N O T E S O N

DEBTOR/CREDITOR

R E L A T I O N S

October 2021

Arbitration in a Bankruptcy Case

In passing the Federal Arbitration Act, Congress expressed its intent that federal courts enforce contract agreements requiring arbitration of disputes. However, there are times when enforcement of an arbitration agreement may conflict with the core objectives of another statutory scheme, such as the bankruptcy law. A bankruptcy judge in Baltimore recently opined regarding the proper balance a court should strike when these two statutes come into conflict.

Prior to his bankruptcy, Mr. McPherson entered into a litigation funding agreement with Camac Fund, L.P., which contained an arbitration clause. Disputes developed between the parties, and Camac invoked the arbitration clause and commenced arbitration. Mr. McPherson asserted counterclaims in the arbitration proceeding, but filed a Chapter 11 case before any hearing in the arbitration. Camac filed motions seeking to have all the disputes between the parties resolved in the arbitration. Mr. McPherson filed pleadings to have the bankruptcy court resolve the disputes.

The judge explained that a claim should be determined by arbitration unless it "stems from the bankruptcy itself or would necessarily be resolved in the claims allowance process." The court identified three categories of claims in dispute: (1) claims for breach of the funding agreement; (2) claims under the Fair Debt Collection Practices Act; and (3) claims arising under the bankruptcy statute. Although all of the claims were factually intertwined, the bankruptcy judge decided that the claims in categories one and two would be determined by arbitration while the claims in category three would be determined by the Bankruptcy Court.

In re McPherson, 2021 Bankr LEXIS 1480 (Bankr. D. Md. 2021).

Exemption for Property in Trust

The State of Maryland permits an individual debtor in bankruptcy to exempt and retain $25,150 from the value of the equity in "owner-occupied residential real property." This is referred to as the homestead exemption. Does this exemption apply where the debtor resides in a house that is owned by a trust created by the debtor?

This question was recently considered by a Maryland bankruptcy court. The debtor listed among his assets a residence owned 50% by a self-settled revocable trust and 50% by his ex-wife. The debtor claimed the homestead exemption for the trust's 50% interest. The bankruptcy trustee opposed the exemption, contending that the house was not "owner-occupied", because it was titled in the trust.

The bankruptcy judge disagreed. The creator of a revocable trust has the power to dispose of and receive the trust property, is taxed on any income generated by the trust property, and may use the trust property. Creditors of the trust creator may reach the trust property to collect their debts. For all these reasons, the judge concluded that the debtor was effectively the owner of property titled in the trust and could claim the exemption.

In re Loughlin, 2021 LEXIS 1030 (Bankr. D. Md. 2021).

○ ○ ○

This newsletter is intended to inform its readers of developments in the area of debtor/creditor relations. It is not legal advice or a legal opinion regarding any specific matter. You should consult a lawyer regarding any questions relating to your particular situation. Congress has required bankruptcy attorneys to state: "I am a debt relief agency. I help people file for bankruptcy relief under the Bankruptcy Code." 11 U.S.C. § 528. If you wish to receive "Notes on Debtor/Creditor Relations", go to www.jamesolsonattorney.com/newsletter.html and click on the link at the word "here".

Prepared by James C. Olson, Attorney and Counselor at Law

One Corporate Center Suite 400 10451 Mill Run Circle Owings Mills, MD 21117 410-356-8852 Fax 443-501-2636 jolson@jamesolsonattorney.com