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By Lynn Middendorf

In ***Capital Communications Federal Credit Union v. Boodrow*, 126 F.3d 43 (2d Cir. 1997)**, the United States Court of Appeals for the Second Circuit held that a debtor who has filed for bankruptcy under Chapter 7 may retain possession of the collateral for a loan and continue to make loan payments under the loan agreement as long as the debtor remains current on his payments. Presented with a case of first impression, the court found that the debtor's retention of collateral, without redemption or reaffirmation, does not violate 11 U.S.C. § 521(2).

A debtor who files for bankruptcy has three options under § 521(2) regarding debts secured by personal property. First, a debtor may "surrender," or return his collateral to a creditor. Second, he may "redeem," or keep the collateral by paying the creditor for the property. Finally, he may "reaffirm" his financing agreement with the creditor by entering into a new loan arrangement, even an agreement potentially containing new terms.

In the present case, Brian Boodrow ("Boodrow") had secured a car loan from Capital Communications Federal Credit Union ("Capital"), for $15,900 to pay for a 1992 Pontiac Grand Am. In May 1995, Boodrow filed for bankruptcy under Chapter 7 of the Code. When Boodrow filed for bankruptcy, the amount outstanding on the loan was $8,820 and the car's market value was $9,650.

After submitting his bankruptcy petition, Boodrow indicated that he intended to keep his car and reaffirm his debt with Capital by filing a statement of intention as required by 11 U.S.C. § 521(2). When Boodrow determined, however, that he could not return to work full-time because of a permanent disability, he did not reaffirm his loan agreement with Capital. Instead, he simply kept the car, retained the proper insurance, and stayed current on his monthly loan payments.

In July 1995, Capital filed a motion to lift Boodrow's automatic stay and for other relief on the grounds that Boodrow had failed to follow the requirements of § 521(2). Capital argued that Boodrow had to turn the car over, pay the entire market value of the car, or reaffirm his debt under § 521(2), and that Boodrow's failure to comply with § 521(2) constituted "cause" to lift the automatic stay.

In August 1995, the bankruptcy court heard Capital's motion but reserved its decision. In September 1995, the court discharged Boodrow from bankruptcy. Then in December, the court denied Capital's motion to lift Boodrow's automatic stay. The bankruptcy court held that Capital had not shown sufficient cause to lift the stay because § 521(2) permits a debtor to keep his collateral and continue payments according to the loan agreement. In addition, the court held that Capital had not shown that it would be harmed if the stay remained in place. Capital appealed and both the district court and the Second Circuit affirmed the bankruptcy court's decision.

Discharge of Bankruptcy Does Not Necessarily Make a Case Moot

The Second Circuit first addressed whether the case was moot since Boodrow's discharge from bankruptcy occurred before a decision was reached on Capital's motion to lift the automatic stay. The court discussed two main issues. The first issue was whether the automatic stay dissolved as a result of Boodrow's discharge from bankruptcy. Under 11 U.S.C. § 362(c)(1), "the stay of an act against property of the estate . . . continues until such property is no longer property of the estate." In other words, an automatic stay will not terminate merely upon a debtor's discharge from bankruptcy. The court held that the stay did not dissolve at discharge because Boodrow still retained the car after September 1995.

The second issue the court addressed was whether the court remained able to grant any relief to Capital even after Boodrow's discharge from bankruptcy. According to the U.S. Supreme Court, a case is moot only if the court of jurisdiction can no longer grant any relief to the injured party. The court reasoned that Capital was seeking a lift of the automatic stay either to recover the vehicle or benefit from proceeds of comparable monetary value. Therefore, because the bankruptcy court granted Boodrow the discharge while he retained possession of the vehicle, the court essentially perpetuated the alleged harm that Capital was seeking to avoid in its motion to lift the stay. The Second Circuit held that it could grant Capital the relief it sought if it agreed with Capital's interpretation of § 521(2). For example, the court could remand the case back to the bankruptcy court and order Boodrow to comply with § 521(2). After remand, Capital could still receive monetary compensation at the value of Boodrow's outstanding loan or simply repossess the vehicle. Because

Capital could still attain relief, the court held that the case was not moot.

Court Offers a Broad Interpretation

In examining the merits of the case, the Second Circuit explained that a bankruptcy court can lift an automatic stay if the movant shows cause. Capital argued that, pursuant to § 362(d)(1), it had shown cause that the stay should be lifted because Boodrow failed to comply with § 521(2). Capital asserted that because Boodrow did not reaffirm his debt, turn the car over to his creditor, or pay his creditor the full value of the car, he did not meet the requirements of § 521(2). The court acknowledged that other circuits have held that a debtor is exclusively limited to the options specified in § 521(2). Boodrow responded that he had met the requirements of § 521(2) by notifying Capital of his intentions to keep the car and to continue making payments under the original loan agreement, thus, Capital had not shown cause to lift the stay. The court noted that other circuits had found these actions met the requirements of § 521(2) and examined several reasons for finding that Boodrow had met the requirements of § 521(2), beginning with the text of the statute.

In interpreting § 521(2), the court first turned to the text of the statute which states:

> within thirty days after the date of the filing of a petition under chapter 7 . . . the debtor shall file with the clerk a statement of his intention with respect to the retention or surrender of such property and, if applicable, specifying that such property is claimed as exempt, that the debtor intends to redeem such property, or that the debtor intends to reaffirm debts secured by such property.

The bankruptcy court and the district court had held that the language of the statute did not restrict Boodrow to those three options. Both courts looked to the decision of *Home Owners Funding Corp. v. Belanger*, 962 F.2d 345 (4th Cir. 1992), where the Fourth Circuit examined the phrase "if applicable" in § 521(2) and determined that such a phrase implied that the section's provisions were not exclusive. The bankruptcy court and the district court, therefore, permitted Boodrow to retain his car and continue payments to the creditor under the original loan agreement, a procedure which they called "reinstatement."

Capital, however, argued that the statute limited debtors only to the three express options of surrender, redemption, and reaffirmation. Capital relied on the Seventh Circuit's interpretation of "if applicable" in *Taylor v. AGE Federal Credit Union (In re Taylor)*, 3 F.3d 1512 (11th Cir. 1993). The Seventh Circuit had held that the statute's "if applicable" phrase merely distinguished the option of "retention or surrender" from the options of redemption or reaffirmation; the phrase, however, did not indicate that the debtor had other courses of action.

Moreover, Capital argued that its interpretation of § 521(2) was more sensible when § 521 was compared to other provisions of the statute. Under § 521(2)(B), the debtor must take action regarding the collateral within 45 days after serving his notice of intention to the creditor. Since Boodrow could not possibly pay the entire loan on his vehicle within 45 days after he decided to retain the property, allowing him to choose reinstatement conflicts with § 521(2) as a whole. Lastly, Capital contended that because there are no other options provided anywhere else in the Bankruptcy Code, those listed in § 521(2) are exclusive.

Unable to ascertain Congress' intent regarding the exclusivity of the options listed in § 521(2) from the Code's language, the court turned to the statute's legislative history. Congressional subcommittee reports suggested that the statute was designed as a notice provision in order to let the creditor know what the debtor was planning to do with the collateral used to secure debts. The court concluded that, since the purpose of the statute was to serve notice, it did not necessarily limit the options open to a debtor who wanted to keep the collateral and simply stay current on his loan. The court also held that even if the 45 day time limit in § 521(2) was contrary to the principle of reinstatement, the statute was nevertheless a notice provision, and debtors had a reinstatement option opened to them. Additionally, the court noted that a bankruptcy court has the discretion of extending the time period beyond 45 days.

The court concluded that the decisions of the bankruptcy court and the district court were consistent with the Code's policy of giving a debtor who has been discharged from bankruptcy a "fresh start." The U.S. Supreme Court has discussed the fresh start policy for debtors recently discharged from bankruptcy. Limiting a debtor to the three options listed in § 521(2) would prevent the debtor from having a fresh start. The Second Circuit reasoned that a debtor would probably not have the resources to redeem the collateral. Therefore, the debtor, if restricted to the three options in § 521(2), would either have to reaffirm the loan agreement or surrender the collateral. Since

reaffirmation involves renewed negotiations with the creditor, who frequently possesses greater bargaining power, the creditor would benefit from a new agreement. In addition, a debtor opting for surrender may have to give up important property, that being a car in this case. Thus, limiting debtors to the options provided in § 521(2) might prevent debtors from having a fresh start after discharge.

Capital responded that if a bankruptcy court permitted a debtor to retain his collateral without redeeming or reaffirming, a creditor would run the risk of serious financial harm. After discharge from bankruptcy, a debtor is free from liability on loans. Capital argued that if a debtor defaulted on a loan after discharge, a creditor would only be able to recover the collateral but would not be able to recovery the difference between the outstanding loan balance and the present value of the property. Capital also argued that after discharge the debtor, released from liability to the loan, would have no motivation to maintain the condition of the collateral or continue payments if the value of the collateral depreciates below the outstanding loan debt. Additionally, Capital contended that Boodrow's reading of § 521(2) essentially eliminates the reaffirmation option because no reasonable debtor would choose to reaffirm a debt and impose new liability on himself.

The court disagreed with Capital's arguments. Creditors would not be harmed substantially by reinstatement because creditors are entitled to recover the collateral's value if the debtor defaults on the loan. Hence, creditors would not face substantial harm if the value of the collateral was greater than the outstanding loan payments at the time of default. The court reasoned that a debtor is motivated to stay current on payments and maintain the value of the collateral because a debtor's chance of obtaining credit for a new, similar property is hampered by his bankruptcy. For example, Boodrow argued that he wanted to stay current on his loan and maintain his car because he had no way of obtaining another one. Additionally, the court reasoned that a debtor may choose to reaffirm his debt, even when reinstatement is an option, in order to reestablish credit or make a new loan agreement that would help him avoid default and cure any arrearage he may have had before filing for bankruptcy.

After examining the language of § 521(2), its legislative history, and the Code's policies, the court held that a debtor may retain his collateral and continue to make payments on a loan according to a loan's original agreement if he is current on his loan payments.

The court also explained that a bankruptcy court has the discretion to decide whether a debtor may retain collateral on a loan and continue making payments under the loan's original agreement. A bankruptcy court would consider the debtor's past payment history, the difference between the collateral value and the outstanding loan amount, and other pertinent factors. A debtor whose conduct indicated that he would not be able to continue making timely payments would probably not be protected from the automatic stay. The court then held that in this case, the bankruptcy court had not abused its discretion in denying Capital its motion to lift the stay. Capital had the burden of showing that it would suffer an affirmative harm if the bankruptcy court did not lift the stay. However, the court found that there was no evidence to indicate that Boodrow would fail to make timely payments. In addition, Capital had already conceded that the value of the collateral substantially outweighed the outstanding loan balance. Capital would still be able to recover the full outstanding loan if Boodrow defaulted. In other words, Capital had not shown an affirmative harm that would result from the bankruptcy court's decision. Therefore, the bankruptcy court had not abused its discretion when it denied Capital's motion.

Dissent Disagrees with Majority on Mootness and Interpretation

The dissent disagreed with the majority on both the mootness issue and the interpretation of § 521(2). The dissent first asserted that the case was moot, even before the bankruptcy court rendered its decision, and should have been dismissed. The dissent also disagreed with the majority's broad interpretation of § 521(2).

On the issue of mootness, the dissent reasoned that when Capital first filed its motion to lift the automatic stay in July 1995, there was a live dispute. However, when the bankruptcy court discharged Boodrow in September 1995 before rendering a decision on Capital's motion, a live dispute on the motion no longer existed. Under 11 U.S.C. § 362(c)(2)(C), a discharge from bankruptcy dissolves an automatic stay by operation of law. The automatic stay, therefore, lacked any valid legal existence after Boodrow was discharged from bankruptcy. Capital then lost any interest in the outcome of its motion to lift the stay.

Judge Shadur, the author of the dissenting opinion, first responded to the majority's conclusion that Boodrow's case was still opened after discharge because he retained the collateral. The dissent explained that after discharge, debtors under chapter

7 do not possess the collateral property. Rather, the trustee retains possessory rights. Boodrow, therefore, did not truly retain possession of his car after discharge.

Judge Shadur also disagreed with the majority's reasoning that the court was still able to grant relief to Capital if it agreed with Capital's interpretation of § 521(2). The majority had reasoned that relief could take the form of remanding back to the bankruptcy court with an order to compel Boodrow to comply with the statute, which the majority explained was Capital's real purpose in filing its motion to lift the stay. The dissent reasoned that Capital had not filed a motion to dismiss or compel Boodrow to comply with § 521(2). Capital's motion to lift the stay was an end total in itself. The only reason that Capital filed a motion to lift the automatic stay was to pursue further remedies under state law. The dissent suggested that the majority had read additional requests for relief into Capital's motion to create a live controversy. Since Capital had only requested relief in the form of lifting the stay, the majority was essentially rewriting Capital's motion. Therefore, when the bankruptcy court discharged Boodrow, no additional controversy remained regarding Capital's motion to lift the stay.

The dissent further dismissed Capital's claim that the case should be heard as an exception to the mootness doctrine because the issue was "capable of repetition, yet evading review." The exception allows certain special issues into review even if they are moot. The dissent explained that the exception to the mootness doctrine was only applicable in special circumstances: both where the case ended too soon so that the issue was never fully litigated prior to becoming moot, and where one could reasonably expect that the injured party would probably face the same issue again in future proceedings. The dissent found that such an exception did not apply because prior judicial deliberations in other jurisdictions showed that the courts had fully litigated the validity of reinstatement under § 521(2). The dissent contended that the court lacked jurisdiction to hear the merits of Capital's motion to lift the automatic stay when it became moot.

In addressing the merits of interpreting § 521(2), the dissent contended that Congress had listed all of a debtor's options in § 521(2). That section only provides three options: surrender, redemption, or reaffirmation. Accordingly, the phrase, "if applicable," does not give the debtor a fourth option to keep the collateral and continue payments. Furthermore, the dissent pointed out that the 45-day time limit specified in § 521(2) means that a debtor cannot continue payments for months or years under reinstatement and remain consistent with such a time limit. The dissent also stated that, because reinstatement options are not mentioned in any other provision of the Code, the provisions of § 521(2) must be exclusive. The dissent also noted that debtors would obviously opt for reinstatement over any other option under § 521(2) because a debtor would not have to pay the full balance of his loan in one lump sum payment or negotiate with his creditors in a reaffirmation agreement where he would have substantially inferior bargaining power. Though reinstatement is desirable to debtors, if Congress did not intend for the debtor to have a reinstatement option, the court may not devise a new alternative for the debtor.

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Purchaser of Ship Allowed to Recover for Damage to Ship's Equipment

By Zachary Raimi

In ***Saratoga Fishing Co. v. J.M. Martinac & Co.*, 117 S. Ct. 1783 (1997), on remand *sub nom.* *Saratoga Fishing Co. v. Marco Seattle Inc.*, 122 F.3d 1250 (1997),** the United States Supreme Court reversed the United States Court of Appeals for the Ninth Circuit by holding that a plaintiff in admiralty may recover for physical damage that a defective portion of a ship caused to equipment that the original owner added to the ship before the plaintiff purchased the vessel. The Court found that Plaintiff could recover under admiralty tort rules because the added equipment was not part of the "product itself" -- the ship -- but rather was "other property" distinct from the ship.

Defective Hydraulic System Caused Fishing Vessel to Sink

In the early 1970s, J.M. Martinac & Company ("Martinac") manufactured a ship, a component of which