

**General Bankruptcy Law -- Multiple Choice**  
**50 Questions -- Choose Best Answer**  
**Total Time -- Two Hours Passing Score -- 30 Correct**

NOTE: The following questions and sample answers were prepared April 1999 and are based on the status of the law as of early 1999. Thus, while the sample answers will give you insight into how the examination was constructed, in some instances they may no longer reflect the prevailing view of the law. Since time is seldom a problem on this section of the exam, we suggest that you read each question carefully and that you choose your answer by eliminating the incorrect choices. This will force you to focus on the issues raised by the question. You will not be penalized for wrong answers, so you should answer every question, even if you are not certain of your answer. To receive a passing score, you must answer 60% correctly, or answer at least 30 questions correctly. You may not refer to the Code or any other material.

STAND ALONE QUESTION

- [1]<sup>1</sup> Bob Brother, Donna Debtor's brother, personally guaranteed Donna's consumer loan from the Big Bank. If the Donna Debtor files a petition in bankruptcy and receives a discharge of the Big Bank loan, then Bob Brother:
- a. will remain liable on his guarantee of the Big Bank loan because Donna's discharge does not affect the liability of third parties on the debt.
  - b. will remain liable on his guarantee of the Big Bank loan unless Donna filed her petition under Chapter 13 of the Bankruptcy Code.
  - c. will be relieved of liability on his guarantee of the Big Bank loan because the debt is a consumer debt.
  - d. will be relieved of liability on his guarantee of the Big Bank loan because Donna's discharge eliminated the underlying debt.

FACT PATTERN A [For Questions 2 & 3]

This morning Debtor Inc. filed a petition under Chapter 7 of the Bankruptcy Code. Although Debtor Inc. has been insolvent for the past two years, Sandy Shareholder, its sole shareholder and chief executive officer, has been struggling to keep the company afloat. As is common with many troubled enterprises, Debtor Inc. had failed to remit \$50,000 in employee "trust fund" withholding taxes. Several months ago Sandy was advised that the IRS was asserting against her the 100% penalty for those taxes since she was the "responsible party." Concerned about her personal liability, Sandy sent a \$50,000 check to the IRS with instructions to apply it to Debtor Inc. withholding tax liability. The check was

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<sup>1</sup>A is correct under §24(e). B and C refer to issues that might affect the co-debtor stay under §301, but that do not affect the discharge.

drawn on the general corporate checking account. The check cleared 110 days ago.

[2]<sup>2</sup> If the trustee attempts to recover the \$50,000 payment from the IRS, which of the following statements is the most accurate?

- a. The trustee will prevail because Sandy was an insider of Debtor Inc.
- b. The trustee will prevail because the check was drawn on the general corporate checking account.
- c. The IRS will prevail because the payment of withholding taxes is in the ordinary course of business.
- d. The IRS will prevail because there was no transfer of an interest in Debtor Inc.'s property.

[3]<sup>3</sup> If the trustee attempts to recover the \$50,000 payment from Sandy, which of the following statements is the most accurate?

- a. The trustee will prevail because Sandy was an insider of Debtor Inc.
- b. The trustee will prevail because Sandy was the entity for whose benefit the transfer was made.
- c. Sandy will prevail because Sandy was not a creditor of Debtor Inc.
- d. Sandy will prevail because the check cleared 110 days ago.

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<sup>2</sup>D is correct because it states the holding of Begier v. IRS, 110 S.Ct. 2258 (1990). B was rejected by Begier. A is incorrect both because of Beiger, and because Levit v. Ingersoll Rand Financial (In re Deprizio), 874 F.2d. 1186 (7th Cir. 1989), holds that 100% penalty is not the same debt as the corporation's tax debt. C is incorrect because this payment is not an ordinary course payment.

<sup>3</sup>C is correct under Levit v. Ingersoll Rand Financial (In re Deprizio), 874 F.2d. 1186 (7th Cir. 1989).

## STAND ALONE QUESTION

- [4]<sup>4</sup> Which of the following is not a "claim" under the Bankruptcy Code?
- As part of the debtor's criminal sentence, the state court ordered the debtor to pay restitution to the victim of the crime.
  - As part of an environmental enforcement action, the state court permanently enjoined the debtor from bringing additional industrial waste onto the waste site.
  - The "pain and suffering" of Verna Victim that resulted from a collision involving her car and the debtor's car. Verna filed suit alleging that the debtor was negligent, but the debtor has denied any negligence and has asserted that Verna was at fault in the collision. The suit had not yet come to trial when bankruptcy was filed.
  - Big Bank made a "non-recourse" loan to the debtor. Thus, although the loan is secured by a lien on the debtor's car, the debtor has no personal liability on the loan.

## FACT PATTERN B [For Questions 5 - 9]

Bankrupt Inc. filed a petition under Chapter 7 of the Bankruptcy Code last May 15th. Several years before then, Bankrupt Inc. had borrowed \$100,000 on an unsecured basis from the Lender. Under the terms of the loan agreement, the loan was to be repaid in monthly installments of \$1,000, due on the first day of each month. Since the payments were made by way of an automatic funds transfer from Bankrupt Inc.'s general corporate checking account, all payments were made on their due dates up to and including the May 1st installment payment (immediately before the bankruptcy). Nevertheless, Lender became concerned about Bankrupt Inc.'s deteriorating financial condition. As a result, Bankruptcy Inc.'s sole shareholder, Richie Rich, agreed to personally guarantee the Lender loan and to cause Bankrupt Inc. to grant the Lender a lien on Bankrupt Inc.'s inventory. The value of the inventory exceeded the outstanding loan balance. In addition, Richie Rich had sufficient assets to pay the debt in full if the guarantee was enforced. The security agreement was executed and Lender's security interest attached to the inventory 100 days before the bankruptcy petition was filed. The guaranty agreement was executed 80 days before the bankruptcy petition was filed. However, the UCC financing statement covering the inventory was misplaced by Lender's lawyer. The lawyer discovered the error on May 14th and the financing statement was properly filed on May 15th, exactly one hour after Bankrupt Inc. had filed its bankruptcy petition. Neither the lawyer nor Lender was aware of the bankruptcy filing when the financing statement was filed. (Assume that Article Nine ["Secured Transactions"] of the Uniform Commercial Code has been adopted in the relevant jurisdiction.)

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<sup>4</sup>B is not a claim under Ohio v. Kovacs, 105 S.Ct. 705 (1985). A is a claim under Pa. Dept. of Public Welfare v. Davenport, 110 S.Ct. 2126 (1990). C is a claim because §101 defines "claim" to include contingent, unliquidated, and disputed claims. D is a claim under Johnson v. Home State Bank, 111 S.Ct. 2150 (1991).

- [5]<sup>5</sup> If the trustee attempts to recover the May 1st installment payment to Lender, which of the following statements is the most accurate?
- a. The trustee will prevail because Richie Rich was an insider of Bankrupt Inc.
  - b. The trustee will prevail because the debt was a long-term loan rather than a short-term trade debt.
  - c. Lender will prevail because the \$1,000 payment did not enable it to receive more than it otherwise would have received because Richie Rich's guarantee assured it full payment.
  - d. Lender will prevail because the payment was made in the ordinary course of business.

- [6]<sup>6</sup> If the trustee institutes an adversary proceeding against Lender to recover the May 1st installment payment, which of the following statements is the most accurate?
- a. Lender will be entitled to a jury trial because an adversary proceeding is plenary in nature.
  - b. Lender will be entitled to a jury trial, but only if it has not filed a proof of claim against the estate.
  - c. Lender will not be entitled to a jury trial because the trustee's claim against Lender is equitable in nature.
  - d. Lender will not be entitled to a jury trial because the bankruptcy court is a court of equity.

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<sup>5</sup>D is correct under Union Bank v. Wolas, 112 S.Ct. 527 (1991). B was rejected by Wolas. C is incorrect because it is the payout in the bankruptcy case that controls. A is incorrect because Richie Rich's insider status is irrelevant.

<sup>6</sup>B is the best answer. It states the holding of Langenkamp v. Culp, 111 S.Ct. 330 (1990). Although D is a correct statement under Langenkamp, it is not as good an answer as B, because D would apply only if a proof of claim had been filed. A was the 10th Circuit's view that was rejected in Langenkamp. C is incorrect because under Granfinanciera v. Nordberg, 109 S.Ct. 2782 (1989), a preference claim for monetary relief is "legal."

- [7]<sup>7</sup> If the Lender decides to enforce the guaranty by instituting a legal action against Richie Rich, which of the following statements is the most accurate?
- a. Lender's action will violate the automatic stay because it is an attempt to collect a claim against Bankrupt Inc. that arose before the commencement of the bankruptcy case.
  - b. Lender's action will be enjoined under ' 105 because it will interfere with Richie Rich's ability to reorganize Bankrupt Inc.
  - c. Lender's action will not violate the automatic stay because Richie Rich has not filed a petition in bankruptcy.
  - d. Lender's action will not violate the automatic stay if the action against Richie Rich was necessary to prevent irreparable damage to the Lender.

- [8]<sup>8</sup> The filing of the financing statement by Lender's lawyer:
- a. violated the automatic stay because it perfected Lender's security interest in Bankrupt Inc.'s inventory.
  - b. violated the automatic stay because it enabled Lender to receive more than it otherwise would have received.
  - c. did not violate the automatic stay because it was accomplished before either Lender or its lawyer had notice of the bankruptcy.
  - d. did not violate the automatic stay because it merely perfected an interest in property that Lender had acquired before bankruptcy, and it was accomplished within 10 days of the filing of the bankruptcy petition.

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<sup>7</sup>C is correct. Co-debtor stays are provided only in Chapter 12 and 13 and only for consumer debts. See ¶201 & 1301. A is incorrect because 362(a)(1 & 6) only apply to actions "against the debtor." B is incorrect because this is a Chapter 7 case.

<sup>8</sup>A is correct under 362(a)(4). B is incorrect because preferential effect is not an element of a stay violation. C is incorrect because knowledge is not an element of a stay violation. D is incorrect because this is not a case where the trustee is subject to the earlier perfection under ¶546 and because the 10-day period under ¶547(e) runs from the date of attachment.

- [9]<sup>9</sup> If the Trustee attempts to avoid Lender's lien on Bankrupt Inc.'s inventory, which of the following statements is the most accurate?
- a. The trustee will prevail because Bankrupt Inc. received no value from Lender in exchange for the lien.
  - b. The trustee will prevail because the lien was not yet perfected at the time the petition in bankruptcy was filed.
  - c. Lender will prevail because the lien attached to Bankrupt Inc's inventory 100 days before the petition in bankruptcy was filed.
  - d. Lender will prevail because Lender acquired its lien before bankruptcy, and perfection occurred within 10 days of the filing of the bankruptcy petition.

FACT PATTERN C [For Questions 10 - 16]

Nine months ago, Lazy Loan Co. obtained a \$50,000 judgment against Don Debtor in the Circuit Court of Main County. The debt arose out of a consumer loan made to Don several years earlier. Eight months ago, Lazy Loan recorded the judgment by filing an "abstract of judgment" with the Main County Recorder of Deeds. Under the relevant state's judgment lien statute, that action gave Lazy Loan a judgment lien on all real estate owned by Don in Main County. At that time, the only Main County real estate owned by Don was Blackacre. For several years, Don had lived in an apartment downtown and had leased Blackacre to Tina Tenant. Eleven months ago, Tina's lease expired and she vacated the premises. Ten months ago, Don moved out of his downtown apartment and moved into Blackacre, establishing it as his homestead. Although the relevant state has "opted out" of the Federal exemption scheme under '522(d), state law allows individuals a homestead exemption of \$100,000. However, under the relevant state law, the homestead exemption can not be asserted against a debt like the Lazy Loan Co. debt that arose before the property became a homestead. Blackacre is worth only \$50,000.

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<sup>9</sup>B is correct because '544(a)(1) allows the trustee to avoid unperfected security interests. Thus, C is incorrect. A is incorrect because value is not relevant under the '544 strong arm power. D is incorrect because this is not a case where the trustee is subject to the earlier perfection under '546.

[10]<sup>10</sup> If Don files a petition under Chapter 7 of the Bankruptcy Code today, which of the following statements is the most accurate?

- a. Don can avoid Lazy Loan's lien on Blackacre because Don received no value from Lazy Loan in exchange for the creation of the lien within the year preceding bankruptcy.
- b. Don can avoid Lazy Loan's lien on Blackacre because it impairs the homestead exemption to which Don otherwise would have been entitled.
- c. Don can not avoid Lazy Loan's lien on Blackacre because Blackacre did not become Don's homestead until after the Lazy Loan Co. debt arose.
- d. Don can not avoid Lazy Loan's lien on Blackacre because the lien is a "statutory lien" created by a state statute, rather than a "judicial lien" created by judicial action.

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<sup>10</sup>B is correct under Owen v. Owen, 111 S.Ct. 1833 (1991), because the judicial lien "fixed" upon an interest that would otherwise have been exempt. A is incorrect because "value" under §48(d)(2)(A) includes the securing of an antecedent debt. C is incorrect under Owen because the test is not whether the property actually is exempt from the particular claim, but whether it would be exempt but for the lien. D is incorrect because the lien is a ? judicial lien? and not a "statutory lien" under §01.

[11]<sup>11</sup> For this question only, assume that Don files a petition under either Chapter 11 or Chapter 13, assume that Lazy Loan's lien can not be avoided, and assume that Lazy Loan objects to the treatment of its claim under Don's plan. Don's plan can still be confirmed:

- a. if the plan surrenders Blackacre to Lazy Loan on the effective date of the plan.
- b. if the plan allows Lazy Loan to retain its \$50,000 lien on Blackacre and proposes to pay Lazy Loan \$50,000 in a lump sum payment on the fifth anniversary of the effective date of the plan.
- c. if the plan allows Lazy Loan to retain its \$50,000 lien on Blackacre and proposes to pay Lazy Loan \$50,000 in twelve consecutive equal monthly installments of \$4,166.67 each, beginning one month after the effective date of the plan ( $\$4,166.67 \times 12 = \$50,000$ ).
- d. both (a) and (c) are correct.

ADDITION TO FACT PATTERN C [For Questions 12 - 16]

In addition to the \$50,000 Lazy Loan debt, Don owes \$10,000 on an unsecured loan to Betty Bestfriend, \$1,000 each to ten separate department stores on unsecured charge account debts, and \$20,000 on an unsecured loan to Ellen Exfriend, Don's former girlfriend. All of those debts are consumer debts. In addition, although Tina Tenant left Blackacre in perfect condition, Don has not yet returned her \$5,000 security deposit. As required by the relevant state landlord/tenant law, Don deposited the security deposit into a special non-interest bearing trust account at the bank. The account is titled in "Don Debtor, as trustee for Tina Tenant, tenant of Blackacre." In addition, Don has a personal savings account at the bank with a balance of \$100,000, and a \$2.00 lottery ticket for next week's drawing of Pennsylvania State Lottery (the jackpot is \$23,000,000). He owns no other property (except Blackacre -- worth \$50,000).

For the last several months, Don has not been making the scheduled payments on any of his debts, except the debt owed to Betty Bestfriend (all payments to Betty have been made promptly when due, but \$10,000 is still owed). Five months ago, Ellen Exfriend filed suit against Don to collect the \$20,000 owed to her. Although Don has disputed Ellen's claim and raised several defenses in that legal action, he acknowledged in his discovery deposition that the only reason he was disputing the debt was because he was mad at Ellen for breaking up with him. Ellen has moved for summary judgment, and your review of the file convinces you that the summary judgment motion is certain to be granted.

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<sup>11</sup>A is correct. Both B and C are incorrect because neither proposal includes interest, thereby violating the "present value" requirements of both the Chapter 11 and Chapter 13 secured creditor cram down provisions.

[12]<sup>12</sup> If Don wishes to file bankruptcy, which of the following statements is the most accurate?

- a. Don is eligible to file a petition under Chapter 13, but only if he has regular income.
- b. Don is not eligible to file bankruptcy because the value of his assets exceeds the amount of his debts.
- c. Don is not eligible to file a petition under Chapter 11, unless he is engaged in business.
- d. both (a) and (c) are correct.

[13]<sup>13</sup> If Don files a petition in bankruptcy, which of the following statements is the most accurate?

- a. Don's estate will include Blackacre because it is Don's principal residence.
- b. Don's estate will not include Blackacre because Don has no equity in Blackacre.
- c. Tina Tenant will be entitled to receive the \$5,000 security deposit because she has the equitable title to the bank account.
- d. Tina Tenant will not be entitled to receive the \$5,000 security deposit because Don has the legal title to the bank account.

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<sup>12</sup>A is correct. B is incorrect because there is no insolvency requirement under the Code. C was rejected in Toibb v. Radloff, 111 S.Ct. 2197 (1991). Thus, D is incorrect.

<sup>13</sup>C is correct because §41(d) limits the estate's interest in the account to Don's bare legal interest as trustee. Thus, D is incorrect. A is incorrect because the fact that the property is Don's principal residence is not the reason that it is included in the estate. B is incorrect because equity is not required in order for a lien asset to be included in the estate.

[14]<sup>14</sup> If Don files bankruptcy this morning and if Don's lottery ticket is the winning ticket at next week's drawing of the Pennsylvania State Lottery, which of the following statements is the most accurate?

- a. The lottery winnings would be property of Don's bankruptcy estate because Don purchased the lottery ticket before the involuntary petition was filed.
- b. The lottery winnings would be property of Don's bankruptcy estate because the drawing took place within 180 days after the involuntary petition was filed.
- c. The lottery winnings would not be property of Don's bankruptcy estate because the drawing did not take place until after the involuntary petition was filed.
- d. The lottery winnings would not be property of Don's bankruptcy estate because the assets that were already in the estate before the drawing were sufficient to satisfy all claims in full.

[15]<sup>15</sup> If Don's creditors commence an involuntary bankruptcy case against him, the bankruptcy court:

- a. will order relief against Don because he is not making current payments to any creditor except Betty.
- b. will order relief against Don because he has more than twelve unsecured creditors.
- c. will not order relief against Don because involuntary relief is not available against a debtor who is not a moneyed, business, or commercial corporation.
- d. will not order relief against Don because involuntary relief is not available against a debtor who is not insolvent.

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<sup>14</sup>A is correct because the ticket itself was property of the estate and §41 includes proceeds of property of the estate in the estate. Thus, C is incorrect. B is incorrect because the 180 day rule only applies to inheritance, life insurance and marital property settlements. D is incorrect because the asset-to-debt ratio is not relevant to the "property of the estate" determination.

<sup>15</sup>A is correct because one ground for involuntary relief under §303(h) is that the debtor is generally not paying such debtor's debts as they become due. Thus, D is incorrect because balance sheet insolvency is not required. C is incorrect because that limitation applies only to corporations. B is incorrect because the number of creditors is not a limitation on the availability of involuntary relief; it merely determines how many creditors must join in the petition.

[16]<sup>16</sup> Assume that the bankruptcy court will order relief against Don if a proper involuntary petition is filed under ' 303 of the Bankruptcy Code. The petition will be successful if:

- a. Lazy Loan and Ellen Exfriend join in the petition.
- b. Ellen Exfriend, Betty Bestfriend, and one of the department stores join in the petition.
- c. three of the department stores join in the petition.
- d. Tina Tenant, alone, files the petition.

#### STAND ALONE QUESTION

[17]<sup>17</sup> One month before bankruptcy, Donna Debtor paid Linda Lawyer a flat fee of \$2,000 to handle her Chapter 7 bankruptcy. Linda counseled Donna about her financial problems and prepared and filed a Chapter 7 petition and related schedules. Since the full fee was paid in advance, Linda did not seek compensation from the bankruptcy estate under ' 330 of the Bankruptcy Code. Although the legal services provided by Linda were beneficial to Donna, the reasonable value of the services was only \$1,500. Further, although Linda=s services were beneficial to Donna, they were of no benefit to the Chapter 7 estate. Which of the following statements is the most accurate?

- a. Linda Lawyer may keep the entire fee payment because the fee was not paid from property of the Chapter 7 estate.
- b. Linda Lawyer may keep the entire fee payment because it was paid before the services were rendered.
- c. Linda Lawyer can be required to return \$500 because the fee payment exceeded the reasonable value of the services to Donna by that amount.
- d. Linda Lawyer can be required to return the entire fee payment because the services were of no benefit to the Chapter 7 estate.

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<sup>16</sup>B is correct because '303 requires at least three creditors because Don has more than twelve creditors. That requirement eliminates A and D. C is incorrect because the unsecured portion of the petitioning creditor's claims must exceed \$10,775 (in 1999). Finally, the dispute with Ellen is not "bona fide" and the fact that the payments to Betty are current does not prevent her from joining the petition under '303.

<sup>17</sup>C is correct because '329(b) gives the court power to review attorney's fees paid within one year prior to bankruptcy, even though the fee was paid by a third party and even though the attorney has not applied for compensation. Thus, A is incorrect. B is incorrect because it focuses on a preference element that is not relevant under '329. D is incorrect because benefit to the estate is not relevant because the fees were not paid from the estate.

FACT PATTERN D [For Questions 18 - 20]

Don Debtor owes \$500,000 in non-contingent, liquidated, unsecured debts and, in addition, owes Big Bank \$250,000 on a purchase-money mortgage loan secured by his home. Five months ago, Don filed a petition under Chapter 7 of the Bankruptcy Code. As of the time of filing, Don's home had dropped in value to only \$100,000.

[18]<sup>18</sup> In Don's Chapter 7 case:

- a. Big Bank's secured claim will be \$250,000.
- b. Big Bank's secured claim will be \$150,000.
- c. Big Bank's unsecured claim will be \$250,000.
- d. Big Bank's unsecured claim will be \$150,000.

ADDITION TO FACT PATTERN D [For Questions 19 - 20]

A month ago, Don received a discharge under § 524 of the Bankruptcy Code. The Chapter 7 trustee had filed a "no asset" report, so there was no distribution to creditors.

[19]<sup>19</sup> Don's discharge will:

- a. enjoin the Big Bank from attempting to collect its claim by foreclosing on Don's home.
- b. enjoin the Big Bank from attempting to collect its claim by garnishing Don's next paycheck.
- c. not enjoin Big Bank's collection activity because there was no distribution to creditors.
- d. not enjoin Big Bank's collection activity because the Bankruptcy Code provides special protection to claims secured by real estate that is the debtor's principal residence.

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<sup>18</sup>D is correct because § 506(a) bifurcates an under-secured creditor's claim into secured and unsecured portions. Here Big Bank will have two claims: an unsecured claim of \$150,000, and a secured claim of \$100,000.

<sup>19</sup>B is correct because the discharge only enjoins enforcement of claims as a personal liability of the debtor. Thus, A is incorrect because the discharge does not prevent enforcement of the mortgage lien. C is incorrect because the amount of distribution is irrelevant to the discharge question. D is incorrect because the special treatment of home mortgages does not apply in Chapter 7 cases.

[20]<sup>20</sup> If Don filed a petition under Chapter 13 today, which of the following statements is the most accurate?

- a. Don=s petition would be dismissed because serial filings are prohibited.
- b. Don=s petition would be dismissed if filed in bad faith.
- c. Big Bank's surviving rights against Don and his property would not constitute a "claim" under the Bankruptcy Code.
- d. Don would be ineligible for Chapter 13 because of the \$500,000 in non-contingent, liquidated unsecured debts.

### STAND ALONE QUESTION

[21]<sup>21</sup> Assume that Don Debtor is an individual and that both he and Pam Partner are general partners in the law firm of Partner & Debtor. In addition, Don Debtor owns 10 percent of the outstanding stock in Corporation Inc. If Don Debtor files bankruptcy, which of the following is not necessarily an "insider" under the Bankruptcy Code?

- a. The firm of Partner and Debtor.
- b. Pam Partner.
- c. Pam Partner's son.
- d. Corporation Inc.

### FACT PATTERN E [For Questions 22 & 23]

Fred Fraud set up a corporation named Frauds R Us Inc. to operate a "ponzi" scheme. Under the scheme, Fred would promise extremely high returns in order to persuade investors to invest their life savings with Frauds R Us Inc. In order to keep the scheme going, Frauds R Us Inc. would use the money from later investors to pay off the earlier investors. Ultimately the scheme collapsed and the defrauded investors filed separate class actions against both Fred and Frauds R Us, Inc. in state court.

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<sup>20</sup>B is correct under Johnson v. Home State Bank, 111 S.Ct. 2150 (1991). Johnson also rejects both A and D. C is incorrect because those debts were discharged in the prior Chapter 7 case.

<sup>21</sup>D is correct. Under §101, the partnership, his general partner, and his general partner's relative are all insiders. Thus, A, B, & C are incorrect. Although the insider definition also includes "affiliates", §101 defines affiliate to require that the debtor hold at least 20 percent of the corporation's stock.

The Frauds R Us Inc. suit has not yet been set for trial. The suit against Fred did go to trial and the jury found that Fred had engaged in fraud and awarded damages against him and in favor of the investor-plaintiffs. Under the relevant state law, the preponderance of the evidence standard applies in fraud actions. Fred did not appeal, and the judgment became final several months ago. Last week, one of the investor-plaintiffs garnished Fred's bank account. Both Fred and Frauds R Us Inc. immediately filed petitions under Chapter 7 of the Bankruptcy Code.

[22]<sup>22</sup> In the Frauds R Us Inc. Chapter 7 case, the claims of the investors:

- a. will be discharged because Frauds R Us Inc. is a corporation.
- b. will be discharged because the suit was still pending and the claims were unliquidated at the time the petition in bankruptcy was filed.
- c. will not be discharged because Frauds R Us Inc. obtained the investors' funds through actual fraud.
- d. will not be discharged because Frauds R Us Inc. is a corporation.

[23]<sup>23</sup> Assume that one of the investor-plaintiffs in the state court action asserts that Fred's debt to the investor is non-dischargeable because of fraud. Which of the following statements is the most accurate?

- a. The state court finding of fraud will be given collateral estoppel effect in the dischargeability action because the discharge is limited to honest debtors.
- b. The state court finding of fraud will be given collateral estoppel effect in the dischargeability action because the "preponderance of the evidence" standard applies to such non-dischargeability actions.
- c. The state court finding of fraud will not be given collateral estoppel effect in the dischargeability action because the state court finding was based on the "preponderance of the evidence" standard of proof, rather than the "clear and convincing" standard.
- d. The state court finding of fraud will not be given collateral estoppel effect in the dischargeability action because the usual collateral estoppel rules do not apply in bankruptcy.

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<sup>22</sup>D is correct because 727(a)(1) limits the Chapter 7 discharge to individuals. Thus, A is incorrect. B is incorrect because the Code's expansive definition of "claim" includes unliquidated claims. C is incorrect because the 523 exceptions to discharge apply only to individuals.

<sup>23</sup>B is correct under Grogan v. Garner, 111 S.Ct. 654 (1991). C and D were rejected by Grogan.

## STAND ALONE QUESTION

[24]<sup>24</sup> If a Chapter 11 debtor receives a discharge, the debts are discharged:

- a. when the plan is confirmed, whether or not the debtor makes any of the scheduled payments under the plan.
- b. when the first payment is made under the plan, whether or not the debtor makes any of the additional scheduled payments under the plan.
- c. when there has been substantial consummation of the plan.
- d. when all of the scheduled payments under the plan have been made.

## FACT PATTERN F [For Questions 25 - 29]

This morning Donna Debtor filed a petition under Chapter 7 of the Bankruptcy Code. Three years ago, Donna fraudulently conveyed Blackacre to her mom. However, she made no attempt to conceal the transfer, believing correctly that her creditors were too unsophisticated to attack the transfer. Under the relevant state fraudulent conveyance law, only those creditors who held claims against Donna at the time of the transfer can avoid it as fraudulent. A five-year statute of limitations applies to such actions. Two years ago, Donna's fortunes improved briefly and she paid off all of her old creditors except Connie Creditor, who still holds a \$3,000 unsecured claim against Donna. Since then, Donna's financial situation has deteriorated, and she now owes a total of \$100,000 in unsecured debt (including Connie's claim). Assume that Blackacre is worth \$50,000.

[25]<sup>25</sup> If the Chapter 7 trustee attacks the transfer of Blackacre to mom, which of the following statements is the most accurate?

- a. The trustee can recover only \$3,000 because that is the amount of Connie Creditor's claim.
- b. The trustee can recover \$50,000 because Connie Creditor's claim is an allowable unsecured claim.
- c. The trustee can not avoid the transfer because it occurred more than one year ago.
- d. The trustee can not avoid the transfer because the avoidance action belongs to Connie

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<sup>24</sup>A is correct under §141(d)(1)(A). Thus, B, C, and D are incorrect.

<sup>25</sup>B is correct because §544(b) allows the trustee to avoid any transfer that is voidable by a creditor holding an allowable unsecured claim. Thus, D is incorrect. A is incorrect because §544 does not limit the avoiding power to the amount of the creditor's claim. C is incorrect because the one-year limitation applies only under §548.

Creditor and can not be asserted by the estate.

[26]<sup>26</sup> If the trustee objects to Donna's discharge under '727 on the basis of the fraudulent transfer to mom, which of the following statements is the most accurate?

- a. The discharge will be denied because the bankruptcy discharge is available only to an "honest debtor," and Donna's fraudulent intent shows that she is not honest.
- b. The discharge will be denied because Donna did not purge the fraud by reversing the transfer prior to filing her petition in bankruptcy.
- c. The discharge will be granted because only Connie Creditor has standing to raise an objection to discharge based on that ground.
- d. The discharge will be granted because the transfer occurred more than one year ago.

ADDITION TO FACT PATTERN F [For Questions 27 - 29]

Donna also owes the IRS \$10,000 for income taxes from two years ago. Donna properly filed the tax return on April 15th of last year showing that the \$10,000 in taxes were due. However, she has not yet paid them, despite demand by the IRS. Although the IRS attempted to file a tax lien against Donna two months ago, the local agent got confused and filed it in the wrong county.

[27]<sup>27</sup> Assume that the IRS receives notice of Donna's bankruptcy, but fails to file a timely proof of claim for the tax debt. Which of the following statements is the most accurate?

- a. The tax debt will be discharged.
- b. The tax debt will be subordinated to all timely filed claims.
- c. The doctrine of sovereign immunity will prevent the bankruptcy court from dealing with the tax debt.
- d. The Chapter 7 trustee may file a proof of claim for the tax debt.

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<sup>26</sup>D is correct because 727(a)(2) is limited to transfers within one year before bankruptcy. Further, since Donna did not conceal the transfer, the fraud can not be considered to have continued into the one-year period.

<sup>27</sup>D is correct under '501(c). A is incorrect because the tax debt is less than three years old. B is incorrect because priority claims are not subordinated even if tardily filed under '726(a)(1). C is incorrect because '106 waives federal sovereign immunity.

[28]<sup>28</sup> If the IRS asserts a tax lien against any property of the estate, which of the following statements is the most accurate?

- a. The trustee could avoid the tax lien because it was filed less than 90 days ago.
- b. The trustee could avoid the tax lien because it was filed in the wrong county.
- c. The trustee could not avoid the tax lien because it is a Astatutory lien.@
- d. The trustee could not avoid the tax lien because it secures a tax debt that is less than three years old.

[29]<sup>29</sup> Assume that the trustee recovers Blackacre (value = \$50,000) and \$10,000 in additional assets, for a total estate of \$60,000. Assume that Donna claims no exempt property. Also assume that the bankruptcy court allows the trustee reasonable compensation of \$1,000, and that there are no other administrative expenses. Finally, assume that all creditors file timely proofs of claim, and that the IRS tax lien is avoided by the trustee. Donna's estate will be distributed in the following order of priority:

- a. first, the trustee will receive \$1,000; second, the IRS will receive \$10,000; third, Connie Creditor will receive \$3,000; and fourth, the creditors holding the remaining \$97,000 in unsecured claims will share the remaining \$46,000 pro rata.
- b. first, the trustee will receive \$1,000; second, the IRS will receive \$10,000; and third, Connie Creditor and the creditors holding the remaining \$97,000 in unsecured claims will share the remaining \$49,000 pro rata.
- c. first, the trustee will receive \$1,000; second, the IRS, Connie Creditor, and the creditors holding the remaining \$97,000 in unsecured claims will share the remaining \$59,000 pro rata.
- d. the trustee, the IRS, Connie Creditor, and the creditors holding the remaining \$97,000 in unsecured claims will all share \$60,000 pro rata.

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<sup>28</sup>B is correct under the §45(2) power to avoid unperfected statutory liens. Thus C is incorrect. A is incorrect both because the filing was ineffective and because §47(c)(6) would have protected it from attack had it been effective. D incorrectly focuses on a tax discharge factor that has no application to lien avoidance.

<sup>29</sup>B is correct. The trustee's fee comes first under §07(a)(1). The tax debt falls within the three-year period under §07(a)(7), so it comes next. All other unsecured claims come after the §07 claims and share pro rata under §26(a)(2) & (b), even though Connie's status was used to recover Blackacre.

## STAND ALONE QUESTION

[30]<sup>30</sup> Absent an extension, if you wish to take an appeal from a bankruptcy court judgment in a core proceeding, your notice of appeal must be filed:

- a. within ten days of entry of the judgment.
- b. within twenty days of entry of the judgment.
- c. within thirty days of entry of the judgment.
- d. within ninety days of entry of the judgment.

## FACT PATTERN G [For Questions 31 - 35]

Five years ago, Debtor Inc. entered into a lease of office space with Lessor Inc. The term of the lease was ten years, and the monthly rental of \$10,000 was due on the first of each month. The lease agreement absolutely prohibited any assignment of Debtor Inc.'s rights under the lease, and prohibited any subletting of the premises. Those provisions were valid and enforceable under the relevant state law. In addition, the lease agreement expressly provided that the filing of a petition in bankruptcy was a default, automatically terminating the lease and entitling Lessor Inc. to immediate possession of the premises. Debtor Inc. missed the lease payment due on the 1st day of last month. On the 15th day of last month, Debtor Inc. filed a petition under Chapter 11 of the Bankruptcy Code. Under the lease agreement, the failure to make a lease payment when due constitutes a default, giving Lessor Inc. the option to terminate the lease upon written notice to Debtor Inc. Lessor Inc. has taken no action with respect to Debtor Inc.'s missed payment.

[31]<sup>31</sup> Which of the following statements is the most accurate?

- a. Debtor Inc.'s bankruptcy estate includes its rights under the lease because those rights were legal interests of Debtor Inc. in property on the 15th day of last month.
- b. Debtor Inc.'s bankruptcy estate does not include its rights under the lease because of the provision in the lease agreement prohibiting assignment.
- c. Debtor Inc.'s bankruptcy estate does not include its rights under the lease because Debtor Inc. is in default because it missed the lease payment due on the 1st day of last month.

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<sup>30</sup>A is correct because Bankr. Rule 8001(a) requires a timely notice of appeal and Bankr. Rule 8002(a) sets a 10-day time period. All other answers are incorrect because they reflect other commonly used time periods under the Federal Rules.

<sup>31</sup>A is correct under §541(a)(1). B and D are rejected by §541(c)(1). C is incorrect because the payment default did not terminate Debtor Inc.'s interest under the lease.

d. Debtor Inc.'s bankruptcy estate does not include its rights under the lease because Debtor Inc. is in default because it filed a petition in bankruptcy.

[32]<sup>32</sup> Assume that the Debtor Inc. has the ability to perform its future obligations under the lease. If Debtor Inc. wishes to continue using the leased premises, which of the following statements is the most accurate?

- a. Debtor Inc. can assume the lease over Lessor Inc.'s objection if it promptly pays Lessor Inc. \$10,000.
- b. Debtor Inc. can assume the lease over Lessor Inc.'s objection if it promptly dismisses its bankruptcy case.
- c. Debtor Inc. can not assume the lease over Lessor Inc.'s objection because Debtor Inc. is in default for filing bankruptcy.
- d. Debtor Inc. can not assume the lease over Lessor Inc.'s objection because Debtor Inc. is in default for failing to make the lease payment due on the 1st day of last month.

[33]<sup>33</sup> Assume that during the first three months after the case was filed the management of Debtor Inc. was pre-occupied with other matters and took no action with respect to the lease other than to make the regularly scheduled post-petition monthly lease payments. Which of the following statements is the most accurate?

- a. Debtor Inc. can assume or reject the lease at any time before the confirmation of its plan, unless the court orders otherwise.
- b. Debtor Inc. is deemed to have assumed the lease by making the current monthly payments.
- c. Debtor Inc. can not assume the lease because it is deemed rejected.
- d. Debtor Inc. can not assume the lease because it is too late to promptly cure defaults.

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<sup>32</sup>A is correct under §365(b)(1). Thus, D is incorrect. B and C are incorrect because "bankruptcy default" clauses need not be cured. See §365(b)(2).

<sup>33</sup>C is correct because a non-residential real estate lease is deemed rejected after 60 days under §365(d)(1). The rule stated in A applies only to residential real estate and personal property leases. B is incorrect because the mere continuation of payments does not constitute an assumption. D is incorrect because, but for C, three months would not be too late to cure defaults.

[34]<sup>34</sup> Assume that under the relevant state law, when a lease is breached, the lessor has no duty to mitigate damages, but is entitled to damages equal to the full amount of rent to be paid for the remainder of the original lease term. If Debtor Inc. rejects the lease immediately after filing bankruptcy, and if five years remain of the original lease term, then:

- a. Lessor Inc. will have an administrative expense claim equal to five year's rent under the lease (not considering the unpaid lease payment that was due on the 1st day of last month).
- b. Lessor Inc. will have an administrative expense claim equal to one year's rent under the lease (not considering the unpaid lease payment that was due on the 1st day of last month).
- c. Lessor Inc. will have a general unsecured claim equal to five year's rent under the lease (not considering the unpaid lease payment that was due on the 1st day of last month).
- d. Lessor Inc. will have a general unsecured claim equal to one year's rent under the lease (not considering the unpaid lease payment that was due on the 1st day of last month).

[35]<sup>35</sup> If Debtor Inc. assumes the lease, which of the following statements is the most accurate?

- a. Debtor Inc. can assign the lease to a third party over Lessor Inc.'s objection if there is adequate assurance that the assignee can perform the future obligations under the lease.
- b. Debtor Inc. can assign the lease to a third party over Lessor Inc.'s objection if Debtor Inc. also remains liable for the performance of the future obligations under the lease.
- c. Debtor Inc. can not assign the lease to a third party over Lessor Inc.'s objection because of the lease provision prohibiting such assignments.
- d. Debtor Inc. can not assign the lease to a third party over Lessor Inc.'s objection unless Lessor Inc.'s refusal to consent to the assignment is unreasonable.

### STAND ALONE QUESTION

[36]<sup>36</sup> Big Bank has a valid and perfected lien on a truck belonging to the debtor. The debtor wishes

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<sup>34</sup>D is correct. First, the rejection of the lease constitutes a pre-petition breach under §365(g). Second, §502(b)(6) limits a real estate lessor's claim to the rent for the greater of one year or 15% of the remaining lease term (8 months here).

<sup>35</sup>A is correct under §365(f). C and D are incorrect because §365(f)(1) overrides the restriction on assignment. B is incorrect because §365(k) relieves the estate from further liability on the assigned lease.

<sup>36</sup>C is correct under Assoc. Commercial Corp. v. Rash, 117 S.Ct. 1879 (1997). Thus, A, B and D are incorrect. Although some courts actually use an average value, C is a better answer than D because

to retain the truck and cram down the secured claim in his/her Chapter 13 plan. If the court wishes to determine the value of the truck for cram down purposes, which of the following statements is the most accurate?

- a. The court should use the foreclosure sale value of the truck .
- b. The court should use the wholesale value of the truck.
- c. The court should use the replacement value of the truck.
- d. The court should use the average of the foreclosure sale value and the replacement value.

FACT PATTERN H [For Questions 37 & 38]

At the time that Furniture Store Inc. filed its petition under Chapter 11 of the Bankruptcy Code, the Big Bank had a valid security interest in all of Furniture Store Inc.'s inventory, and accounts receivable. The security agreement also granted the Big Bank a security interest in any proceeds of those items of collateral. Big Bank had properly perfected its security interest. Since the Chapter 11 filing, Furniture Store Inc. has remained in possession of its assets and has continued to operate its business as a debtor in possession.

[37]<sup>37</sup> In order for Furniture Store Inc. to sell its inventory in the ordinary course of business, the Bankruptcy Code requires:

- a. that Big Bank consent.
- b. that the court authorize the sale after notice and a hearing.
- c. neither consent nor court authorization.
- d. that the proceeds of the sales be remitted directly to Big Bank.

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it correctly states the applicable legal standard.

<sup>37</sup>C is correct because §363(c)(1) permits ordinary course sales of collateral if the business of the debtor is authorized to be operated. Thus, A and B are incorrect. D is incorrect because §363 does not require remittance of sale proceeds.

[38]<sup>38</sup> Assume that Furniture Store Inc. sold some inventory for cash and wishes to use that cash in the ordinary course of its business. Which of the following statements is the most accurate?

- a. Furniture Store Inc. can use the cash in the ordinary course of business only if Big Bank consents.
- b. Furniture Store Inc. can use the cash in the ordinary course of business only if the court authorizes the use of the cash after notice and a hearing.
- c. Furniture Store Inc. can use the cash in the ordinary course of business if either Big Bank consents or the court authorizes the use of the cash after notice and a hearing.
- d. Neither consent nor court authorization are necessary in order for Furniture Store Inc. to use the cash in the ordinary course of business.

### STAND ALONE QUESTION

[39]<sup>39</sup> For several years, Don Debtor worked as a computer programmer at the main office of a large national corporation in Atlanta, Georgia. During that time, Don's residence, domicile, and all of his assets were located in Atlanta, which is in the Northern District of Georgia. Recently, Don was transferred to the Nashville, Tennessee, branch office of his employer. Exactly 60 days ago, Don moved to Nashville, taking all of his assets with him. Don bought a nice home in Nashville and has no plans to leave. Nashville is located in the Middle District of Tennessee. If Don wishes to file a petition in bankruptcy today, which of the following statements is the most accurate?

- a. The petition may be filed in the Middle District of Tennessee, because Don now resides there.
- b. The petition may be filed in the Middle District of Tennessee, because all of Don's assets are now located there.
- c. The petition may be filed in the Northern District of Georgia because the principal office of the business for which Don works is located there.
- d. The petition may be filed in the Northern District of Georgia because Don resided there

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<sup>38</sup>C is the best answer because §63(c)(2) prohibits use of cash collateral absent either consent or court authorization. Thus, D is incorrect. Both A and B are incorrect because they each list only one of those alternatives.

<sup>39</sup>D is correct because 28 U.S.C. §1408 provides that, in cases where the debtor's residence has changed, the case must be filed in the district where the debtor resided for the longer portion of the 180 days preceding the filing. Thus, A is incorrect. Similarly, B is incorrect because the 180 day rule also applies to the "principal assets" test. C is incorrect because it states the rule that would apply if Don's employer wished to file bankruptcy.

until 60 days ago.

FACT PATTERN I [For Questions 40 & 41]

Prior to bankruptcy, Debtor Inc. contracted with Builder Inc. to remodel Debtor Inc.'s offices. Debtor Inc. paid for the work in advance, but half way through the remodeling project, and without any justification, Builder Inc. walked off the job, breaching the contract. The damages to Debtor Inc. resulting from Builder Inc.'s breach of the contract exceed \$100,000. The breach occurred on January 15, 1990. Two years later, on January 15, 1992, Debtor Inc. filed a petition under Chapter 11 of the Bankruptcy Code. On May 1, 1992, the case was converted to a case under Chapter 7 and a Chapter 7 trustee was appointed. There is no diversity of citizenship between Debtor Inc. and Builder Inc.

[40]<sup>40</sup> If Debtor Inc.'s Chapter 7 trustee wishes to bring suit against Builder Inc. to recover damages on a state law-based breach of contract claim, which of the following statements is the most accurate?

- a. The lawsuit may be filed in federal court because it arises under bankruptcy law.
- b. The lawsuit may be filed in federal court because it affects the liquidation of the assets of the estate.
- c. The lawsuit may not be filed in federal court because it involves only a state-law claim and there is no diversity of citizenship.
- d. The lawsuit may not be filed in federal court because the claim did not arise in the bankruptcy case.

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<sup>40</sup>B is correct because 28 U.S.C. §1334(b) extends federal jurisdiction to "related to" matters, including state law claims that do not satisfy the normal diversity requirement. Thus, C is incorrect. [Although there is an argument that Article III requires diversity for such state law-based claims, B is still the better answer.] A is incorrect because this claim does not arise under bankruptcy law. D is incorrect because "arising in" jurisdiction is merely an alternative to "related to" jurisdiction.

[41]<sup>41</sup> Assume that the relevant state statute of limitations requires that actions based on contracts be brought within three years of the breach. If the Chapter 7 trustee wishes to bring suit against Builder Inc. to recover damages on a state law-based breach of contract claim, which of the following statements is the most accurate?

- a. The lawsuit must be filed within three years of the breach of contract.
- b. The lawsuit must be filed within two years of the Chapter 11 petition date.
- c. The lawsuit must be filed within two years of date on which the case was converted to Chapter 7.
- d. The lawsuit must be filed before the case is closed or dismissed.

#### STAND ALONE QUESTION

[42]<sup>42</sup> Millie Millionaire owns and operates the Lone Star Saloon as a sole proprietorship. The business is in terrible financial shape. However, Millie's private finances are in great shape overall, due in large part to her inherited wealth. If Millie wishes to reorganize the Lone Star Saloon under the Bankruptcy Code, then:

- a. a joint petition must be filed by both Millie Millionaire and the Lone Star Saloon.
- b. a petition must be filed by Millie Millionaire, individually, in which case all of Millie's assets will be administered by the bankruptcy court.
- c. a petition must be filed by the Lone Star Saloon.
- d. a petition must be filed by Millie Millionaire, on behalf of the Lone Star Saloon, in which case only the assets related to the Lone Star Saloon will be administered by the bankruptcy court.

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<sup>41</sup>B is correct because §108(a) extends any unexpired limitation period to the later of the end of the original limitations period or two years after the order for relief. Thus, C and D are incorrect. Since two years after the order for relief is later than the original three-year limitation period, A is incorrect.

<sup>42</sup>B is correct, because the Lone Star Saloon, as a sole proprietorship, is not an entity that may be a debtor under §109.

FACT PATTERN J [For Questions 43 - 45]

Two years ago, Don Debtor applied for a loan through Big Bank's "instant phone loan" program. Under that program, Don provided the loan application information to the loan officer by telephone. When the loan officer asked Don about his financial condition, Don fraudulently exaggerated the value of his assets and omitted several of his debts. Based on the false financial information provided by Don, the loan officer approved the loan. The next day, Don stopped by the Big Bank, signed the loan note and received the loan proceeds. Big Bank has since discovered Don's fraud. When Big Bank heard that Don was considering filing a petition under Chapter 7 of the Bankruptcy Code, the loan officer called Don and told him that the Big Bank would "block his discharge and raise all sorts of hell" if he tried to get out of the loan. After some discussion, Don and the loan officer agreed that Don would omit the Big Bank loan from his bankruptcy schedules so that the debt would pass through the bankruptcy unaffected. In exchange, the Big Bank agreed not to object to Don's discharge. A week later, Don filed a petition under Chapter 7 of the Bankruptcy Code, but did not list the Big Bank loan in his schedules. The next day Don called the loan officer on the telephone to tell him that he had filed bankruptcy and that he had complied with the agreement by leaving the Big Bank loan off his schedules. The Big Bank never received any official notice of Don's bankruptcy.

[43]<sup>43</sup> If the Big Bank takes no further action, which of the following statements is the most accurate?

- a. The loan debt will be discharged because Don told the loan officer about his bankruptcy.
- b. The loan debt will be discharged because the Big Bank has unclean hands.
- c. The loan debt will not be discharged because its claim was not listed in Don's schedules.
- d. The loan debt will not be discharged because Don fraudulently induced the Big Bank to make the loan.

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<sup>43</sup>A is correct under §23(a)(3) because the Big Bank had actual knowledge of the bankruptcy. Thus C is incorrect. D is incorrect because the §23(a)(2) "fraud" exception to discharge must be raised in the bankruptcy case. See §23(c).

[44]<sup>44</sup> As a result of Don's agreement with the Big Bank and his omission of that debt from his schedules:

- a. Don has committed a federal criminal offense.
- b. Don has reaffirmed the Big Bank loan debt.
- c. Don can be denied a discharge under Chapter 7.
- d. both (a) and (c) are correct.

[45]<sup>45</sup> Assume that, despite the agreement with Don, the Big Bank files a timely proof of claim and timely files an adversary proceeding to have its claim held non-dischargeable. Which of the following statements is the most accurate?

- a. The loan debt will be discharged because the bankruptcy court will grant Don specific performance of the Big Bank's agreement not to object to Don's discharge.
- b. The loan debt will be discharged because Don's loan application was taken over the phone.
- c. The loan debt will not be discharged because Don acted with an actual fraudulent intent.
- d. The loan debt will not be discharged because the fraud occurred less than three years prior to bankruptcy.

FACT PATTERN K [For Questions 46 - 48]

Don Debtor, an automobile mechanic, paid \$100,000 for his home when he purchased it (10) years ago. Don made a \$10,000 cash down payment and obtained an \$90,000 purchase money mortgage from the Big Bank. Two years ago, Don refinanced his mortgage with Big Bank. Since the home had appreciated in value, Big Bank was willing to loan Don more than the remaining balance on the original loan. Don used the extra loan proceeds to pay off a car loan and the balances on several charge cards. Unfortunately for Don, he did not cancel the charge cards. Exactly two months ago, he

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<sup>44</sup>D is the best answer. C is correct because Don's omission of the debt from his schedules clearly violates the 727(a)(4)(a) "false oath" objection to discharge, and arguably the agreement with the Big Bank also violates the 727(a)(4)(c) "receipt of advantage for forbearing to act" objection to discharge. C is correct because these also constitute "bankruptcy crimes" under 18 U.S.C. 152.

<sup>45</sup>B is correct because under 523(a)(2)(B) a false statement of financial condition must be in writing before it can support a non-dischargeability action. Thus, C is incorrect.

filed a petition under Chapter 7 of the Bankruptcy Code. Assume that the total mortgage debt as of the date of bankruptcy was \$120,000 and that interest was accruing at the rate of \$1,000 per month. Assume also that Don Debtor will be liable for any deficiency upon foreclosure of the Big Bank's mortgage.

[46]<sup>46</sup> Assume the value of the home is \$150,000. Which of the following statements is the most accurate?

- a. Two months after the petition was filed, the total amount of the Big Bank's allowable secured claim is \$120,000.
- b. Two months after the petition was filed, the total amount of the Big Bank's allowable secured claim is \$122,000.
- c. Big Bank is entitled to have the automatic stay lifted because the home is not necessary to an effective reorganization.
- d. Both (a) and (c) are correct.

[47]<sup>47</sup> Assume the value of the home is \$120,000. Which of the following statements is the most accurate?

- a. Two months after the petition was filed, the total amount of the Big Bank's allowable secured claim is \$120,000.
- b. Two months after the petition was filed, the total amount of the Big Bank's allowable secured claim is \$122,000.
- c. Big Bank is entitled to have the automatic stay lifted because the home is not necessary to an effective reorganization.
- d. Both (a) and (c) are correct.

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<sup>46</sup>B is correct because under §506(b), an oversecured creditor may continue to accrue interest on its claim post-petition. C is not correct because §362(d)(2) also requires a lack of equity.

<sup>47</sup>D is the best answer. A is correct because we now have both lack of equity and no effective reorganization (this is a Chapter 7 case). C is correct because §506(a) and §502(b) combine to limit the claim to the amount due as of the filing date.

[48]<sup>48</sup> Assume the value of the home has dropped to \$110,000, and assume that the balance due on the Big Bank mortgage is \$120,000. If the Chapter 7 trustee sells the home (with the Big Bank's consent) for \$110,000, which of the following statements is the most accurate?

- a. The Chapter 7 estate has a taxable gain of \$10,000 on the sale.
- b. Don has a taxable gain of \$10,000 on the sale.
- c. Don has a tax loss of \$10,000 on the sale.
- d. Don will have taxable income when he receives a discharge of the remaining indebtedness to the Big Bank under ' 524 of the Bankruptcy Code.

FACT PATTERN L [For Questions 49 & 50]

Ten months prior to filing her petition under Chapter 7, Donna Debtor sold her home to Bob Badman for \$50,000 because she needed the money to pay off some debts. Donna had no fraudulent intent and actually believed that \$50,000 was a fair price. In fact, the fair market value of the home at the time of the sale was actually \$100,000. Bob had no other connection or relationship with Donna. However, he was acting in bad faith, he knew what the house was worth, he knew that Donna was insolvent and in a desperate financial condition, and he knew that he was taking advantage of her. At all relevant times, Donna was insolvent.

[49]<sup>49</sup> Which of the following statements is the most accurate?

- a. The Chapter 7 trustee can not avoid the sale because it occurred more than 90 days before the filing of the Chapter 7 petition.
- b. The Chapter 7 trustee can not avoid the sale because Donna lacked actual fraudulent intent.
- c. The Chapter 7 trustee can avoid the sale because Bob Badman acted in bad faith.
- d. The Chapter 7 trustee can avoid the sale if the court finds that \$60,000 is not reasonably equivalent to \$100,000.

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<sup>48</sup>Only A is correct, because the transfer from the debtor to the estate is not a taxable event. The estate acquires the debtor's basis of \$100,000 and (absent an abandonment) has a gain upon sale. See In re Bentley, 916 F.2d 431 (8th Cir. 1990). D is incorrect because the discharge of indebtedness in bankruptcy does not result in taxable income.

<sup>49</sup>D is the best answer because §548 avoids constructively fraudulent transfers where the debtor receives less than a reasonably equivalent value, without regard to intent. Thus, B and C are incorrect. [The good faith issue raised by C goes to Bob's rights to recover what he paid under §548(c).] A incorrectly focuses on a preference element which does not apply under §548.

[50]<sup>50</sup> Assume that the trustee successfully avoids the sale. Which of the following statements is the most accurate?

- a. The Chapter 7 trustee may recover either Donna's home or its value.
- b. Donna may assert her exemption rights in the recovered home.
- c. Bob Badman is entitled to a \$60,000 lien on the home.
- d. Bob Badman is entitled to a \$60,000 credit against the Chapter 7 trustee's \$100,000 avoidance recovery.

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<sup>50</sup>A is the best answer under §50(a). B is incorrect under §522(g) because the transfer was a voluntary one. C and D are incorrect because §548(c) protects only those transferees who act in good faith.