No. 08-1134

In the Supreme Court of the United States

UNITED STUDENT AID FUNDS, INC.,
Petitioner,

v.

FRANCISCO J. ESPINOSA,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

Brief of the States of Oregon, Alaska, Hawaii, Michigan, Missouri, Nevada, Ohio, Tennessee, Utah, Washington and Wyoming

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QUESTIONS PRESENTED

Section 523(a)(8) of the Bankruptcy Code provides that student loans are nondischargeable unless there is an affirmative showing by the debtor that repayment of the loan would impose an undue hardship. In turn, Rule 7001(6) of the Federal Rules of Bankruptcy Procedure ("Bankruptcy Rule") provides that an action to determine the dischargeability of a debt must be brought by way of an adversary proceeding (a separate proceeding within a bankruptcy case that is litigated directly between the debtor and the other party). Finally, Bankruptcy Rule 7004 provides that an adversary proceeding is to be initiated by the service of a summons and complaint on the defendant party. The questions presented are:

1. Where a debtor ignores the requirements of Bankruptcy Rules 7001(6) and 7004 and purports to discharge a student debt by inclusion of language in a Chapter 13 plan, has the debtor satisfied the requirements of *Mullane v. Cent. Hanover Bank & Trust Co.*,, 339 U.S. 306 (1950) – that due process requires that a party must provide "notice reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections?"

2. If the debtor has failed to satisfy those due process requirements by failing to initiate an adversary proceeding and to serve the student loan creditor with a summons and complaint, is the plan confirmation order void in that respect, is the order void, or may the bankruptcy court nevertheless presume that

the party agrees with the proposed action such that it can be bound by *res judicata* to an order approving that action?

3. Does the bankruptcy court have authority to approve a plan that provides for actions that the Bankruptcy Rules state must be taken by adversary action?

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STATEMENT OF AMICI INTEREST

The Amici states are parties that appear as secured and unsecured creditors in bankruptcy cases. They may enforce student loans and, as such, are directly affected by the Ninth Circuit's holding. The logic of the analysis below, though, extends far beyond student loans to any discharge exception in Chapter 13 which, since the 2005 amendments to the Bankruptcy Code, now include, *inter alia*, those arising from late or non-filed tax returns, from taxes a debtor sought to fraudulently evade, from debts that the debtor failed to timely schedule, from domestic support obligations, from drunk driving judgments, and from criminal sentences.

Those debts are excepted from discharge under Sections 523 and 1328(a) without need for action by the creditor. Taken together, the Bankruptcy Code and Rules provide that the determination of whether a particular debt falls into those exceptions must be made by a separate proceeding, directed at and naming a specific creditor, in a complaint with allegations sufficient to satisfy Bankruptcy Rule 9011, and served by means of a summons. That is a distinctive method of proceeding from that used to confirm a plan and provides notice with far greater force and clarity to creditors that the debtor is seeking to discharge their debt.

The Ninth's Circuit's analysis, though, which countenances debtors' actions that flout those provisions of the Bankruptcy Code and the Rules, creates a chaotic process in Chapter 13 that lays traps for the unwary, requires prudent parties to incur unnecessary costs, and burdens courts with the need to review plans multiple times. This process – often referred to as "discharge by declaration" or "discharge by ambush" – is antithetical to a debtor's obligation to deal equitably with its creditors when it seeks the enormous equitable benefit of a discharge.

Similarly, to the extent that the Amici states appear as secured creditors, they are also concerned with attempts by debtors to use Chapter 13 plans to invalidate security interests, even though Bankruptcy Rule 7001(2) provides that actions to "determine the extent, priority, and validity" of liens must also be brought by adversary proceedings. The Ninth Circuit's analysis would equally allow such plans to trump the provisions of the Code and the Rules. The Amici states have an interest in this case to ensure that their liens – for taxes, for costs of environmental cleanups, and for a myriad of other purposes – are not lost when debtors ignore the rules.

Under the decision here, creditors must *assume* debtors will include unlawful provisions in their plan and fail to provide legally-required notice thereof, so that they must devote their efforts to ferreting out those provisions and forcing debtors to rewrite their plans. At best, the decision places substantial unnecessary costs and burdens on *all* parties in the case as well as the courts. At worst, those who do not anticipate the debtor's violations will lose rights Congress intended them to retain. Moreover, since the costs of administering the student loan system are not personally apportioned but, rather, are imposed equally on all student debtors,[1] those added costs will be spread onto borrowers who do play by the rules. The costs for protecting other debts and secured interests from frivolous plan provisions will similarly fall squarely on taxpayers of the Amici states.

Those costs will be increased even further by virtue of the Ninth Circuit's final ruling in the case – namely, that bankruptcy courts may not act *sua sponte* to bar confirmation of abusive plans and to police the actions of debtors and their counsel. The outbreak of "discharge by ambush" cases a decade ago was contained not only by the heightened diligence of creditors, but also by stern warnings by bankruptcy courts that inclusion of such provisions was improper and sanctionable. The Ninth Circuit's holdings, though, if left standing, will engender a new explosion of these cases, recreating the burden, costs, and uncertainty that occurred before. That is particularly true in light of the broad venue provisions of the Code which allow debtors to obtain favorable rulings merely by changing their residence. In an era of unprecedented budget shortfalls, the Amici states are deeply concerned that they not be forced to shoulder unnecessary costs to protect themselves from debtors who refuse to abide by the Code and Bankruptcy Rules.

STATEMENT OF CASE

In 1988-89, Mr. Espinosa obtained various gov-

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[1] *See Black v. Educational Credit Mgmt. Corp.*, 459 F.3d 796, 800-01 (7th Cir. 2006) (upholding imposition of collection costs as uniform percentage of debt owed).

ernment guaranteed student loans. In 1992, he filed a Chapter 13 case that listed his student loans as his only debts, proposed to pay only the principal, and stated any unpaid amounts (i.e., the prepetition and postpetition interest) would be discharged. He did not file an adversary proceeding to seek discharge of his debts, and his plan did not assert that payment of the interest would be an "undue hardship." Instead of serving an officer, managing or general agent, or other agent authorized to receive service of process with a summons and complaint as required by Bankruptcy Rule 7004(a) and (b)(3), Mr. Espinosa mailed a copy of his plan to a post office box used to receive payments on his loans.

The lender filed a proof of claim that was not objected to. It was later notified that the plan amount differed from its claim. It did not object to payment of that different amount. The standard discharge order was entered in 1997, providing that any debt for a student loan was excepted from discharge. In 2000, the Education Department began collection efforts and caused his income tax refunds to be intercepted. Three years later, in 2003, Espinosa filed a motion alleging that those actions violated the discharge injunction. The lender recalled the loans from the Education Department and moved, under Fed. R. Civ. P. 60(b)(4), for relief from the confirmation order. The bankruptcy court ruled for Espinosa, but the district court reversed, holding that the confirmation order was void for lack of due process. On further appeal, the Ninth Circuit remanded to the bankruptcy court to indicate if its original discharge order (which contradicted the plan terms) had been a clerical error, and, upon being informed that the order *was* in error, the Ninth Circuit reversed the District Court and, entered the order at issue here. *In re Espinosa*, 553 F.3d 1193 (9th Cir. 2008)

ARGUMENT

The Ninth Circuit's analysis reduces to a few propositions. First, despite Bankruptcy Rule 7001(6), which requires an adversary proceeding and a showing of undue hardship to discharge a student loan debt, a debtor's plan may provide that the debt will be discharged and no such proof will be required. Second, despite the requirement in Bankruptcy Rule 7004 that an adversary proceeding must be brought by means of a complaint and summons served upon specified parties at a specified address, the debtor may mail a copy of the plan to a different address and without naming those specific parties. Third, the creditor has no right to assume that legal requirements for notice will be complied with so as to limit its involvement in the case in accordance with those requirements. And fourth, violation of the Rules has no relevance to the question of whether due process has been accorded to litigants such that *Mullane* has been satisfied. Instead, the Ninth Circuit assumes that *Mullane* prescribes some generic degree of notice that is adequate, even if that form of notice *violates* a rule or statute. Thus, under its view, if that general level of notice is provided, it is irrelevant that the creditor would have expected something better and could have been misled by its absence.

That analysis, the Amici states submit, violates the basic holding of *Mullane* that due process must be decided after an analysis of *all of the circumstances.* Those circumstances surely include the fact that creditors have been told what notice they are to receive and are entitled to rely thereon. That fact is true in any civil proceeding; it is critical in the unique scenario posed by bankruptcy proceedings.

I. Bankruptcy's unique nature demands a consistent application of the rules.

Bankruptcy is quantitatively – and, in turn, qualitatively – different from any other form of litigation in federal court. Bankruptcy filings are far greater than all other federal cases combined – and the ratio has increased dramatically during the twenty years since Mr. Espinosa received his loans. In 1988, when he took out the loans, there were 549,612 nonbusiness bankruptcies. By 1992, when he filed his petition, that number had soared to 900,874, and by 1997, when he received a discharge, the number had grown by another 50 percent to 1,350,118. From 1998 to 2004, the number varied between a low of 1,217,972 in 2000 and a high of 1,625,208 in 2003.[2] After Congress amended the Code in April 2005, 620,000 petitions were filed in October 2005 alone to avoid the effective date of the new act, resulting in an

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[2] All filing rates taken from charts maintained by American Bankruptcy Institute: http://www.abiworld.org/AM/AMTemplate.cfm?Section=Home&TEMPLATE=/CM/Content Display.cfm&CONTENTID=56822. All websites cited herein were viewed on April 7, 2009.

annual total or more than 2 million cases.[3] After dropping dramatically the following year (to just under 600,000 cases), the numbers have grown each succeeding year – to more than 800,000 in 2007, over 1 million in 2008, and a projected total of perhaps as many as 1.4 to 1.6 million in 2009.[4]

By contrast, in 1992, there were 66,875 federal criminal and 229,850 federal civil cases for a total of 296,725 filings,[5] less than a third of the 900,000 plus bankruptcy filings. By 1997, other federal filings had risen only to 322,390, compared to 1.35 million bankruptcy filings – a 4.1 to 1 ratio. Those other filings varied little in succeeding years, averaging about 340,000 cases a year from 2004 to 2008. Even with an initial slowing after the 2005 amendments, bankruptcy cases during that period averaged about 1.2 million or about three and half times the rest of federal cases. As filings soar again this year, the ratio should move back above the 4 to 1 mark. Chapter 13

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[3] *See* http://www.abiworld.org/AM/Template.cfm? Section=Home&TEMPLATE=/CM/ContentDisplay.cfm&CONTENTID=42631.

[4] *See* Appendix 1 for 2006-08 statistics. See http://www.creditslips.org/creditslips/2009/04/my-entry.html#more for predictions by Professor Robert Lawless for 2009 filings.

[5] *See* http://www.ojp.usdoj.gov/bjs/pub/pdf/cfjs92.pdf p. 12 (criminal filings) and http://www.lectlaw.com/files/jud09.htm (civil filings). (Criminal statistics are for calendar year 1992; the civil statistics are for FY 93, beginning October 1992).

cases typically have comprised about 30 percent of all consumer cases.[6] Thus, except for the exceptional year of 2006, Chapter 13 cases alone have equaled (or substantially exceeded) the total of the rest of the federal civil system during this entire period.

The reality is that bankruptcy, at least on the consumer debtor side, is a high volume, highly standardized practice that uses software packages, form pleadings, standard plans, "no look" fee approvals, and the like to handle the wholesale business of processing hundreds of thousands of petitions each year. In that regard, while the federal courts obviously handle many complex, multi-party cases, most civil litigation still involves only two-party disputes raising a finite number of related issues. Bankruptcy cases, by contrast, inevitably involve unrelated claims by many different parties against the debtor. The debtor (or trustee), in turn, must analyze a wide variety of state law and Code-created claims against creditors and third parties, contest liens of those parties, and defend challenges to the claimed exemptions. Further, in filings under Chapters 11, 12, and 13, debtors have broad leeway to propose plan terms and creditors may vote on and/or object to those proposed plans. And, finally, the debtor and his creditors may litigate his right to a general discharge, or whether specific debts may be discharged. That multitude of proceedings, moreover, takes place on a highly compressed

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[6] *See* http://www.abiworld.org/AM/AMTemplate.cfm?Section=Home&TEMPLATE=/CM/ContentDisplay.cfm.

schedule compared to normal federal litigation.[7]

This cacophony of actions could result in chaos in the absence of the carefully-orchestrated provisions of the Code and the Rules which set procedural mechanisms for different types of actions, with specific notice, timing, and objection provisions for each. Those clearly spelled out rules give all parties the information they need to navigate the complex waters of bankruptcy litigation without running aground. If those provisions can be ignored, however, creditors will be left unsure as to what they must do to retain their rights and be forced to incur added costs to litigate issues the Code and Rules have already settled.

Creditors, though, should have a right to receive the notice due to them under the Rules and to gauge their actions accordingly. That truism undoubtedly applies even when a defendant is involved in only one case with a single other party, but the need for rules to be followed increases geometrically where a single defendant, such as the student loan creditors – or a tax authority of the Amici states – may be faced with literally thousands or tens of thousands of cases in a

[7] Plans must be filed no later than 15 days after the petition date. Bankruptcy Rule 3015(a). The confirmation hearing currently must be at least 20 days after the Section 341 meeting of creditors, which in turn, under Bankruptcy Rule 2003(a) is to be held between 20 and 50 days after the case is filed. Section 1324(b). Thus, if the plan is filed on the 15th day, the plan confirmation hearing could be as early as the 40th day of the case. Before 2005, there was no minimum period set between the petition date and the confirmation hearing.

single year.[8] To cope with those filings in an economically realistic fashion, creditors must set up automated systems to handle their cases, delegate much of the work to paralegals, and train secretarial staff as to which matters must be brought to counsel's attention and which do not require further action. In making those case-handling judgments, creditors have a right to gauge their actions in accordance with the clear terms of the Code and the Rules.

That is particularly true when a third salient reality of Chapter 13 cases is considered, namely, the fact that, despite the array of potential litigation relative to any given filing, these are usually low-dollar cases. In FY 2007, for instance, the payments made through Chapter 13 cases totaled some $2.8 billion for secured claims, $390 million for debtors' counsel, $300 million for priority debt, and $257 million for the trustees, for a total of about $3.75 billion - leaving only $1.35 billion for all unsecured creditors.[9] Divided by the

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[8] As noted by the defendant, the federal student loan programs service more than $500 billion of loans. The defendant here received notice of 24,411 bankruptcies in 2008 alone. U.S. DEPT. OF EDUC., FINANCIAL AND PERFORMANCE QUARTERLY UPDATE, Issue 2008-2, at 7 (Sept. 30, 2008).

[9] *See* http://www.usdoj.gov/ust/eo/private_trustee/library/chapter13/docs/ch13ar07-AARpt.xls; FY-2007 Chapter 13 Trustee Audited Annual Reports. The total was even less before the 2005 amendments – *see* Prof. Scott F. Norberg, *Chapter 13 Project: Little Paid to Unsecureds*, 26 Amer. Bank. Inst. J. 1 (March 2007) (less than 20% of receipts went to

roughly 300,000 Chapter 13 cases filed in 2007, that resulted in an average payout to unsecured creditors of little more than $4,500 per case. When potential recoveries are so small, unsecured creditors like the student lenders here must judge carefully how much to spend on reviewing and litigating plan terms, knowing that their real hope of payment comes from collecting nondischargeable debts after the plan is finished and competing obligations are discharged.

Finally, it is important to consider how Chapter 13 plans will be structured if a debtor knows that it must comply with the law. The Chapter 13 discharge in Section 1328 excepts certain debts (including student loans) from discharge. Further, it is well settled that interest accruing on non-dischargeable debts (such as was the case here) is also excepted from the discharge. *Bruning v. United States*, 376 U.S. 358, 360 (1964); *In re Foster*, 319 F.3d 495, 497-98 (9th Cir. 2003). If a debtor knows it cannot discharge such debts through plan provisions, it not only has no incentive to discriminate against those debts, it has a positive incentive to give them *preferential* treatment. Courts differ on whether such treatment is allowed; the point is simply that, if the debtor knows he can discharge the debt only by filing an adversary complaint, he has every reason to pay as much as possible on such debts under its plan, since each dollar not paid on a nondischargeable debt is a one that he must pay later. Accordingly, a creditor that does not want to waste money in Chapter 13 cases or run up costs

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unsecured creditors).

for those who *are* paying their debts, can rely on those built-in incentives to ensure that it will receive as much under the plan as it is legally entitled to. It can, then, direct its limited resources to higher-priority issues, such as defending actual undue hardship adversary actions.

On the other hand, if debtors are free to ignore both the substantive and procedural requirements of the Code and the Rules, then they have every reason to underpay disfavored creditors or seek to discharge debts improperly through plan provisions. Thus, until creditors are alerted by decisions such as the one below, debtors can obtain substantial and unwarranted benefits from those who make the mistake of relying on the rule they have read. And, while creditors with many cases presumably will learn to adapt to a new regimen based on this altered version of the Rules (*albeit* at substantial, unnecessary cost and burden to all parties), occasional creditors may not learn until too late that they were foolish to have assumed that the Rules applied to debtors too. That is not a state of affairs that this Court should tolerate; the Amici states urge the Court to take certiorari on this case in order to reverse the decision below.

II. The decision below conflicts with holdings of this Court and other circuits.

In *Tennessee Student Assistance Corp. v. Hood*, 541 U.S. 440, 449-452 (2004), this Court described the student loan discharge provisions, noting that Section 523(a)(8) is "self-executing;" that the debtor must "affirmatively secure[] a hardship determination" to discharge a student loan debt; that creditors are given "greater procedural protection" before such debts can be discharged even though creditors are not generally entitled to personal service prior to the entry of the discharge; and that an adversary proceeding must be filed to discharge the debt. This Court did, to be sure, state that "*absent Rule 7001(6)*, a debtor could proceed by motion, . . . which would raise no constitutional concern," 541 U.S. at 453 (emphasis added), but that does not mean, as the Ninth Circuit stated that it would be "wrong and dangerous" to allow Congress to define what is required for due process if it chooses to do so. *Espinosa*, 553 F.3d at 1204. The reality is that Rule 7001(6) *does* exist and it *does* impose positive obligations on a debtor – obligations that cannot be disregarded in evaluating the rights of the creditor. The suggestion that *Hood* allows courts to disregard the effect of Rule 7001(6) was rightfully rejected out of hand by *In re Hanson*, 397 F.3d 482, 487 (7th Cir. 2005). Correcting the Ninth Circuit's misreading of *Hood* is itself sufficient reason to grant certiorari.

Even absent the conflict with *Hood*, the Ninth Circuit's ruling puts it squarely in conflict with five other Circuits, as well as this Court's holding in *Mullane*. The Ninth Circuit openly conceded that it had placed itself on the opposite side of all of its sister circuits, as well as the District Court in this case, and the Ninth Circuit Bankruptcy Appellate Panel in *In re Repp,* 307 B.R. 144 (9th Cir. BAP 2004), *reversed by Espinosa,* 553 F.3d at 1204, n. 6. Its decision to give debtors who live in – or move to[10] – the largest

[10] Under the venue provisions of 28 U.S.C. § 1408, a

circuit in the country a preferable position vis-à-vis discharging their student loans compared to those in those other circuits, creates the sort of split that calls for resolution by this Court.

The cases in the other circuits involved the same fact pattern as here – a Chapter 13 debtor who used plan language to discharge a debt, ignoring the Rule stating that he must bring an adversary action to determine undue hardship. In each case, the creditor did not object to the plan or appeal from confirmation, but sought to collect the debt after the plan ended and was met by the contention that the confirmed plan was *res judicata* of the issue. In each case, the Circuit Court held, contrary to the Ninth Circuit's ruling here, the orders were void due to the debtor's violation of due process. Indeed, although the Tenth Circuit had initially relied on *res judicata* principles to uphold "discharge by declaration" in *Andersen v. UNIPAC-NEBHELP* (*In re Anderson*), 179 F.3d 1253 (10th Cir. 1999), it eventually overruled *Andersen* in its *en banc* decision in *Educ. Credit. Mgmt. Corp. v. Mersmann (In re Mersmann)*, 505 F.3d 1033 (2007), when it considered the due process issues the Ninth Circuit rejected in this case.

Further, the same issue has also arisen with respect to whether liens can be invalidated through plan provisions, rather than adversary proceedings as required by Bankruptcy Rule 7001(2). *See In re Man-*

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case may be brought wherever a debtor is currently domiciled, regardless of where the debt was incurred or the lender located.

saray-Ruffin, 530 F.3d 230, 35-36 (3rd Cir. 2008); *In re Bateman*, 331 F.3d 821, 830-833 (11th Cir. 2003); *Cen-Pen Corp. v. Hanson*, 58 F.3d 89 (4th Cir. 1995), all holding that liens cannot be invalidated through plan provisions. Indeed, *see In re Brawders,* 503 F.3d 856, 859-870 (9th Cir. 2007) (affirming decision by Bankruptcy Appellate Panel) and *In re Enewally*, 368 F.3d 165, 1173 (9th Cir. 2004), both of which appear to endorse the same concept. Thus, the Ninth Circuit is in conflict with itself on these issues, and its student loan analysis sets up conflicts with this line of decisions as well.

In short, the Ninth Circuit has created uncertainty where the Bankruptcy Rules prescribe a bright-line requirement, leaving parties to grapple with an amorphous balancing process despite the fact that Congress has prescribed the proper process with complete clarity. Under the Rules, the result is simple – either a summons and complaint are properly served on a proper party, or they are not. But under the Ninth Circuit's approach, courts must decide whether some other, lesser form of notice is adequate under the circumstances of each particular case. Indeed, if its approach is correct, why would it not equally allow parties to disregard the provisions of Fed. R. Civ. Proc. 4 when they commence an ordinary civil action? If one can ignore the duty to serve a complaint and summons yet still bind a party to a default judgment in bankruptcy by mailing some document to the other party, why should that same result not obtain in other litigation? The suggestion would be absurd outside of bankruptcy; it is no less so in bankruptcy.

If anything, it is more necessary in light of the complex, multi-faceted bankruptcy process. The Ninth Circuit's opinion imposes added costs and burdens with no countervailing benefits. Indeed, by gratuitously reviving an abuse that was largely eliminated through the vigilance of creditors and courts, the Ninth Circuit has made handling of bankruptcy matters more difficult than necessary. Those difficulties will increase in light of the new discharge exceptions in Chapter 13 discharge, giving debtors greater incentives to evade the Rules. It is critical that certiorari is granted here so that the Court may bring the law in the Ninth Circuit back into conformity with that of the other Circuit Courts and restore the constitutionally mandated "uniform" law of bankruptcy. U.S. Const. art. I, § 8, cl. 4.

III. The Ninth Circuit erred in its ruling on the merits.

It is also important for this Court to grant certiorari because of the Ninth Circuit's plain error in its rulings on the merits. The discussion below merely touches on the problems with the Ninth Circuit's ruling that must be corrected. Specifically, the decision below erred in not finding that the confirmation order was void for lack of due process in two separate, but related aspects. The Ninth Circuit's rejection of these arguments further illustrates the split among the Circuit Courts on these issues.

A. Where the Bankruptcy Code and Rules prescribe the procedure for discharge of a student loan, the bankruptcy court cannot approve a plan that ignores the procedure.

The Bankruptcy Rules state that an adversary proceeding is the exclusive procedure for determining the dischargeability of a debt in bankruptcy court. Bankruptcy Rule 7001(6). *Hood*, 541 U.S. at 449-452. Under Section 1322(b)(11), a Chapter 13 plan may contain any provision "not inconsistent with this title." Similarly, Section 1325(a)(1) provides that the court "shall confirm a plan if – (1) the plan complies with the provisions of this chapter and with the other applicable provisions of this title; . . . [and] (3) the plan has been proposed in good faith and not by any means forbidden by law." Thus, Congress has thrice stated that plans must only contain lawful provisions and that courts may only confirm lawful plans.

Based on those provisions, and as set out in more detail in Petitioner's brief, other Circuits have held that the Bankruptcy Court lacks the authority to grant a discharge of student loan debt through the plan process. *See Whelton v. Educ. Credit Mgmt. Corp.*, 432 F.3d 150, 154-55, 156, n.2 (2nd Cir. 2005) (using plan process makes discharge provision "void *ab initio*"); *Banks v. Sallie Mae Servicing Corp.*, 299 F.3d 296, 300 (4th Cir. 2002). Section 1325 does not issue mere hortatory admonishments to the debtor; rather, it imposes *requirements* the plan must satisfy to be confirmed. *Mersmann*, 505 F.3d at 1048, 1049 ("§ 1325(a)(1) . . . permits the confirmation of a plan *only* if it is consistent with the rest of the Code;" "bankruptcy court lacks authority to confirm" plan that does not use adversary proceeding); *Hanson*, 397 F.3d at 487 ("Failure to comply with the Code has been said to render the plan and any confirming order 'nugatory.'"). *See also Shaw v. Aurgroup Financial Credit Union*, 552 F.3d 447, 455-58 (6th Cir. 2009); *In re Jones*, 530 F.3d 1284, 1289-90 (10th Cir. 2008), both holding requirements of Section 1325(a) are mandatory. Even if this position is in dispute, that simply creates further conflicts that this Court should resolve. That is particularly true where the Ninth Circuit ended its discussion with the conclusion that bankruptcy courts not only could confirm plans that violated the Code – but they were *barred* from refusing to do so. *Espinosa*, 533 F.3d at 1205 (reversing prior decisions denying confirmation of such plans). Such a clear conflict cries out to be resolved by this Court.

B. Where the Bankruptcy Code or Rules prescribe a particular form of notice, denial of that notice violates due process.

An adversary proceeding is commenced by filing a complaint that must, under Bankruptcy Rule 7008 show "that the [debtor] is entitled to relief" and the specific relief sought. Thus, unlike a debtor's bare demand in a plan for a discharge, a complaint must show the alleged hardship, name the lender, set out the desired relief, and be served by summons on a high-level official or person designated to receive service. Those measures bring home to the creditor in a clear and direct fashion that its *specific* interests are being challenged and that it must look to those interests or suffer a default. By comparison, the debtor need not even serve a full Chapter 13 plan on creditors, only a summary thereof. Bankruptcy Rule 3015(d). Indeed, Section 521(e)(3) now states that a plan is provided to a creditor *only* if it requests the plan and pays for the copy it receives.

In short, the notice requirements for an adversary proceeding are far more exacting than the notice required for confirmation of a Chapter 13 plan. Nevertheless, because USA Funds received some "notice" that a plan was filed, and could have inquired into the effect of the proposed plan on its claim, the Ninth Circuit held that it had received all the notice that it was due on the discharge issue. That conclusion is incorrect both practically and legally. As a practical matter, large creditors, like USA Funds, receive "tidal waves of mail. . . . The quantity 'of notice' that is issued by the bankruptcy system is so overwhelming that it is necessary to have clear rules in order for creditors to know what notices to notice as opposed to the notices that are deafening legal background noise. The Code and the Rules set forth those clear standards and it is up to the courts to ensure that the lines are not blurred." *In re Ruehle*, 412 F.3d 679, 682-83 (6th Cir. 2004).

As a legal matter, this Court has stated that due process requires "notice reasonably calculated, *under all the circumstances*, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections." *Mullane v. Central Hanover Bank & Trust*, 339 U.S. 306, 314 (1950) (emphasis added). The other Circuits have concluded that, at a minimum, that means that parties must receive the notice they have been promised. *See, e.g., Banks*, 299 F.3d at 303 ("due process generally entitles a party to receive the notice specified before an order binding the party will be afforded preclusive effect"); *Ruehle*, 412 F.3d at 684-85 (parties are "entitled to the prescribed level of notice for the process to be due"); *Mersmann*, 503 F.3d at 1049 ("creditor has a right to assume that he will receive all of the notices *required by statute* before his claim is forever barred.").

That principle was stated by this Court in *City of New York v. New York, New Haven & Hartford R.R.*, 344 U.S. 293 (1953) where it considered whether a party could be bound by a confirmation order where it knew of the case but had not been mailed notice of the hearing on the plan as required under the statute and the rules. This Court rejected the argument that knowledge of the case would put a party on inquiry notice so that it would be obligated to take steps to learn of the hearing, stating that "even creditors who have knowledge of a reorganization have a right to assume that the *statutory* 'reasonable notice' will be given them before their claims are forever barred." (Emphasis added). Courts continue to apply that rule in Chapter 11 cases, even where they also find that the different circumstances in Chapter 7 and 13 cases *can* bind parties to mere inquiry notice. *See In re Metzger*, 346 B.R. 806, 817-19 (Bankr. N.D. Cal. 2006), explaining the differences and noting the effect of varying statutory provisions in the different chapters. Thus, it is clear that there is no one single size notice that satisfies all constitutional duties.

The same is true here – the creditors have been told that they will receive a particular form of "reasonable notice," but the debtor provided a different, lesser form of notice that it argues was "good enough." The Ninth Circuit decided that, because the alternative service might have been adequate, in the absence of any specified provisions in the statute or Rule, that it was immaterial that it was not the service that was *required*. That conclusion, though, ignores the critical distinction between being given *no* information and being given *misleading* information. If nothing had been said about how undue hardship would be decided, the creditor would have no alternative but to examine each paper it received with care to determine if a discharge action was lurking within. But, where a specific form of notice is specified, creditors have a right to rely thereon and limit their monitoring efforts accordingly.

Put another way, if the Rules had said, "no action can be taken to affect the discharge of any debt unless the notice is sent in a blue envelope," a creditor could not be faulted for not reviewing documents sent in white envelopes to determine if attempts were being made to affect their debts. The result is no different here – the creditor is told explicitly what to expect, but the debtor used a different mode entirely. The Ninth Circuit held that the lender was sophisticated and it was "highly unlikely" that it was misled by "customary bankruptcy procedure," *Espinosa,* 553 F.3d at 1205 – a statement true only if is "customary" for debtors to ignore the Code and the Rules.

The Ninth Circuit's basic error is its failure to apply *Mullane*'s requirement that due process requires consideration of *all the circumstances*. In *Mullane*, a trustee sought to settle its accounts where thousands of parties were involved and it could not ascertain names and addresses for many of them. The trustee relied on state law that *allowed* publication notice for all parties, but this Court held that such notice could be used only for unknown creditors. Known creditors were entitled to actual service even where there was no reason to believe the trustee had done anything wrong or that any party would sue. Moreover, this was the only action involving the beneficiaries, not one of thousands to which they must respond. Nevertheless, this Court made clear that due process was not a mere gesture, but must be calculated by what a person would do who truly wanted to communicate to another.

Here, by contrast, the debtor is *violating* the Rules, the plan takes away the creditor's rights, the debtor typically has a manageable number of creditors to notify and knows their contact information, while the creditor is dealing with a huge case load that must be carefully managed. Under those circumstances, the debtor knows that creditors will justifiably rely on the Rules to determine the efforts they must make. Allowing debtors to exploit that reliance does not satisfy *Mullane*; it is the antithesis of *Mullane*. Nor can it simply be assumed, as the Ninth Circuit held, that creditors actually *agree* that their claims should be discharged so that it would be *improper* for bankruptcy courts to challenge such provisions *sua sponte*, despite their broad policing powers under Section 105(a). By doing so, the Ninth Circuit has reinvigorated the concept of discharge by ambush, while removing a powerful tool to alleviate the problem. Under all of these circumstances, this is plainly a decision that demands reversal.

CONCLUSION

For the foregoing reasons, the petition for writ of certiorari should be granted.

Respectfully submitted,

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