate than recently. Moreover, I think that the happenstance of a circuit conflict will be the most salient explanation for the grant of *certiorari*. Beyond that, one can only speculate.

ENDNOTES

¹The following table sets forth the basic statistics. The numbers are taken from the *Harvard Law Review's* annual review of the Supreme Court. For the total number of "opinions written," I have used the number of cases which appear under the *Method of Disposition* column, currently found in Table II of the annual review. As to the categorization of a case as a "bankr. opinion," I have relied upon Table III of the annual review, and have supplemented that table when appropriate.

Year	Opinions Written	Bankr. Opinions	Percent
OT 1992	119	3	2.52%
OT 1991	127	9	7.09%
OT 1990	129	6	4.65%
3-YEAR AVG.			4.75%
OT 1989	151	2	1.32%
OT 1988	170	2	1.18%
OT 1987	167	2	1.20%
OT 1986	175	1	0.57%
OT 1985	172	1	0.58%
OT 1984	175	2	1.14%
OT 1983	184	1	0.54%
OT 1982	182	2	1.10%
OT 1981	216	3	1.39%
OT 1980	159	0	0.00%
10-YEAR AVG.			1.02%

²The eighteen cases are as follows, with a short description of its holding following each:

October Term 1990

- *Langenkamp v. Culp*, 498 U.S. 42 (1990) (*per curiam*). Filing a proof of claim constitutes a waiver of jury trial rights for preference actions
- *Grogan v. Garner*, 498 U.S. 279 (1991). Dischargeability determined by preponderance of evidence standard; collateral estoppel applies to state court findings on relevant issues
- *Farrey v. Sanderfoot*, 111 S. Ct. 1825 (1991). Husband may not use Section 522(f) to avoid lien on former marital residence imposed by court in divorce proceedings if those proceedings restructured ownership interests so that spouse's lien was created at the same time as debtor's interest

- *Owen v. Owen*, 111 S. Ct. 1833 (1991). Husband may not retroactively take advantage of revision of state homestead exemption
- *Johnson v. Home State Bank*, 111 S. Ct. 2150 (1991). Debtor may file Chapter 13 case to reorganize home mortgage payments after discharging personal liability in Chapter 7 case
- *Toibb v. Radloff*, 111 S. Ct. 2197 (1991). Individuals may file Chapter 11 even if not engaged in business

October Term 1991

- *Board of Governors of the Federal Reserve System v. MCorp. Financial, Inc.*, 112 S. Ct. 459 (1991). Automatic stay in bankruptcy does not affect Federal Reserve's ability to force contributions of capital to bank subsidiaries under Fed's source of strength powers
- *Union Bank v. Wolas*, 112 S. Ct. 527 (1991). Payments on long-term debt may qualify as being made in the ordinary course of business for purposes of exception to preference law
- *Dewsnup v. Timm*, 112 S. Ct. 773 (1992). Chapter 7 debtor may not "strip down" undersecured mortgage, discharge deficiency, and redeem property secured at market value
- *United States v. Nordic Village, Inc.*, 112 S. Ct. 1011 (1992). United States Government, as recipient of preference payment of corporate insider's tax payment, has sovereign immunity
- *Holywell Corp. v. Smith*, 112 S. Ct. 1021 (1992). Liquidating trustee of Chapter 11 concern must file fiduciary tax returns
- *Connecticut Nat'l Bank v. Germain*, 112 S. Ct. 1146 (1992). Special jurisdictional statutes for bankruptcy appeals do not affect other avenues of appeal from district courts
- *Barnhill v. Johnson*, 112 S. Ct. 1386 (1992). For purposes of preferences, transfer is made when check honored, not when delivered
- *Taylor v. Freeland & Kronz*, 112 S. Ct. 1644 (1992). Trustee in bankruptcy must object to debtor's claimed exemptions within thirty-day period; no

exception for exemptions taken in bad faith or without any statutory justification

- *Patterson v. Shumate*, 112 S. Ct. 2242 (1992). ERISA-qualified pension plan exempt from bankruptcy court distribution

October Term 1992

- *Pioneer Inv. Serv. Co. v. Brunswick Assoc. Ltd. Ptnshp.*, 113 S. Ct. 1489 (1993). Excusable neglect in filing a proof of claim is subject to a balancing test which includes the good faith of the parties
- *Nobelman v. American Savings Bank*, 113 S. Ct. 2106 (1993). Chapter 13 plan may not affect the rights of a holder of a mortgage secured solely by the debtor's primary residence even if value of home is less than obligations secured by home
- *Rake v. Wade*, 113 S. Ct. 2187 (1993). Chapter 13 debtor must include post-petition interest, even if not required by applicable non-bankruptcy law, in any effort to cure defaulted mortgage
³498 U.S. at 44.

⁴The Court's focus on the filing of a proof of claim seems formalistic and potentially mischievous. The Code presumes filing in some circumstances (section 1111(a)), permits the debtor to file a claim for any creditor in others (Bankr. R. 3004), and has been interpreted loosely with respect to informal proofs of claim. Will the Court treat any of these circumstances as the filing of a proof of claim within *Langenkamp*? If *Langenkamp's* requirement of filing is taken at face value, rather than as evidence of implied consent, they might.

⁵498 U.S. at 284 n.11.

⁶See 28 U.S.C. § 1738.

⁷498 U.S. at 282 n.2.

⁸111 S. Ct. at 1829.

⁹11 S. Ct. at 1832.

¹⁰111 S. Ct. at 1831.

¹¹111 S. Ct. at 1831 n.4.

¹²See 11 U.S.C. § 522(d)(1)-(6); (8).

¹³Not surprisingly, the lower courts found that the debtor did not have an interest in the property, as the majority

defined it, and ruled for the non-debtor. *Owen v. Owen*, 961 F.2d 170, 172 (11th Cir.), *cert. denied*, 113 S. Ct. 659 (1992).

¹⁴896 F.2d 1394 (2d Cir.), *cert. granted*, 110 S. Ct. 3269, *cert. vacated and reinstated on remand*, 924 F.2d 36 (2d Cir.), *cert. denied*, 111 S. Ct. 2041 (1991).

¹⁵112 S. Ct. at 530.

¹⁶*Id.* at 534.

¹⁷*Id.* at 533-34.

¹⁸Judge Jones, of the Fifth Circuit Court of Appeals, believes that *Dewsnup* has "clouded" statutory construction in bankruptcy. *Phoenix Mutual Life Ins. Co. vs. Greystone III Joint Venture (In re Greystone III Joint Venture)*, 995 F.2d 1274, 1285 (5th Cir. 1992) (Jones, J., dissenting from grant of rehearing). In one of the more literate defenses of plain meaning, she echoed Galileo's words when asked to affirm church doctrine that the sun revolves around the Earth: "*eppur si muove*" ("And yet it moves"). *Id.* Time will tell whether, as Judge Jones apparently believes, the context revolves around a statute, or whether the statute is the satellite controlled by context.

¹⁹112 S. Ct. at 787.

²⁰112 S. Ct. at 1151.

²¹*Id.* at 1150 (Stevens, J., concurring).

²²112 S. Ct. 1149.

²³Note: the statutory reference is to the second section 101(54); Congress

hasn't gotten its act sufficiently together to iron out all the duplicated section designations.

²⁴See UNIFORM COMMERCIAL CODE § 3-802(1)(b); Revised § 3-310(b).

²⁵112 S. Ct. at 1392.

²⁶112 S. Ct. at 2249.

²⁷440 U.S. 48 (1978).

²⁸*Id.* at 2250-51.

²⁹95 B.R. 134 (9th Cir. BAP 1988).

³⁰The Court also attempted to show that its result was consistent with a claims analysis.

Congress chose to use the phrase "claim secured . . . by" in § 1322(b)(2)'s exception, rather than repeating the term of art "secured claim." The unqualified word "claim" is broadly defined under the Code to encompass any "right to payment, whether . . . secure[d] or unsecured" or any "right to an equitable remedy for breach of performance if such breach gives rise to a right to payment, whether . . . secure[d] or unsecured." 11 U.S.C. § 101(5) (1988 ed., Supp. III). It is also plausible, therefore, to read "a claim secured only by a [homestead lien]" as referring to the lienholder's entire claim, including both the secured and the unsecured components of the claim.

113 S. Ct. at 2111.

³¹S. 540, 103d Cong., 1st Sess., § 310(c) (1993) (Oct. 28, 1993). *See also* S. REP. NO. 168, 103d Cong., 1st Sess. 53 (1993).

³²The Court's waffling on *Ben Cooper* is further evidence of an inability to agree on a unified approach.

³³Robert K. Rasmussen, *A Study of the Costs and Benefits of Textualism: The Supreme Court's Bankruptcy Cases*, 71 WASH. U.L.Q. 535 (1993).

³⁴*Union Bank*, 112 S. Ct. at 112.

³⁵Indeed, it affirmatively avoided the issue in *Ben Cooper*.

³⁶As this article was going to press, the court granted *certiorari* in *Bonner Mall Partnership v. U.S. Bancorp Mortgage Co. (In re Bonner Mall Partnership)*, 2 F.3d 899 (9th Cir. 1993), *cert. granted*, 66 U.S.L.W. 3451 (Jan. 10, 1994) (No. 93-714). *Bonner Mall* presents the issue of the viability of the new value exception/corollary to the absolute priority rule, an issue the court ducked the last time it was presented. *Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 203 n.3 (1988). It also presents an issue of appellate jurisdiction, being a denial of relief from stay and, thus, might allow the court to avoid the issue again.



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