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Conversion of Bankruptcy Cases

Professor Margaret Howard
Washington & Lee University Law School

I. Property of the post-conversion estate

A. Chapter 13 → Chapter 7

1. Generally

In a Chapter 13 case, property of the estate includes the debtor's earnings post-petition and pre-conversion. § 1306. Thus, the question arose whether property acquired by the debtor post-filing and pre-conversion—generally, earnings—should be property of the estate, given that those assets would not have been included in the estate if a Chapter 7 had been filed in the first place. The concern was that a debtor would be worse off for having tried a repayment plan.

Before 1994, the courts divided. Some held that the date of the petition, rather than the date of conversion, controlled determinations of what assets were property of the estate. Thus, amounts acquired after the original petition's date, remaining in the trustee's hands at the time of conversion, were to be returned to the debtor. In *Bobroff v. Continental Bank (In re Bobroff)*, 766 F.2d 797 (3d Cir.1985), for example, the court held that § 1306 could be used to determine what comprises property of the estate; debtors would be reluctant to file Chapter 13 if property acquired during the course of the rehabilitation effort were subject to creditors' claims upon the failure of that effort. The court asserted that "no reason of policy suggests itself why the creditors should not be put back in precisely the same position as they would have been had the debtor never sought to repay his debts. *Id.* at 803. *See also In re Young*, 66 F.3d 376 (1st Cir. 1995).

Other courts held, however, that property the debtor owned at the time of conversion became property of the converted estate. The leading case taking this view, *In re Lybrook*, 951 F.2d 136 (7th Cir. 1991), expressed a belief that requiring post-petition income of the Chapter 13 estate to remain property of the estate upon conversion to Chapter 7 would prevent Chapter 13 from becoming a financial planning device debtors could use as a temporary respite from creditors. "[A] rule of once in, always in is necessary to discourage strategic, opportunistic behavior that hurts creditors without advancing any legitimate interest of debtors. . . . If [the debtor's] position deteriorates further it is the creditors who will bear the loss, while if he should get lucky and win a

lottery or a legal judgment, or inherit money . . . he will be able to keep his windfall" by converting to Chapter 7. *Id.* at 137-38. *See also Baker v. Rank (In re Baker)*, 154 F.3d 534 (5th Cir. 1998); *In re Calder*, 973 F.2d 862, 865-66 (10th Cir. 1992); *Resendez v. Lindquist*, 691 F.2d 397 (8th Cir. 1982).

Section 348(f)(1) was added in 1994 to resolve this question. Under § 348(f)(1)(A), property of the estate consists of property the debtor owned at the time the original Chapter 13 petition was filed, and still has at the time of conversion. The amendment was expressly designed to overrule *Lybrook* and to adopt the reasoning of *Bobroff*. H.R. Rep. No. 835, 103d Cong., 2d Sess. 57 (1994). Thus, post-petition earnings that constituted property of the Chapter 13 estate only because of the special rule of § 1306, will not be property of the post-conversion Chapter 7 estate.

In *Stamm v. Morton (In re Stamm)*, 222 F.3d 216 (5th Cir. 2000), debtors in separate cases, consolidated for appeal, filed Chapter 13 petitions and made payments from their earnings to the trustee, but were unable to confirm plans. After they converted to Chapter 7s, the Chapter 13 trustee turned over those payments to the Chapter 7 trustees, who sought a determination of whether the funds were the property of the Chapter 7 estates. The Fifth Circuit held that, under the plain language of § 348(f)(1)(A), wages, earned after the filing of a Chapter 13 and before conversion to Chapter 7 are not part of the Chapter 7 estate. Thus, the funds had to be returned to the debtors. *Accord, Alexander v. Jensen-Carter (In re Alexander)*, 236 F.3d 431 (8th Cir. 2001)

2. Cases involving bad faith

If the debtor converted in bad faith, the rules change. In such a case, property of the estate consists of property in the Chapter 13 case as of the date of conversion. § 348(f)(2). The Code, however, provides no definition of "bad faith."

In *In re Bejarano*, 302 B.R. 559 (Bankr. N.D. Ohio 2003), the debtors were in an automobile accident post-petition, resulting in their child's broken arm. In addition, they became entitled to tax refunds of over $4,000 during that period. They sought to convert the case to Chapter 7 and to exempt the refunds and the unliquidated personal injury claims.

The court noted that bad faith cannot be premised solely on the fact that a debtor acquired assets post-petition and then sought to take advantage of § 348(f). In the absence of a statutory definition, the court sought "the normal everyday meaning of the term." *Id.* at 562. Looking to a circuit case decided in a different context, the court held that bad faith "implies the conscious doing of a wrong because of dishonest purpose or moral obliquity; . . . it contemplates a state of mind affirmatively operating with furtive design or ill will." *Id.* (quoting *U.S. v. True*, 250 F.3d 410, 423 (6th Cir. 2001)). Application of this standard requires consideration of "any and all relevant factual circumstances." *Id.*

See also In re Doetsch 2007 BankrLexis 3161 (Bankr. NDNY Sep. 12, 07)

The facts cited by the trustee, in arguing that the debtors were trying to manipulate the bankruptcy process, included the tardiness of their motion to convert (made one day before the scheduled hearing on the trustee's motion to dismiss their Chapter 13 petition), their failure to make but one payment—of only $500—to the trustee despite pendency of their case for a year, failure to attend the third rescheduled meeting of creditors, the incurring of additional post-petition and pre-conversion debt, and the fact that this was their second Chapter 13 filing. The court found that these factors indicated, at the very least, that the debtors would never confirm a plan, much less carry it out. The factors also suggested that the debtors were trying to prolong the benefits of the automatic stay, knowing full well that they were unable to propose a confirmable plan. On the other hand, the personal injury claims were not acquired until well after the Chapter 13 petition was filed, so the debtors had not filed initially in an effort to deprive their creditors of that asset. And the fact that the debtors had been given an extended time to file a plan suggested that the debtors sincerely believed that they could formulate a viable plan. The most important factor relied upon by the court in finding no bad faith, however, was the small value of the assets involved. "[N]either of the assets at issue in this case are worth a significant amount of money to the Debtors. Moreover, on account of exemptions, such assets are likely worth even less to the Trustee. As such, the Court does not see a huge motive for the Debtors to manipulate the bankruptcy system." *Id.* at 563. The court held that the greater weight of the evidence supported the conclusion that the debtors did not convert their case in bad faith.

The court in *In re Siegfried*, 219 B.R. 581, 585 (D. Colo. 1998), applying a similar "all of the circumstances" test for bad faith, came to the opposite conclusion in light of the debtor's

> pattern of dissembling, failure to fully or accurately disclose financial affairs, disingenuous explanations of wrongful conduct and unfair manipulation of the bankruptcy system to the detriment of his creditors. This continuing pattern of lack of disclosure and procedural gymnastics, combined with an eleventh-hour conversion to another chapter to avoid imminent hearings on (1) objections to confirmation, including objections alleging lack of good faith; and (2) Debtor's eligibility under Section 109(e), is sufficient to find that this case was converted in bad faith.

Id. at 585-86.

B. Chapter 12 → Chapter 7

A similar problem arises when a Chapter 12 case is converted to Chapter 7 as when a Chapter 13 is originally filed—namely, that property acquired by the debtor post-filing and pre-conversion (generally, earnings) might become property of the converted estate, even though those assets would not have been included in the estate if a Chapter 7 had been filed in the first place. Unlike the situation when a Chapter 13 was originally filed, however, § 348(f) offers no solution when the original case was a Chapter 12; that provision is limited, by its terms, to Chapter 13s. Thus, the concern expressed by

Bobroff—that a debtor might be worse off for having tried a repayment plan under Chapter 12, facing the loss of property that would not have been in the estate if a Chapter 7 had been filed in the first place—remains a viable concern in this context.

C. Chapter 11 → Chapter 7

The debtor in *Patrick A. Casey, P.A. v. Hochman*, 963 F.2d 1347 (10th Cir. 1992), invented a medical device while in Chapter 11, before grant of a creditor's motion to convert the case to Chapter 7. The question was whether the device, its patent, and the income from a licensing agreement relating to the device were part of the Chapter 7 estate. Creditors argued that post-petition property is generally within the estate, with two exceptions—§ 541(a)(6), which deals with proceeds, etc., from property of the estate, and § 541(a)(5) which applies to certain types of property, acquired within 180 days of filing. The court responded that the creditors

> simply have the general rule backwards; under § 541(a)(1) the general rule is that the estate includes interests of the debtor in property as of the commencement of the case. Both of these provisions relied on (§ 541(a)(5) and (6)) are actually exceptions from the general rule that post-petition acquisitions are property of the debtor—exceptions specially provided to include particular property within the bankruptcy estate.

Id. at 1351. Thus, the court held that the property rights in the patent for the medical device did not become property of the Chapter 7 estate because those rights did not exist at the time of commencement of the case.

The Tenth Circuit decided *Calder*, which is cited above, shortly after *Hochman*. *Calder* dealt with the conversion of a Chapter 13 to a Chapter 7, and appears to have reached a conclusion that is incompatible with *Hochman*. In *Calder*, the Court held that all property in a debtor's Chapter 13 estate, including funds in the estate because of § 1306, are part of the post-conversion Chapter 7 estate. The Court disclaimed any inconsistency, however:

> In *Hochman*, this court held that when a *Chapter 11* case is converted to Chapter 7, the date of filing the original Chapter 11 petition determines what property constitutes the Chapter 7 estate. [963 F.2d] at 1350. Thus, property acquired *after* the filing of a Chapter 11 petition—which is *not* part of the Chapter 11 estate—continues *not* to be part of the bankruptcy estate upon conversion to Chapter 7. We agree with the Fifth Circuit that a conversion from Chapter 13 to Chapter 7 is distinguishable from a conversion from Chapter 11 to Chapter 7. *See Stinson v. Williamson (In re Williamson)*, 804 F.2d 1355, 1359-62 (5th Cir. 1986). The most important distinguishing factor is that in Chapter 11 there is no provision akin to 1306(a).

973 F.2d at 866 n.5

When the case is converted after confirmation of a plan, courts disagree regarding the question of what property remains in the Chapter 7 estate. Some hold that no property remains in the Chapter 7 estate; thus, the trustee has nothing to administer, because § 1141(b) vests all property of the estate in the debtor upon confirmation. In *Harker v. Troutman Enters. (In re Troutman Enters.)*, 253 B.R. 1 (6th Cir. BAP 2000), *vacated on other grounds*, 286 F.3d 359 (6th Cir. 2002), for example, the court observed that "[n]othing in the Code provides that the postconfirmation conversion of a Chapter 11 case to Chapter 7 alters the effect of § 1141(b) & (c)." 253 B.R. at 5. Under § 348(a), the date of the original Chapter 11 filing is treated as the date the Chapter 7 case was commenced. By that time, however, confirmation of the plan has vested the debtor with all property of the estate, § 1141(b). "Accordingly, no provision of the Bankruptcy Code provides for the property to revest in the estate upon conversion from Chapter 11 to Chapter 7 and there is no property in the Chapter 7 estate unless the plan specifically provides for property to remain in the estate." *Id.*

The property subject to dispute in *Harker* had not been disclosed in the debtor's schedules. The bankruptcy court relied on that fact in holding that the property had not vested in the reorganized debtor upon confirmation and, thus, had become property of the post-conversion Chapter 7 estate. The panel rejected that view, because § 1141(b) provides that *all* property of the estate vests in the reorganized debtor (unless the plan provides otherwise) and "[t]here is no explicit exception in the Code for undisclosed property." *Id.* at 6.

Other courts disagree, and hold that property vested in the debtor upon plan confirmation becomes property of the estate in the converted case. In *Bezner v. United Jersey Bank (In re Midway, Inc.)*, 166 B.R. 585 (Bankr. D.N.J. 1994), the issue was whether accounts receivable generated after plan confirmation were property of the post-conversion Chapter 7 estate. The court acknowledged that a "literal reading"—much like *Harker*'s, perhaps—could lead to the conclusion that, upon conversion, no property remains in the estate. The court asserted, however, that such a reading "ignores the provisions of chapter 7 providing for distribution of estate property." *Id.* at 590. The court also relied on cases dealing with the conversion of Chapter 13 cases to Chapter 7, either after confirmation of the plan or after the debtor has paid over funds to the trustee, holding that the estate included the debtor's interests in property as of the conversion date. These cases relied on § 348(d), which treats claims arising after confirmation of a Chapter 13 plan, but before conversion to Chapter 7, as prepetition claims in the Chapter 7 case. Thus, the court held that the estate consisted of the debtor's interests in property, including the accounts receivable, on the date the case was converted to Chapter 7. Of course, § 348(f)(1), which was effective after *Bezner* was decided, now undermines the analogy between claims and property that the court found persuasive.

II. Debtor's right to convert

A. Chapter 7 → Chapters 11, 12 or 13

As long as the Chapter 7 case was not previously converted from one of the reorganization chapters, § 706(a) gives debtors in Chapter 7 a one-time right to convert to one of the other chapters. The relevant portions of the legislative history state:

> Subsection (a) of this section [§ 706] gives the debtor the one-time absolute right of conversion of a liquidation case to a reorganization or individual repayment plan case. If the case has already once been converted from Chapter 11 or 13 to Chapter 7, then the debtor does not have that right. The policy of the provision is that the debtor should always be given the opportunity to repay his debts * * * .

S. Rep. No. 95-98,9 at 94, reprinted in 1978 U.S.C.C.A.N. 5787, 5880. *See also* H.R. Rep. No. 95-595, at 380, reprinted in 1978 U.S.C.C.A.N. 5963, 6336.

The question is whether the debtor's right to convert under § 706(a) is absolute, as the legislative history suggests. Several questions spring from this uncertainty.

1. Debtor's right to convert to a chapter for which he or she is ineligible

The first of these questions is whether a debtor, exercising this one-time "absolute" right, can convert to a chapter for which he or she is ineligible. Section 706(d) appears to prohibit such a conversion, yet an "absolute" right may mean just that. The debtor made such an argument in *Gulley v. DePaola*, 301 B.R. 361 (M.D. Ala. 2003), seeking to convert to Chapter 13 despite her lack of regular income. The court found some support for the debtor's position in the legislative history and in cases such as *Martin v. Martin*, 880 F.2d 857 (5th Cir. 1989), and *In re Carter*, 285 B.R. 61 (N.D. Ga. 2002). Even *Martin* and *Carter*, however, recognized that the right to convert could be denied in extreme or egregious circumstances:

> Courts which have determined that the conversion right is not absolute have reasoned that although the "absolute" nature of the right is said to derive from the language "at any time," those words do not mean "regardless of the circumstances," but instead refer literally to the time at which the motion to convert can be made, which is at any stage of the Chapter 7 case.

301 B.R. at 364. These courts adopted the position that the right to convert can be denied in appropriate circumstances, according to *Gulley*, in an effort to avoid holding that §§ 706(a) and (d) are in conflict. The court in *Gulley* relied on the plain meaning of § 706(d)—"that, regardless of what is provided in § 706(a), if a person is not eligible to be a debtor under the chapter to which she seeks to convert her case, she cannot convert her Chapter 7 case." *Id.* The court concluded that even if the legislative history supported the debtor's view, it would be relevant only if the statute language were unclear. *See also In re Evans*, 2004 Bankr. LEXIS 1156 (Bankr. M.D. Ala. 2004) (following *Gulley*).

2. Debtor's right to convert despite bad faith

The second of these questions is whether a debtor's lack of good faith provides the bankruptcy court appropriate grounds for denying the debtor's motion to convert.

Courts have taken two, distinctly different approaches. Some courts hold that the right to convert is absolute and unfettered (as long as the case has not been converted previously). These courts rely on the plain meaning of the statute—"may" and "at any time"—and the legislative history, quoted above.

In *In re Bowman*, 181 B.R. 836 (Bankr. D. Md. 1995), the debtor filed a no-asset Chapter 7 and got a discharge. On same day the final decree was entered, she amended her schedules to reflect a $400,000 civil claim. She asserted that the claim would pay all her creditors in full, and moved to dismiss her bankruptcy case. Rather than dismissing the case, the court vacated the final decree and directed the Chapter 7 trustee to investigate whether to pursue the claim on behalf of the estate. The trustee employed special counsel and received a settlement offer that would leave no surplus for the debtor. She objected to the settlement and sought to convert to Chapter 11, in order to pursue the claim.

The court looked to *In re Finney*, 992 F.2d 43, 45 (4th Cir. 1993), which held that a debtor has a one-time absolute right to convert, but "also found the facts justified the bankruptcy court's sua sponte consideration of whether an immediate reconversion under 11 U.S.C. § 1112(b) was warranted under the standards enunciated in *Carolin Corp. v. Miller*, 886 F.2d 693 (4th Cir. 1989)." *Bowman* concluded that debtors have a one-time absolute right to convert even if they have been recalcitrant or acted fraudulently. The debtor in this case had not acted so badly that the court could, under § 105, abrogate her statutory right to convert, although she had failed to disclose the claim—an asset—until after discharge and filed her motion to convert immediately after the trustee indicated his intent to accept the settlement offer. Clearly, however, the interests of the debtor directly conflicted with those of her creditors:

> Unlike the creditors who could lose payment of their claims entirely, the Debtor is in the enviable position of having little risk in pursuing the litigation. If she prevails in the litigation, there is a potential to recover a larger sum of money. If she loses most of her debts are discharged. The time factor of when the creditors will actually receive the money also adds an additional layer of risk for creditors. Pursuing the litigation will inevitably prolong distribution past the time set for trial. There may be further postponements due to discovery disputes, post-trial delay from an appeal, or difficulty in collecting on a judgment.

181 B.R. at 845 (citation omitted). Because that conflict of interest was inconsistent with the debtor's position as debtor-in-possession, the court concluded that it either had to appoint a trustee or reconvert the case to Chapter 7. Under Fourth Circuit authorities, *Carolin* and *Finney*, reconversion under § 1112(b) is appropriate when the facts show subjective bad faith on the debtor's part and that the reorganization effort is objectively futile. The court found the first prong satisfied by the circumstances surrounding the debtor's motion to convert, which suggested an improper purpose—namely, "not to

rehabilitate or reorganize, but to frustrate the process and gain control of the litigation herself at the last minute when the process was not going her way." *Id.* at 846. The second prong was satisfied because the debtor was trying to use Chapter 11 as "a safe haven for riskless litigation." *Id.* Thus, the court allowed conversion to Chapter 11, but immediately converted the case back to Chapter 7 for cause.

In *In re Martin*, 880 F.2d 857 (5th Cir. 1989), the situation was complicated by the fact that the debtor's motion to convert came after discharge had been granted. The court was undeterred:

> The statute itself, as we have noted above, speaks in absolute terms. An exhaustive review of the legislative history reveals nothing which would indicate that a post-discharge motion to convert should be treated differently from any other. Nothing in the cases serves to change this conclusion. Therefore, because the statute provides that the debtor has the right to convert "at any time" and because the parties to this appeal have not posed or briefed the question of what happens to the discharge, we hold simply that the denial of the conversion was improper. We do not reach the question of what happens to the discharge or the underlying debt when the motion to convert is granted after the discharge.

Id. at 859-60. *See also In re Gibbons*, 280 B.R. 833 (Bankr. N.D. Ohio 2002); *In re Widdicombe*, 269 B.R. 803 (Bankr. W.D. Ark. 2001).

Other courts hold that the debtor's right to convert is not absolute, although it should be denied only in egregious cases. If, upon a review of the facts, it appears that the debtor has made the request to convert in bad faith, or has attempted to abuse the bankruptcy process, these courts will deny conversion.

The court in *In re Marcakis*, 254 B.R. 77, 79 (Bankr. E.D.N.Y. 2000), pointed to the legislative history as the source of the erroneous view that the debtor's right to convert is absolute:

> [T]he legislative committee's choice of "absolute" in regard to Section 706(a) is infelicitous to say the least and has spawned an interpretation of the statute couched in hyperbolic terms very much at odds with the equitable considerations of eligibility, good faith and appropriateness which are inherent in a court's review of the facts and circumstances in any request brought on by motion.

In re Marcakis,.

The court in *In re Ponzini*, 277 B.R. 399 (Bankr. E.D. Ark. 2002), took a similar position, relying on *Marcakis*. *Ponzini* noted, first, that the plain meaning of § 706(a) does not give debtors an absolute right to convert a Chapter 7 case to another chapter:

> Section 706(a) does not contain the word "absolute" or any other word or phrase indicating that the right to convert is unequivocal. The courts finding that

> § 706(a) does provide an absolute right to convert have relied on the phrase "at any time" in § 706(a); however, it is more logical to interpret this phrase as referring to the debtor's right to convert at any point in the bankruptcy case's proceedings rather than granting the debtor a one-time absolute right to convert. "The words 'at any time' quite obviously mean that the debtor may seek a conversion at any time in the life of the case. However, 'at any time' is not the same as and does not mean 'regardless of circumstances.'" [*In re*] *Young*, 269 B.R. [816,] 822 [(Bankr. W.D. Mo. 2001)] (*quoting* [*In re*] *Starkey*, 179 B.R. [687,] 692 [(Bankr. N.D. Okla. 1995)]).

Id. at 404. More importantly, § 706(a) provides that the court "may" convert, which suggests that the right to convert "is presumptive rather than absolute." *Id.* The Rules requiring the filing of a motion to convert, notice and a hearing (Rules 1017(2), 9013 and 2002(a)(4)), provide additional evidence that the debtor's right to convert is not absolute. The legislative history spawned the idea that the right to convert is absolute, but its use of that word is not conclusive:

Although the right to convert is not absolute, the motion should be granted in the absence of "extreme circumstances amounting to an abuse of process." *Id.* at 405.

Other courts, like *Ponzini*, use a "totality of the circumstances" approach to determine what conduct is sufficiently egregious to justify denial of the debtor's motion to convert. In *In re Brown*, 293 B.R. 865 (Bankr. W.D. Mich. 2003), the court found sufficient bad faith in the debtor's "almost constant efforts to avoid the consequences of chapter 7 bankruptcy—namely the sale of" his residence. *Id.* at 871. The debtor had undervalued the property on his schedules, repeatedly failed to appear at § 341 meetings, and failed to pay the filing fee on time. When sale of the property became imminent, he refused to allow access to the trustee, the trustee's realtor or a prospective buyer, in the process ignoring court orders to the contrary. The court denied the debtor's motion to convert, finding that it was just another attempt to manipulate the bankruptcy process and avoid sale of the residence:

> Section 706(a) provides honest debtors with an [sic] one-time absolute right to convert their chapter 7 case to chapter 11 or 13 so that they may have the opportunity to pay off their debts. The "absolute" nature of the conversion right does not extend, however, to situations where conversion is sought as a means of thwarting the chapter 7 trustee's attempts to administer the bankruptcy estate or of escaping unintended consequences of a chapter 7 petition. In such circumstances, as here, the Debtor's motion to convert may be denied for lack of good faith.

Id.

B. Chapter 11→ Chapter 7

Section 1112 provides that a debtor may convert from Chapter 11 to Chapter 7 unless a trustee has been appointed, the case was an involuntary, or the case was previously converted to Chapter 11 by someone other than the debtor.

A party in interest, other than the debtor, may request that the court convert the case to Chapter 7. § 1112(b). Cause must be shown if the debtor is not serving as debtor-in-possession, the Chapter 11 case was an involuntary, or if the case was previously converted to Chapter 11 at the request of an entity other than the debtor. §§ 1112(a)(1) – (3).

In *Texas Extrusion Corp. v. Lockheed Corp. (In re Texas Extrusion Corp.)*, 844 F.2d 1142 (5th Cir.), *cert denied*, 488 U.S. 926 (1988), the debtor moved to convert her Chapter 11 case to a Chapter 7 one week before the scheduled hearing on plan confirmation. A creditor's motion to reconvert the case was granted, over the debtor's protest on due process grounds. The court observed that the debtor's absolute right to convert a Chapter 11 to a Chapter 7 does not carry the right to keep the case in Chapter 7. The bankruptcy court has discretion to decide whether to convert on the basis "of what will most inure to the benefit of all parties in interest." *Id.* at 1161. In this case, the bankruptcy court had not abused its discretion in reconverting the case:

> The motives of [debtor's] counsel in filing her motion to convert her case to a Chapter 7 liquidation one week prior to the confirmation hearing are questionable at best. The bankruptcy court was not unreasonable in finding the primary purpose of the conversion was to interfere with or impede the Chapter 11 reorganization of all four of the debtors. In addition, the same lawyers represented three of the four debtors and were fully conversant with all the facts of the case. Under these circumstances, the one day notice regarding reconversion does not appear to have been unreasonable. The Bankruptcy Code is flexible in allowing the bankruptcy court to fashion notice that is "appropriate in the particular circumstances." 11 U.S.C. § 102(1)(A). Finally, [debtor] did have a hearing on this issue at the beginning of the confirmation hearing. Overall, a review of the record convinces us that the bankruptcy court was properly exercising its discretion in reconverting [debtor's] case back to Chapter 11 and that [she] was not deprived of her due process rights by this action.

Id.

C. Chapter 11 → Chapter 12 or 13

Only the debtor can request conversion of a Chapter 11 case to either Chapter 12 or 13, and then only if the debtor has not been discharged under § 1141(d). Since discharge occurs upon confirmation of a plan, § 1141(d)(1)(A), the debtor can convert only pre-confirmation. In addition, if conversion to Chapter 12 is sought, the conversion must be equitable. § 1112(d)(3).

D. Chapter 12 → Chapter 7

Section 1208 gives the debtor a right to convert from Chapter 12 to Chapter 7 at any time. § 1208(a). Waivers of the right to convert are unenforceable. This right to convert is available to the debtor even if another party has moved for dismissal of the case. §§ 1208(c) & (d).

Other parties may seek the conversion only if the debtor has committed fraud in connection with the case. § 1208(d).

E. Chapter 12 → Chapter 11 or 13

The Code does not provide for the conversion of a Chapter 12 case to Chapter 11 or 13. Congress believed that such a conversion would only lead to delay, given that Chapter 12 is more protective of debtors who qualify for it than either of the other rehabilitation chapters. 172 Cong. Rec. S5557 (daily ed. May 7, 1986) (statement of Sen. Grassley).

Courts have divided on the question whether, in an exercise of their equitable powers, they can permit such a conversion. The court in *In re Orr*, 71 B.R. 639 (Bankr. E.D.N.C. 1987), permitted a debtor to convert from Chapter 12 to Chapter 11, because the debtor was ineligible for Chapter 12 but had nonetheless filed under that chapter in good faith:

> It would be entirely unfair to creditors to permit a debtor who was unsuccessful in chapter 12 to start anew in chapter 11 or chapter 13 after exhausting the chapter 12 process. Chapter 12 is designed to make confirmation of plans easier than confirmation of plans under chapter 11 and, in most cases, it would make no sense to allow a failed chapter 12 debtor to begin again in chapter 11 where confirmation is more difficult.
>
> There may, however, be situations when conversions from chapter 12 to chapter 11 or chapter 13 would not be unfair to creditors and the denial of conversion would be inequitable to the debtor. The case now before the court falls in that category. It is apparent that Mr. and Mrs. Orr filed their petition under chapter 12 in good faith believing that their aggregate debts did not exceed $1,500,000 and that they met the definition of "family farmer" under 11 U.S.C. § 101(17)(A) and the definition of "family farmer with regular annual income" under 11 U.S.C. § 101(18).

Id. at 642 (footnote omitted). The debtors' good faith, but erroneous, belief that they qualified for Chapter 12 was based on errors made by the creditor in both a loan balance provided to the debtors and in a state-court complaint.

Other courts follow a "plain meaning" approach and conclude that the Code prohibits such a conversion. One such decision is *In re Stumbo*, 301 B.R. 34 (Bankr. S.D. Iowa 2002):

> With respect to whether section 1208 permits conversion from Chapter 12 to Chapter 11, there is no controlling case law on point. Accordingly, the Court begins with a plain reading of the statute . . . and finds the answer is in the negative. That is especially clear when section 1208 is compared with similar sections found in Chapters 7, 11 and 13 of the United States Bankruptcy Code. If Congress had intended that a Chapter 12 debtor could convert the case to one under Chapter 11, it easily could have enacted a specific provision to that effect.
>
> In so holding, this Court recognizes there are courts that permit conversion from Chapter 12 to Chapter 11 regardless of the language of the statute or the legislative history as long as the equities of the case so warrant. The seminal case for that proposition appears to be *In re Orr*, 71 B.R. 639 (Bankr. E.D.N.C. 1987). A minority view, represented by *In re Christy*, 80 B.R. 361 (Bankr. E.D. Va. 1987), prefers to read section 1208 strictly and in light of the legislative history. Indeed, both decisions discuss the fact that an earlier version of Chapter 12 did provide for conversion to Chapter 11 or 13. *Orr*, 71 B.R. at 641-42; *Christy*, 80 B.R. at 362-63. Accordingly, but only as an alternative to a plain reading of the statute in the context of the United States Bankruptcy Code, this Court adopts the minority view. See also *Matter of Roeder Land & Cattle Co.*, 82 B.R. 536, 537 (Bankr. D. Neb. 1988)(noting Congress did not enact the draft of section 1208 that would have allowed conversion from Chapter 12 to Chapter 11 or 13 for cases filed under Chapter 12 mistakenly but in good faith).

Id. at 36-37 (footnotes omitted).

F. Chapter 13 → Chapter 7

Section 1307 gives the debtor a right to convert from Chapter 13 to Chapter 7 at any time. § 1307(a). Waivers of the right to convert are unenforceable. This right to convert is available to the debtor even if another party has moved for dismissal of the case. §§ 1307(c).

The court may convert a Chapter 13 case to Chapter 7 upon the request of the US Trustee or a party in interest, for cause, after notice and hearing. § 1307(c). The court may not convert the case without the debtor's consent, however, if the debtor is a farmer. § 1307(e).

G. Chapter 13 → Chapter 11 or 12

The court may convert a Chapter 13 case to Chapter 11 or 12, upon the request of the US Trustee or a party in interest, before confirmation of a plan. § 1307(d). The debtor who wants to convert must make the motion as a party in interest.

As with conversions from Chapter 13 to Chapter 7, the court may not convert from Chapter 13 to Chapters 11 or 12 without the debtor's consent, if the debtor is a farmer.

III. Court's power to convert

A. General rules

Any party in interest may request conversion of a case from one chapter to another, but such a conversion is not a matter of right. Only the debtor, however, can request conversion of a Chapter 7 or 11 case to a case under Chapter 12 or 13, §§ 706(c) & 1112(d)(1)—a sensible result, given that debtors cannot be subjected to Chapters 12 or 13 involuntarily. § 303(a).

Farmers enjoy more protection against involuntary conversion that do other debtors. A Chapter 11 case involving a farmer-debtor (or an eleemosynary institution) cannot be converted to a Chapter 7 unless the debtor requests it. § 1112(c). Nor can a farmer-debtor's Chapter 13 case be converted involuntarily. § 1307(e). The farmer in Chapter 12 may suffer involuntary conversion to Chapter 7 if the debtor has committed fraud in connection with the case. § 1208(d). The farmer in Chapter 7, however, is not protected from involuntary conversion of the case to Chapter 11.

B. Standard for conversion

1. Chapter 7 → 11, 12 or 13

The showing that is necessary in order to obtain such a conversion varies, depending on the chapter involved. Chapter 7, however, is silent on the standard to be applied by a court facing a motion to convert. Thus, the issue is left to the court's sound discretion.

2. Chapter 13 → 11 or 12

As with conversions from Chapter 7 to other chapters, the Code provides no standard to be applied by the court when conversion is sought from Chapter 13 to another rehabilitation chapter.

3. Chapter 12 →

Chapter 12 has no provision for involuntary conversion to another chapter, with one exception—conversion to Chapter 7 is permitted if the debtor committed fraud in connection with the case. § 1208(d). Otherwise, if cause is shown, the case may be dismissed. § 1208(c).

C. Bad faith

A case may be converted from Chapter 11 or 13 to Chapter 7 for "cause." §§ 1112(b) & 1307(c). The Code provides a nonexclusive list of reasons that constitute cause, most of which focus on failure of the reorganization effort. Most of the cases involve allegations of bad faith on the part of the debtor.

D. Use of dismissal to avoid conversion

One of the risks discussed above—that a debtor might be worse off for having tried a repayment plan under Chapter 12 (no longer a concern as to Chapter 13, given § 348(f)(1)(A)), if property is included in the post-conversion estate that would not have been included if a Chapter 7 had been filed in the first place—might be avoided if the debtor exercises the absolute right to dismiss under § 1208(b). Some courts have held, however, that there is no absolute right to dismiss if the debtor has committed fraud. In *Graven v. Fink (In re Graven)*, 936 F.2d 378 (8th Cir. 1991), for example, a farmer who had filed for Chapter 12 reorganization sought to have the petition dismissed pursuant to § 1208(b). Before the petition could actually be dismissed, however, one of the farmer's creditors sought conversion to Chapter 7, alleging with the support of overwhelming evidence that the farmer had fraudulently transferred all of his assets to family members and closely held corporations prior to filing the Chapter 12 petition. Notwithstanding the farmer's § 1208(b) motion to dismiss, the bankruptcy court converted the case as requested by the creditor. The district court affirmed and the farmer appealed to the Eighth Circuit, arguing that § 1208(b) requires immediate dismissal upon a debtor's request, regardless of motions filed by other parties or allegations of fraud.

The Court of Appeals recognized that the language of § 1208(b) seems to give a debtor an absolute right to dismiss a Chapter 12 petition voluntarily, and that § 1208(d) does not specifically state that a motion to convert by a creditor overrides a debtor's motion to dismiss. The court concluded, however, that Congress enacted the Bankruptcy Code to provide protection for honest debtors, "not to provide a shield for those who exploit the code's protection then seek to escape judicial authority when their fraudulent schemes are exposed." *Id.* at 385. To permit § 1208(b) to give debtors an absolute right to dismiss would render meaningless a court's power under § 1208(d), which was enacted to protect against exactly the types of abuses that had occurred in the case. The court upheld conversion of the case to a Chapter 7 proceeding pursuant to § 1208(d).

In a similar fact pattern (although not involving a question of property of the estate), however, the court in *Barbieri v. RAJ Acquisition Corp (In re Barbieri)*, 199 F.3d 616 (2d Cir. 1999), permitted dismissal. The debtor, who had contracted to sell an apartment building, filed a Chapter 13 petition in an effort to escape her contractual obligations when she found another buyer willing to pay a higher price. The bankruptcy court expressed its intention to convert the case to Chapter 7, but the debtor's attorney requested dismissal before the court's order was actually issued. The Second Circuit held that § 1307(b) gives debtors an absolute right to dismiss that is not limited by § 1307(c), as long as the case has not been converted. The court said that "concerns about abuse of the bankruptcy system do not license us to redraft the statute," and listed a number of

other ways that abuse of the bankruptcy process, if it occurs, can be curbed. *See also In re Davenport*, 175 B.R. 355 (Bankr. E.D. Cal. 1994).

In *Beatty v. Traub (In re Beatty)*, 162 B.R. 853 (9th Cir. BAP 1994), the court noted the division of authority on the question whether a bankruptcy court may grant a pending motion to convert the case for cause when the debtor has responded with a request for voluntary dismissal under § 1307 (b). *Compare In re Gillion*, 36 Bankr. 901 (E.D. Ark. 1983) (holding that the debtor's right to dismiss the case voluntarily is absolute, leaving the court no discretion to convert), *with In re Gaudet*, 132 Bankr. 670 (D.R.I. 1991) (holding that bankruptcy courts have authority to grant a pending motion to convert a Chapter 13 case despite the debtor's competing request to dismiss), and *In re Graven*, 936 F.2d 378 (8th Cir. 1991) (construing § 1208). Courts taking the latter view, according to *Beatty*, "reason that harmonizing section 1307(b) and 1307(c) leads to the conclusion that Congress could not have intended to allow the debtor to thwart a creditor's right to request conversion for cause by an unfettered power to voluntarily dismiss the case when faced with a conversion motion." 162 B.R. at 857. *Beatty*, however, adopted the former view:

> The better reasoned view is that a court must dismiss the case upon the debtor's request for dismissal under section 1307(b) if that request is made prior to the effective time of an order converting the case to Chapter 7. This view comports with the plain language of section 1307(c) which states that the court "shall" dismiss the case upon the debtor's request as well as the purposes of Chapter 13 and the voluntary nature of relief under that Chapter.

Id.