

*Wu v. Markosian (In re Markosian)*

United States Bankruptcy Appellate Panel for the Ninth Circuit

February 20, 2014; March 12, 2014, Filed

BAP No. NC-13-1339-JuKiD. Bankruptcy No. 09-50778-ASW.

**Reporter**

506 B.R. 273; 2014 Bankr. LEXIS 961; Bankr. L. Rep. (CCH) P82,603; 59 Bankr. Ct. Dec. 56; 2014 WL 956475  
compel was affirmed.

In re: ARA MARKOSIAN and ANAIT MARKOSIAN, Debtors., Trustee, Appellant, v. ARA MARKOSIAN and ANAIT MARKOSIAN, Appellees.

**Prior History:** [\*\*1] Appeal from the United States Bankruptcy Court for the Northern District of California. Bk. No. 09-50778-ASW. Honorable Arthur S. Weissbrodt, Bankruptcy Judge, Presiding.

**Core Terms**

earnings, bonus, conversion, property of the estate, bankruptcy court, converted, personal service, commencement of the case, postpetition

**Case Summary**

ISSUE: Whether an individual debtor's chapter 11 postpetition earnings which are property of the estate under [11 U.S.C.S. § 1115](#) revert to him or her upon a subsequent conversion to chapter 7. HOLDINGS: [1]-As of the petition date, [11 U.S.C.S. § 541\(a\)\(6\)](#) excluded from the chapter 7 estate earnings from services performed by individual debtors after the commencement of the case. Therefore, by operation of [11 U.S.C.S. § 348\(a\)](#), personal service income that came into debtors' chapter 11 estate was recharacterized as property of debtor under [§ 541\(a\)\(6\)](#) when the case was converted to chapter 7; [2]-Accordingly, upon conversion, the bonus reverted to debtors. The bankruptcy court's grant of debtors' motion to

**LexisNexis® Headnotes**

Bankruptcy Law > ... > Judicial Review > Standards of Review > De Novo Standard of Review

**HN1** An appellate panel reviews issues of statutory construction and conclusions of law, including the bankruptcy court's interpretation of the Bankruptcy Code, de novo.

Governments > Legislation > Interpretation

**HN2** Regarding Statutory construction issues, a court starts with the statutory language.

Bankruptcy Law > Estate Property > Contents of Estate

**HN3** Under [11 U.S.C.S. § 541\(a\)](#), the commencement of a case under the Bankruptcy Code creates an estate. Although the estate may acquire property after the commencement of the case, [§ 541\(a\)\(6\)](#), [\(7\)](#), estate property remains distinct from the debtor's property. Under [§ 541\(a\)\(6\)](#), earnings from services performed by an individual debtor after the commencement of the case are the debtor's property which are excluded from property of the estate.

Bankruptcy Law > Conversion &  
Dismissal > Reorganizations

Bankruptcy Law > Estate Property > Contents of  
Estate

Bankruptcy Law > Reorganizations > General  
Overview

**HN4** In 2005, the Bankruptcy Abuse Prevention and Consumer Protection Act added [11 U.S.C.S. § 1115](#) which, similar to [11 U.S.C.S. §§ 1306, 1207](#), adds an individual debtor's postpetition earnings to property of the chapter 11 estate. However, [§ 1115](#) does not apply upon conversion from chapter 11 to chapter 7. Instead, [11 U.S.C.S. § 348](#) governs the effect of a conversion.

Bankruptcy Law > Conversion &  
Dismissal > Reorganizations

Bankruptcy Law > Estate Property > Contents of  
Estate

Bankruptcy Law > Individuals With Regular  
Income > Estate Property

**HN5** Although [11 U.S.C.S. § 348\(f\)\(1\)\(A\)](#) expressly excludes a debtor's postpetition earnings from property of a chapter 7 estate upon conversion from chapter 13--earnings that are included in the chapter 13 estate under [11 U.S.C.S. § 1306\(a\)\(2\)](#)--there is no parallel provision for chapter 11 debtors.

Bankruptcy Law > Conversion &  
Dismissal > Reorganizations

**HN6** [11 U.S.C.S. § 348\(a\)](#), by its plain language, applies to all cases under Title 11, not just certain ones: (a) Conversion of a case from a case under one chapter of this title to a case under another chapter of this title constitutes an order for relief under the chapter to which the case is converted, but, except as provided in [§ 348 \(b\)](#), [\(c\)](#), does not effect a change in the date of the filing of the petition, the commencement of the case, or the

order for relief.

Bankruptcy Law > Conversion &  
Dismissal > Reorganizations

Bankruptcy Law > Estate Property > Contents of  
Estate

**HN7** [11 U.S.C.S. § 348\(a\)](#) expressly states that the date of the petition remains unchanged. Where a case is converted from Chapter 11 to Chapter 7, property of the estate is determined by the filing date of the Chapter 11 petition, and not by the conversion date. As of the petition date, [11 U.S.C.S. § 541\(a\)\(6\)](#) excludes from the chapter 7 estate earnings from services performed by individual debtors after the commencement of the case. Therefore, by operation of [§ 348\(a\)](#), personal service income that came into a debtors' chapter 11 estate is recharacterized as property of the debtor under [§ 541\(a\)\(6\)](#) when the case is converted to chapter 7.

Bankruptcy Law > Estate Property > Contents of  
Estate

**HN8** [11 U.S.C.S. § 541\(a\)\(7\)](#) makes property of the estate any interest in property that the estate (not the debtor) acquires after the case.

Governments > Legislation > Interpretation

**HN9** Attempting to divine congressional intent from congressional silence is an enterprise of limited utility that offers a fragile foundation for statutory interpretation.

**Counsel:** Johnson C.W. Lee, Esq., argued for appellant.

Carol W. Wu, Chapter 7 trustee; Drew Henwood, Esq., argued for appellees Ara and Anait Markosian.

**Judges:** Before: JURY, KIRSCHER, and DUNN, Bankruptcy Judges.

**Opinion by: JURY**

## **Opinion**

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[\*274] JURY, Bankruptcy Judge:

Ara and Anait Markosian (collectively, Debtors) filed a chapter 7<sup>1</sup> petition which they converted to chapter 11 and then reconverted to chapter 7. After reconversion to chapter 7, Mr. Markosian received a bonus from his employer of over \$102,000 for services rendered while the chapter 11 case was pending. Debtors turned over the bonus to appellant, Carol W. Wu, the chapter 7 trustee, and filed a motion to compel the trustee to return it to Debtors. The bankruptcy court granted Debtors' motion, finding that although the bonus constituted earnings and were property of Debtors' chapter 11 estate under [§ 1115\(a\)\(2\)](#), the bonus reverted to them upon conversion of Debtors' case to chapter 7. This appeal followed.

We address an issue of first impression in this Circuit: whether an individual debtor's chapter 11 postpetition earnings which are property of the estate under [§ 1115](#) revert to him or her upon a subsequent conversion to chapter 7. As a matter of statutory interpretation, we conclude that they do and AFFIRM.

### **I. FACTS**

On February 7, 2009, Debtors filed a chapter 7 petition. The United States Trustee moved to dismiss their case for abuse based on Debtors' high income and their ability to pay their creditors. In response, Debtors converted their case to chapter 11 on February 11, 2010. More than two years later, Debtors were unable to confirm a plan because Mrs. Markosian had lost her job. Debtors

reconverted their case to chapter 7 on March 5, 2012.

In April 2012, Mr. Markosian received \$102,498.42<sup>1</sup> from his employer for personal services provided while Debtors' case was still under chapter 11. Debtors turned over the bonus to the trustee and subsequently filed a motion to determine their interest in it. The bankruptcy court denied Debtors' motion without prejudice in order for Debtors to file a new motion to address [\[\\*\\*3\]](#) whether the bonus was property of their chapter 11 estate pursuant to [§ 1115\(a\)\(2\)](#), and if so, whether it subsequently became property of their chapter 7 estate.

[\[\\*\\*275\]](#) Debtors then filed a motion to compel trustee to return the bonus to them as either partially exempted property of the bankruptcy estate or as property excluded from the chapter 7 estate upon reconversion to chapter 7. Trustee opposed.

On January 18, 2013, the bankruptcy court heard the matter, directed the parties to file supplemental briefs and took the matter under advisement. In June 2013, the bankruptcy court issued its memorandum decision. The court found that the bonus constituted earnings from personal services within the meaning of [§ 1115\(a\)\(2\)](#), but concluded that it ceased to be property of the estate upon conversion to chapter 7 based on the reasoning set forth in [In re Evans, 464 B.R. 429, 438-41 \(Bankr. D. Col. 2011\)](#). [\[\\*\\*4\]](#) Because the court found that the bonus was not property of the chapter 7 estate, it did not reach the question whether the money could be claimed exempt. The bankruptcy court entered an order granting Debtors' motion to

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<sup>1</sup>Mr. Markosian actually received a gross bonus of \$191,191.00. However, statutory reductions reduced the total bonus by \$72,931.21, and trustee discovered during litigation over the rights to the bonus that Mr. Markosian had used some of it to purchase company stock worth \$15,761.37, which remains in his possession or has since been sold.

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<sup>1</sup>Unless otherwise indicated, all chapter and section references are to the Bankruptcy Code, [11 U.S.C. §§ 101-1532](#), [\[\\*\\*2\]](#) and "Rule" references are to the Federal Rules of Bankruptcy Procedure.

compel on July 2, 2013. Trustee timely appealed.

## II. JURISDICTION

The bankruptcy court had jurisdiction over this proceeding under 28 U.S.C. §§ 1334 and 157(b)(2)(A). We have jurisdiction under 28 U.S.C. § 158.

## III. ISSUE

Whether the bankruptcy court erred by finding that the bonus, which was property of Debtors' chapter 11 estate under § 1115(a)(2), reverted to Debtors upon conversion to chapter 7.

## IV. STANDARD OF REVIEW

*HN1* We review issues of statutory construction and conclusions of law, including the bankruptcy court's interpretation of the Bankruptcy Code, de novo. *Samson v. W. Capital Partners, LLC (In re Blixseth)*, 684 F.3d 865, 869 (9th Cir. 2012).

## V. DISCUSSION

As with all *HN2* statutory construction issues, we start with the statutory language. We begin by looking at § 541 which defines property of the estate. *HN3* Under § 541(a), the commencement of a case under the Bankruptcy Code creates an estate. Although the estate may acquire property after the commencement of the case, **[\*\*5]** see § 541(a)(6) and (7), estate property remains distinct from the debtor's property. See *Smith v. Kennedy (In re Smith)*, 235 F.3d 472, 478 (9th Cir. 2000). Under § 541(a)(6), "earnings from services performed by an individual debtor after the commencement of the case" are the debtor's property which are excluded from property of the estate.

*HN4* In 2005, the Bankruptcy Abuse Prevention and Consumer Protection Act added § 1115<sup>2</sup> which,

similar to §§ 1306 and 1207, adds an individual debtor's postpetition earnings to property of the chapter 11 estate. The bankruptcy court found that the bonus received by Mr. Markosian post-conversion was property of Debtors' chapter 11 estate under § 1115(a)(2), a ruling not challenged in this appeal. However, § 1115 does not apply upon conversion from chapter 11 to chapter 7. Instead, § 348 governs the effect of a conversion.

**[\*276]** *HN5* Although § 348(f)(1)(A) expressly excludes a debtor's postpetition earnings from property of a chapter 7 estate upon conversion from chapter 13 — earnings that are included in the chapter 13 estate under § 1306(a)(2) — there is no parallel provision for chapter 11 debtors. In the absence of a specific statutory provision, we rely on *HN6* § 348(a), which by its plain language applies to all cases under Title 11, not just certain ones:

(a) Conversion of a case from a case under one chapter of this title to a case under another chapter of this title constitutes an order for relief under the chapter to which the case is converted, but, except as provided in subsections (b) and (c) of this section, does not effect a change in the date of the filing of the petition, the commencement of the case, or the order for relief.

*HN7* The statute expressly states that the date of the petition remains unchanged. "Where a case is converted from Chapter 11 to Chapter 7, property of the estate is determined by the filing date of the Chapter 11 petition, and not by the conversion date." *Magallanes v. Williams (In re Magallanes)*.

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(a) In a case in which the debtor is an individual, property of the estate includes, in addition to the property specified in section 541--

....

(2) earnings from services performed by the debtor after the commencement of the case but before the case is closed, dismissed, or converted to a case **[\*\*6]** under chapter 7, 12, or 13, whichever occurs first.

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<sup>2</sup> Section 1115 provides in relevant part:

[96 B.R. 253, 255 \(9th Cir. BAP 1988\)](#). [\*\*7] As of the petition date, [§ 541\(a\)\(6\)](#) excludes from the chapter 7 estate earnings from services performed by individual debtors after the commencement of the case. Therefore, by operation of [§ 348\(a\)](#), personal service income that came into Debtors' chapter 11 estate is recharacterized as property of the debtor under [§ 541\(a\)\(6\)](#)<sup>3</sup> when the case is converted to chapter 7. Accordingly, upon conversion, the bonus reverted to Debtors.

While other courts have come to a different conclusion, we respectfully disagree with their method of statutory interpretation. See [Pergament v. Pagano \(In re Tolkin\), 2011 Bankr. LEXIS 1336, 2011 WL 1302191 \(Bankr. E.D.N.Y. 2011\)](#); [In re Hoyle, 2013 Bankr. LEXIS 2640, 2013 WL 3294273 \(Bankr. D. Idaho 2013\)](#) (following [Tolkin](#)). In essence, they rely on Congress's failure to enact a parallel provision to [§ 348\(f\)\(1\)\(A\)](#) for chapter 11 debtors. The [Tolkin](#) court opined:

The language of [\[§ 1115\]](#) parallels the language of [§ 1306](#), and accomplishes the same goal of broadening the scope of property of the debtor's estate significantly beyond the parameters of [§ 541](#). However, unlike in a Chapter 13 case, there is no provision similar to [§ 348\(f\)](#) to modify the result upon conversion of a Chapter 11 case to another chapter. [In re Quillen, 408 B.R. 601, 620 n.33 \[Bankr. D. Md. 2009\]](#) (" . . . [Section 1115](#) . . . is identical to

[Section 1306](#). Curiously though, no counterpart to [Section 348\(f\)](#) was codified in BAPCPA to correspondingly adjust the reach of [Section 1115](#)."). Therefore, what is captured [\*\*9] as property of the debtor's estate under [§ 1115](#) remains as property of the estate, even after the conversion of the case to another chapter.

[\*277] [In re Tolkin, 2011 Bankr. LEXIS 1336, 2011 WL 1302191, at \\*10](#). Following [Tolkin](#), the court in [Hoyle](#) concluded that, "in light of the omission of a provision equivalent to [§ 348\(f\)\(1\)](#) applicable to the converted chapter 11 case, Debtor's arguments that the DIP accounts at conversion are not 'property of the estate' does [sic] not hold." [In re Hoyle, 2013 Bankr. LEXIS 2640, 2013 WL 3294273, at \\*7](#).

To be sure, nowhere does the [Tolkin](#) court mention [§ 348\(a\)](#), instead relying on Congress's failure to enact a provision parallel to [§ 348\(f\)\(1\)\(A\)](#) for chapter 11 debtors. Under this interpretation, [§ 348\(a\)](#) has no independent effect despite the statute's plain language that makes it applicable to all case conversions, including those from chapter 11 to chapter 7. See [Aluminum Co. of Am. v. Bonneville Power Admin., 903 F.2d 585, 590 \(9th Cir. 1990\)](#) (under statutory rules of construction, one provision of a statute should not be interpreted in a way which is internally contradictory or that renders other provisions of the same statute inconsistent or meaningless).

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<sup>3</sup>To the extent trustee contends that the postpetition earnings of Mr. Markosian are property of the chapter 7 estate by operation of [§ 541\(a\)\(7\)](#), we reject that argument. [HN8 Section 541\(a\)\(7\)](#) makes property of the estate any interest in property that the estate (not the debtor) acquires after the case. Here, the bankruptcy court found that the bonus constituted earnings from personal services of Mr. Markosian under [§ 1115\(a\)\(2\)](#) and that ruling was not appealed. Thus, the earnings fall within the earnings exception stated in [§ 541\(a\)\(6\)](#). We note however that there may be chapter 11 cases which are converted to chapter 7 where it is necessary to separate earnings from personal services by an individual from the earnings of a business. See [FitzSimmons v. Walsh \(In re FitzSimmons\), 725 F.2d 1208, 1211 \(9th Cir. 1984\)](#) [\*\*8] (holding that only the debtor's earnings from his own personal services were exempt under [541\(a\)\(6\)](#), as opposed to all profits generated by his law practice).

Further, the Ninth Circuit has cautioned [\*\*10] that [HN9](#) attempting "to divine congressional intent from congressional silence" is "an enterprise of limited utility that offers a fragile foundation for statutory interpretation." [Polar Bear Prods., Inc. v. Timex Corp., 384 F.3d 700, 717 \(9th Cir. 2004\)](#). Rather than creating a rule out of silence, we consider [§ 348\(f\)\(1\)\(A\)](#) in context. In this regard, Congress amended [§ 348](#) in 1994 to add [subsection \(f\)\(1\)\(A\)](#) well before it enacted [§ 1115](#). The legislative history of [§ 348\(f\)\(1\)\(A\)](#) shows that an



amendment was needed to resolve a split among courts concerning whether a chapter 13 debtor's postpetition earnings remained property of the estate upon conversion to chapter 7. *In re Evans*, 464 B.R. at 439 (citing cases and legislative history of § 348(f)(1)(A)). Given the reason for the amendment, the fact that Congress did not enact a parallel provision to § 348(f)(1)(A) for chapter 11 debtors when it enacted § 1115 holds little, if any, significance because there was no split of authority yet to resolve. See *Brown v. Gardner*, 513 U.S. 115, 121, 115 S. Ct. 552, 130 L. Ed. 2d 462 (1994) (congressional silence lacks persuasive significance).

In the end, there is no reason to treat chapter 11 debtors differently than chapter 13 debtors [\*\*11] in this context. As the *Evans* court pointed out, at the time Congress enacted § 348(f), it "clearly conveyed its purpose to avoid penalizing debtors who first attempt a repayment plan . . . [t]here is no policy reason as to 'why the creditors should not be put back in precisely the same position as they would have been had the debtor never sought to repay his debts . . .'" 464 B.R. at 441.

## VI. CONCLUSION

For the reasons stated, we AFFIRM.