

**UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF WISCONSIN**

Cite as: 549 BR 721

**Dominic A. and Barbara J. Gorniak, Debtors
Bankruptcy Case No. 13-15827-7**

United States Bankruptcy Court
W.D. Wisconsin, Madison Division

April 8, 2016

Claire Ann Resop, Steinhilber, Swanson, Resop & Sipsma, Madison, WI for Debtor
Michael E. Kepler, Madison, WI for Trustee

Robert D. Martin, United States Bankruptcy Judge

MEMORANDUM DECISION

Debtors, Dominic and Barbara Gorniak, filed a Chapter 11 case which they converted to Chapter 7 on June 27, 2014. At the time of the conversion, the debtors maintained a debtors in possession (DIP) account which contained \$8,652.43, 100% of which was post-petition earnings of the debtors. The Chapter 7 trustee sought turn-over of the \$8,652.43 arguing that pursuant to 11 U.S.C. §§ 541, 1115(a)(2), 348(f), and existing case law within the Seventh Circuit interpreting these provisions, the funds held in the DIP account on the date of conversion are property of the Chapter 7 bankruptcy estate.

The debtors objected, relying on *In re Evans*, 464 B.R. 429 (Bankr. D. Colo. 2011), and *In re Markosian*, 506 B.R. 273 (B.A.P. 9th Cir. 2014). Debtors argue that pursuant to §§ 348(a) and 348(f) assets of an estate at the time of conversion from Chapter 11 to 7 are treated in the same way as assets of an estate at the time of conversion from Chapter 13 to 7. Additionally, debtors assert that *Harris v. Viegelahn*, 135 S.Ct. 1829 (May 18, 2015), “makes it clear that after a conversion, post-petition earnings are not property of the Chapter 7 estate.”

11 U.S.C. § 541(a)(6) provides:

(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all of the following property, wherever located and by whomever held:

(6) Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.

11 U.S.C. § 541 (2012).

In Chapter 13, § 1306(a)(2) provides:

(a) Property of the estate includes, in addition to the property specified in section 541 of this title -

(2) earnings from services performed by the debtor after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7, 11, or 12 of this title, whichever occurs first.

11 U.S.C. § 1306 (2012).

Similarly, in Chapter 11, § 1115(a)(2), provides:

(a) In a case in which the debtor is an individual, property of the estate includes, in addition to the property specified in section 541 -

(2) earnings from services performed by the debtor after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7, 12, or 13, whichever occurs first.

11 U.S.C. § 1115 (2012).

Section 348(a) provides:

(a) Conversion of a case from a case under one chapter of this title to a case under another chapter of this title constitutes an order for relief under the chapter to which the case is converted, but, except as provided in subsection (b) and (c) of this section does not effect a change in the date of the filing of the petition, the commencement of the case, or the order for relief.

11 U.S.C. § 348 (2012). Additionally, §§ 348(f)(1)(A) and (2) provide:

(f)(1) Except as provided in paragraph (2), when a case under chapter 13 of this title is converted to a case under another chapter under this title –

(A) the property of the estate in the converted case shall consist of property of the estate as of the date of filing of the petition, that remains in the possession of or is under the control of the debtor on the date of conversion

.....

(2) If the debtor converts a case under chapter 13 of this title to a case under another chapter under this title in bad faith, the property of the estate in the converted case shall consist of the property of the estate as of the date of conversion.

11 U.S.C. § 348 (2012). Congress has enacted no analogue to § 348(f)(1)(A) for Chapter 11 to 7 conversions.

Several bankruptcy courts within the Seventh Circuit have addressed the expansive interpretation of § 348(a) suggested by the debtors. In 1986, in *In re Ford*, this court rejected the interpretation. 61 B.R. 913, 916 (Bankr. W.D. Wis. 1986). In 2015, in *In re Meier*, relying on the Seventh Circuit's 1992 *In re Lybrook* decision, the United States Bankruptcy Court for the Northern District of Illinois reached the same conclusion. 528 B.R. 162, 165 (Bankr. N.D. Ill. 2015).

In *In re Ford*, this court analyzed a creditor's argument that for all purposes not specifically excluded by §§ 348(b) and (c), including a determination of what assets are included in the estate, a debtor's converted case must be treated as though it were a Chapter 7 case actually filed on the original petition date. 61 B.R. at 916. Looking to § 348(a), this court found that although that subsection provides that "a chapter 7 case which has been converted from a case under another chapter is considered to have been commenced on the date of the original petition," that "does not mean . . . that all actions taken in the case prior to conversion become nullities." *Id.* at 916. Specifically, in a Chapter 11 to 7 conversion, this court held that "[t]he operation of section 348(a) of the Code does not result in the retroactive divestment of post-petition property acquired by the estate upon conversion to chapter 7." *Id.* at 917-918.

The conclusion in *In re Meier* was based on the Seventh Circuit's 1992 *In re Lybrook* decision. Debtors in *Lybrook* argued that the \$70,000 they received post-petition was not property of the Chapter 7 estate after conversion. Specifically, debtors looked to § 348(a) to argue that "the Chapter 7 proceeding should . . . be deemed to have begun on the day the chapter 13 proceeding was filed." *In re Lybrook*, 951 F.2d at 137 (quoting 11 U.S.C. § 48(a)). And, the \$70,000 would not have been includable in the Chapter 7 estate at that time, so, it should be excluded following conversion. In finding against the debtors, the court was "more impressed by the bankruptcy judge's observation that a rule of once in, always in is necessary to discourage strategic, opportunistic behavior that hurts creditors without advancing any legitimate interest of debtors." *Id.* Accordingly, although the debtors proposed one "possible reading" of § 348(a), "an equally good alternative from a purely semantic perspective is that conversion from Chapter 13 to Chapter 7 does not affect the bankrupt estate but merely assures the continuity of the case for purposes of filing fees, preferences, statutes of limitations, and so forth." *Id.*

In *In re Meier*, the debtor filed for bankruptcy under Chapter 11, but then voluntarily converted to Chapter 7. After conversion Meier asserted that the \$98,004.23 in his DIP checking account, which was post-petition personal services income, was not property of

the estate. Meier's cited the 9th Circuit BAP's *In re Markosian* decision. In finding against Meier, the court rejected the position adopted by both the *In re Markosian* and *In re Evans* courts, and held that:

If Congress had meant to reject the rule in *Lybrook* generally instead of only in Chapter 13, it could have done so. Instead, there is an express statutory command that rejects the *Lybrook* rule for conversions from Chapter 13. § 348(f)(1). However, there is no such statute for Chapter 11, so the *In re Lybrook* interpretation of § 348(a)(1) is still law in this Circuit. Therefore, personal income of a Chapter 11 debtor is property of the Chapter 7 estate after conversion.

....

The money in the subject DIP account is property of the estate and is not subject to any exception.

In re Meier, 528 B.R. at 165; see *In re Hoyle*, 2013 WL 3294273 (Bankr. D. Idaho 2013) ("In light of the omission of a provision equivalent to § 348(f)(1) applicable to the converted chapter 11 case, Debtor's argument that the DIP accounts at conversion are not 'property of the estate' does not hold.") (citing *In re Tolkin*, 2011 WL 1302191 (Bankr. E.D.N.Y. 2011)).

The debtors' misread *Harris*. In *Harris* the Supreme Court addressed the narrow question of what a trustee must do with a debtor's post-petition earnings following conversion from Chapter 13 to Chapter 7. 135 S. Ct. 1829, (2015); see *Id.* at 1835 ("May the trustee distribute the accumulated wage payments to creditors as the Chapter 13 plan required, or must she remit them to the debtor? That is the question this case presents."). The *Harris* decision does not stand for the proposition that all post-petition earnings revert to a debtor when a case is converted from *any* chapter to a Chapter 7. Nowhere does the *Harris* court mention Chapter 11 filings or conversions from Chapter 11 to Chapter 7. See *Id.* ("Two roads individual debtors may take are relevant here: Chapter 7 and Chapter 13 bankruptcy proceedings."). Accordingly, debtors' contentions that, "[t]he reasoning behind *In re Lybrook* and any other similar decision has been unanimously rejected by the U.S. Supreme Court," and that "[t]hese holdings have been overruled by *Harris* and their binding or persuasive authority is no longer valid," are unsupported by the text of the *Harris* decision. Further, debtors' argument that "any court holding that a debtor's post-petition earnings constitute property of the Chapter 7 estate after conversion would . . . be . . . ruling against an explicit Supreme Court holding," is inaccurate, as the *Harris* court did not so hold. The *Harris* court relied on § 348(f), and, accordingly, debtors' reliance on the *Harris* opinion is misplaced. *Id.* at 1837.

Turnover of the DIP account at question here to the trustee is compelled by the controlling law. It may be so ordered.