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## **Supreme Court Stops Bad Faith Chapter 7 Debtor's Conversion To Chapter 13**

By Donald F. Campbell, Jr., Esq.

After the 2005 Bankruptcy Abuse Prevention and Consumer Protect Act (BAPCA), the U.S. Supreme Court's recent decision in Marrama v. Citizens Bank of Mass., et. al., 549 U.S. \_\_\_ (2007) will add a chilling effect to an already frigid court. On February 21, 2007, the Court ended the long-standing practice of debtors invoking an "automatic right" to convert their bankruptcy case from Chapter 7 liquidation to Chapter 13 individual plan of reorganization. The Court's decision will now permit creditors to object to a debtor's conversion, which was typically sought after a creditor or trustee discovered assets concealed by the debtor.

In Marrama, the debtor, Robert Marrama, filed a voluntary petition under Chapter 7 of the Bankruptcy Code seeking a discharge of his pre-petition debts. In schedules attached to his petition, Marrama failed to disclose that he was the beneficiary of a trust, which he created, and that he transferred the Maine property into the trust seven months prior to filing his petition for no consideration. The Chapter 7 Trustee discovered the undisclosed asset and informed Marrama that he would seize the Maine property for sale and distribution for the benefit of creditors. Marrama's apparent fondness for his Maine retreat outweighed his desire for a Chapter 7 discharge and, pursuant to §706(a) of the Code, he filed a notice to convert his case to Chapter 13, which would have permitted Marrama to keep the Maine property in exchange for repaying a portion of his debts to creditors as opposed to walking away from his debts entirely in a Chapter 7. Marrama's main creditor, Citizens Bank, and the Trustee objected to the conversion and the Bankruptcy Court agreed stating that "there is no 'Opps' defense to concealing assets" and ruled the attempted conversion an act of "bad faith."

Marrama appealed the Bankruptcy Court's decision all the way up to the Supreme Court relying upon numerous lower-court decisions that have, in many jurisdictions including New

Jersey, given the debtor an automatic right to convert to Chapter 13. Marrama also cited the U.S. Senate Reports on §706(a), which states that the debtor has a “one-time absolute right of conversion” from Chapter 7 liquidation to a Chapter 13 plan of repayment giving the Debtor “an opportunity to pay his debts.” The Supreme Court, in a 5-4 decision written by Justice Stevens, ended the long-standing debate among the Courts ruling that the debtor’s right to convert to Chapter 13 is expressly conditioned upon a debtor’s right to qualify as a “debtor.” If the court finds the debtor, like Marrama, acted in bad faith, the debtor will not qualify as an individual entitled to a discharge under the Bankruptcy Code under either Chapter, giving the Court cause to deny the debtor’s requested conversion.

Within days of Marrama, the New Jersey Bankruptcy Court issued an unpublished decision in In re Truong denying a Chapter 7 debtors’ conversion to Chapter 13. In that case, the Hon. Novalyn L. Winfield, citing Marrama, found that the debtors fraudulently transferred property and failed to cooperate with the Chapter 7 Trustee, and therefore filed their petition in “bad faith” and were “unworthy of and therefore ineligible for the benefits of Chapter 13.” While the vast majority of conversions by debtors will remain unopposed and permitted by the court, after Marrama and Truong, debtors and the courts can expect many more such objections by Chapter 7 Trustees and astute creditors. A conversion to Chapter 13 not only permits the debtor to retain property, but buys the debtor time (sometimes years) and rids the debtor of a hostile Chapter 7 Trustee. A successful motion denying conversion will force the debtor to either settle with their creditors or risk the loss of property and rights to a discharge.

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ATTORNEYS AT LAW

125 Half Mile Road, Red Bank, NJ 07701 • (732) 741-3900  
441 East State St., Trenton, NJ 08608 • (609) 695-3900  
[www.ghclaw.com](http://www.ghclaw.com)