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TOPICAL HIGHLIGHTS
Bankruptcy
June 13, 2006

Case Administration: Bad faith as basis for denying Chapter 7 debtor's motion to convert-Certiorari Granted.

Granting certiorari from a decision of the First Circuit Court of Appeals, the United States Supreme Court has agreed to decide whether a Chapter 7 debtor's right to convert is absolute.

The First Circuit held that 11 U.S.C.A. § 706(a), which provides that a Chapter 7 debtor "may" convert his case to a case under another chapter "at any time," as long as he is eligible for relief under that chapter and the case has not previously been converted, does not confer on the debtor an absolute right to convert if these two conditions are met. Rather, the bankruptcy court may deny the debtor's motion to convert where the court determines that the debtor engaged in bad faith conduct.

Subsection 706(a) had to be viewed in light of a fundamental canon of the Bankruptcy Code, namely, that a bankruptcy court sitting in equity must take all reasonable steps to prevent a debtor from abusing or manipulating the bankruptcy process to undermine the essential purposes of the Code, including the principle that all of a debtor's assets are to be gathered and deployed in a bona fide effort to satisfy valid claims. The Court of Appeals could discern no evidence from the language of the Code that Congress intended to override the presumptive power and responsibility of the bankruptcy court to weed out abuses of the bankruptcy process at any stage in the bankruptcy proceedings. Moreover, in contrast to other sections of the Code which use the mandatory "shall," the fact that subsection 706(a) contains no such imperative language strongly suggested that it confers a more restricted right upon the debtor, and that the bankruptcy court presumptively retains its discretionary prerogative to deny conversion in some circumstances.

In providing that the debtor may convert a case "at any time," Congress merely conveyed that no artificial time constraints should impede the debtor's election to convert, the Court of Appeals added.

In his petition for a writ of certiorari, the debtor noted that the law on this issue "is in complete disarray," with some courts finding that the right of a Chapter 7 debtor to convert is absolute and unqualified and others concluding that conversion may be denied in the absence of good faith. Both the plain language of the Code and the provision's legislative history make clear that the right to convert is absolute, the debtor argued. (Case below: *In re Marrama*, 430 F.3d 474 (C.A.1 2005).)

Marrama v. Citizens Bank of Mass.

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