

# U.S. Supreme Court Agrees To Hear Arizona Bankruptcy Case

*Three Gust Rosenfeld attorneys convince high court to take case*



*Editor's note: As the nation's final arbiter of legal disputes, the United States Supreme Court is petitioned by a vast number of litigants, but a very small number of cases are selected for review by the court. For example, in 2008, the highest court in the land received more than 10,000 petitions from parties seeking review of their cases—yet heard only about 100 cases. Merely presenting before the court is an honor and privilege as well as a challenging opportunity for attorneys.*

The United States Supreme Court has agreed to hear an Arizona case about the discharge of student loans in bankruptcy. Three Gust Rosenfeld attorneys petitioned the high court to take the case after the Ninth Circuit Court of Appeals ruled that a debtor's student loans could be forgiven in bankruptcy without showing "undue hardship" as Congress requires in the bankruptcy statutes. The case is *United Student Aid Funds v. Espinosa*, No. 08-1134.

Madeleine Wanslee, a creditors' rights and bankruptcy at-

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## Arizona Anti-Deficiency Saga Plays Out Like Primetime Drama

*Existing Statute Changed, Then Change Repealed, Future Uncertain*

### **PROLOGUE:**

This summer, the state legislature grappled with changing Arizona's anti-deficiency law, which protects homeowners who lose their homes in foreclosure from paying a "deficiency" on the property. A deficiency is the difference between the secured debt and the greater of the sale price or the home's fair market value.

Within a 3-month span, this issue unfolded like a primetime drama. Read more about each episode below.

### **EPISODE 1: STATUS QUO**

Arizona law has long protected a homeowner from liability for a foreclosure

deficiency if the home is 1) a residential property of 2-1/2 acres or less and 2) limited to and utilized as a single one-family or a single two-family dwelling.

Interpretive court opinions suggest that while the home must be used as a dwelling, it does not necessarily need to be utilized by the owner as a dwelling. A renter, vacationer, or part-time occupant will do.

### **EPISODE 2: THE CHANGE**

In July, the legislature passed a bill narrowing this anti-deficiency protection by making it applicable only to residential property occupied by the borrower for at least six consecutive months and for which a

certificate of occupancy had been issued.

Under this amendment, many rental or investment homes, Arizona homes occupied only part-time by out-of-state owners, or completed houses without a certificate of occupancy might no longer qualify for anti-deficiency protection.

Slated to go into effect Sept. 30, the new law left many questions unanswered: Would it apply to all existing loans? Or would it apply only to new loans made on and after September 30? Would it apply only to foreclosure sales conducted on and after September 30? And would it apply in cities or towns that don't issue formal certificates of occupancy?

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# COURT

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torney at Gust Rosenfeld, has been fighting this issue on behalf of a student loan guarantor in the Ninth Circuit and various lower courts for more than six years. Sean O'Brien, a bankruptcy attorney, and Charles Wirken, an appellate lawyer, assisted Wanslee in preparing the petition that persuaded the U.S. Supreme Court to hear the case.

"We are pleased that the U.S. Supreme Court has agreed to resolve this issue," Wanslee said. "The Ninth Circuit's decision is contrary to rulings in five other circuits. The court's ruling allows debtors to discharge student loans in a Chapter 13 Bankruptcy without proving 'undue hardship.' Doing so represents a substantial loss of rights for student loan holders."

Wanslee argues that the lower court's ruling fails to comply with bankruptcy law. If the Ninth Circuit's decision is upheld, she says it could adversely affect all student loan holders as well as other creditors typically afforded special treatment under bankruptcy law.

"If allowed to stand, this ruling could have wide-ranging implications that could result in the discharge of other special types of debt such as child support payments, drunk-driving damages, criminal penalties, and tax fraud fines," Wanslee said. "In addition, this ruling negatively impacts the public in general because discharged student loans are ultimately paid by all of us as taxpayers."

With more than 18 years of experience, Wanslee focuses her practice on creditors' rights and related state and federal court litigation, including commercial and consumer bankruptcy, foreclosure, replevin, deficiency and guarantor actions, collections, and loan workouts. She has handled more than 24 appeals on behalf of her clients. In addition, she is Board Certified in Consumer Bankruptcy Law by the American Board of Certification.

If you have questions about this case or other Arizona bankruptcy law issues, please contact one of the attorneys below.

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WANSLEE



O'BRIEN



WIRKEN

# ANTI-DEFICIENCY

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## EPISODE 3: THE RECKONING

The amendment generated heated reaction, particularly from the real estate, investment and development broker communities. After strong lobbying, the amendment was repealed on September 4, 2009 before it even went into effect.

## POTENTIAL EPISODE 4: HERE WE GO AGAIN?

So this leaves things the same, for now. In other words, the pre-summer anti-deficiency protections remain. However, the legislature will meet again next year. Stay tuned to see if this saga continues.

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# ET·Y·MOL·O·GY COR·NER

## The Magic of the Supreme Court



It should come as no surprise to anyone that "supreme" comes from the Latin "supremus" or the "highest" – thus the highest court. Oddly enough, the word "abracadabra," or magical formula, is linked to "supreme." It is derived from the Late Greek "Abraxas," a gnostic name for supreme god. Abracadabra is, thus, a word of great weight and power. Perhaps, when the Supreme Court issues an opinion, it should begin "Abracadabra"!

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# Bankruptcy Bargains:

## *Asset Acquisitions for Buyers, Financing Opportunities for Lenders*

*I was seldom able to see an opportunity until it had ceased to be one. – Mark Twain*

The current economic environment has created opportunities both for those seeking to acquire assets and for those lenders willing to finance distressed-asset acquisitions. These opportunities are arising with greater frequency in the context of bankruptcy court sales made under Section 363 of the Bankruptcy Code.

### **BUYER BENEFITS OF BANKRUPTCY SALES**

Whether under Chapter 7 or Chapter 11, bankruptcy sales offer the buyer significant benefits and protections that generally do not exist in an otherwise distressed-asset sale. The key benefit is that it makes the resulting sale “free and clear,” meaning that the buyer acquires the assets free and clear of all liens, claims and encumbrances. Caution should be exercised, however, because certain claims—such as environmental and product liability claims—may survive the sale and instead pass to the buyer.

Another buyer benefit associated with bankruptcy sales is that a purchaser who acts in good faith, pays value, and acts without knowledge of adverse claims in the sale transaction is entitled to special protection under the Bankruptcy Code. Specifically, the Bank-

ruptcy Code provides that a sale to a good faith purchaser cannot be reversed or set aside on appeal. It is therefore important for any sale order to make these very specific findings.

### **LENDER CHALLENGES**

From the lender’s perspective, there are challenges when determining whether to finance an acquisition out of bankruptcy. First, the lender should thoroughly understand the sale procedure, which is most often an auction. That process starts with the Bankruptcy Court’s approval of bidding procedures that establish the rules of the auction including key dates, advertising requirements, bidder pre-qualification, submission of opening bids, and the due diligence period. Also regulated is the auction process, which involves bidding rules such as bid increments, sale approval and closing.

Lenders are typically asked to issue a loan commitment during the due diligence period. Thus, a potential lender will usually need to move quickly to fund the transaction. Financing should be conditional based on the lender’s approval of a proposed sale order determining that the buyer is a good faith purchaser.

### **OBLIGATIONS OF BUYERS AND LENDERS**

Buyers and lenders alike must conduct due diligence in all areas of the sale.

This includes:

- Understanding the property’s history and condition.
- Knowing who may assert liens on the assets to be sold and other interested parties such as utility companies, local taxing authorities, landlords, other creditors, etc.
- Paying special attention to the notice given, making sure it’s done properly in order to avoid later efforts to set aside the sale order.

### **RECOGNIZING THE OPPORTUNITY**

As Mark Twain noted, opportunity is sometimes hard to recognize. If you do recognize a bankruptcy sale opportunity, remember that every opportunity brings risk. Experienced bankruptcy counsel can help you avoid some risk by ensuring there will not be any post-closing challenges or surprises for either the lender or the borrower.

Your legal counsel can help you tackle any bankruptcy sale issues by analyzing the transaction and assisting in preparing the critically important sale order and the acquisition and financing documents.

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# Arizona Legislative Updates

The Arizona Legislature recently passed a number of new laws. We highlight a few below:

## OPEN MEETING LAW CHANGES (SB 1303)

Before Senate Bill 1303 passed, cities and towns with a population of more than 2,500 were required to post the following items on the community's website:

- A record of the meeting within 3 days of its occurrence
- A statement describing legal actions taken by the municipality
- The approved minutes of the meeting within 2 days of the approval of that meeting's minutes

Now, changes to the law under Senate Bill 1303 require these postings to remain on the city or town's website for one (1) year after the required posting.

In addition, this bill states that a public body that is required to post an agenda 24 hours before any meeting may now include Saturdays in that calculation as long as the public has physical access to the posting location on Saturday in addition to access to the public body's website.

## CHARTER SCHOOL ZONING CHANGES (HB 2099)

House Bill 2099 addresses how charter schools are treated under local zoning laws. Before the new law, charter schools were treated as public schools only for the purposes of assessing fees including site plan fees and development fees.

Now, under House Bill 2099, charter schools are treated as public schools for zoning purposes as well. Arizona's public schools are generally exempt from city, town or county zoning restrictions. This means that there are generally no zoning restrictions on where a public school—and now a charter school—may be developed in a local community.

In addition, House Bill 2099 allows municipalities and counties to adopt a zoning restriction that prohibits a charter school from operating in an existing single-family residence located on property smaller than 1 acre. Finally, the law clarifies that charter schools are subject to building codes, including life and safety building codes, of the local community and state.

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## Federal Stimulus Legislation Affects COBRA Coverage

Employees who are involuntarily terminated between September 1, 2008 and December 31, 2009, and their covered dependents, are eligible for a 65 percent subsidy of their COBRA premiums for up to nine months.

- Employees pay 35% and employers may recover 65% as a credit against income tax withholding and FICA taxes. To receive the payroll tax credit, employers must submit reports to the Treasury Department.
- The 65% subsidy does not apply to those with adjusted gross income above \$125,000 (\$250,000 joint) in the year received.
- Employees terminated involuntarily on or after September 1, 2008 who did elect COBRA are eligible, but the subsidy is not retroactive.
- Employees who elected COBRA

initially but lost coverage due to non-payment of premiums will be entitled to notice and the premium subsidy.

- The premium assistance paid by the employer/government is not taxable.
- Employers must provide notice to eligible individuals. Model notices for the COBRA subsidy can be found at: <http://www.dol.gov/ebsa/COBRA.html>.
- A person covered by COBRA who becomes eligible for another health plan or ceases to be eligible for premium assistance must notify the employer or otherwise will be required to pay a penalty equal to 110% of the premium reduction.

### FOR MORE INFORMATION

If you have any questions, please



contact any of our firm's Employment Law attorneys:

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# PERSONAL NOTES

**Timothy Barton** is a member of the Board of Directors of Desert Mission, the community service arm of John C. Lincoln Health Network.

**Peter Collins, Jr.**, was named one of the *Best Lawyers in America*® again for 2010, and was also named one of Tucson's Top Lawyers for insurance law by *Tucson Lifestyle Magazine*.

**Peter Collins, Jr.**, and **Chas Wirken** served as faculty members of the 2009 Arizona College of Trial Advocacy. Peter and Chas revived the College five years ago and the program has quickly become a staple of high-quality continuing legal education for young lawyers in Arizona.

**John Hay** facilitated a workshop on Professionalism for the State Bar of Arizona in August. In September, he gave a National Business Institute presentation on drafting LLC agreements.

**Marty Jones** was invited by the International Conference on Shopping Centers to host a roundtable discussion about the Importance of Environmental Due Diligence in Real Estate Transactions at the 2009 ICSC Law Conference in October.

**Ming Kang** spoke about real estate law to members of the

Taiwanese American Association of Arizona.

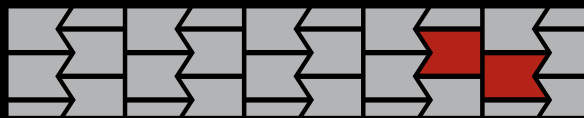
**Scott Malm** spoke at a National Business Institute seminar on boundary law.

**Craig McCarthy**, his wife Elizabeth and their three children have been selected as "Family of the Year" by the Ahwatukee Foothills branch of the Valley of the Sun YMCA Association. In November, the organization will present the McCarthys with a plaque at an awards ceremony at U.S. Airways Center. McCarthy serves on the branch's Board of Directors and is co-chair of a capital campaign to build a new teen center and pre-school facility. In addition, McCarthy is a member of the Board of Directors for the Arizona Association of Defense Counsel (AADC).

*Arizona Business* magazine named **Chris McNichol** one of the "Top Lawyers" in Real Estate and Construction law. He is also the new Chair of the Arizona Conservation Acquisition Board. Recently, he spoke on real estate issues at various conferences, including at the Arizona Trustee Association's Convention, at the Arizona School of Real Estate, and at the State Bar of Arizona's "Ins and Outs of Foreclosure" program in San Diego.

In June, **Melanie McBride** was admitted to the U.S. Supreme Court, and she attended the swearing in ceremony in Washington, D.C.

**Chas Wirken** is co-chair of the Mesa United Way 2009-2010 campaign. In addition, he is co-president of the Lorna Lockwood Inn of Court for 2009-2010. The American Inn of Court program is designed to improve civility and professionalism among lawyers.



## Red Flags Rule Delayed

The Federal Trade Commission announced that the August 1, 2009 enforcement date of the Red Flags Rule will be delayed until November 1, 2009. The purpose of the extension is to enable businesses to gain a better understanding of the Rule and any obligations that they may have under it.

The delayed enforcement does not prevent other federal agencies (e.g., federal bank regulatory agencies) from enforcing the original November 1, 2008, compliance deadline for institutions subject to their oversight.

The Red Flags Rule applies to any business that extends credit to customers. The program is intended to help fight identity theft. Further information can be found at the FTC website: [www.ftc.gov/redflagsrule](http://www.ftc.gov/redflagsrule).

If you have any questions about the Red Flags Rule, please contact David Pennartz at 602.257.7418 or [dpennartz@gustlaw.com](mailto:dpennartz@gustlaw.com).

## Gust Rosenfeld Donates Thousands of Cookies To Local Children's Hospital

When David Pennartz asked his co-workers to participate in a last-minute cookie drive this summer, he thought he'd get a few boxes of treats to give to the Phoenix Children's Hospital Foundation, where he serves as a community volunteer. He never imagined that his fellow attorneys and support staff

would donate thousands of cookies to his cause within just a 2-day period. One anonymous cookie donor even sneaked into David's office and created this impressive cookie pyramid.



## Recent Changes to Arizona's Concealed Weapon Law

Arizona Governor Jan Brewer recently signed two laws clarifying the rules governing carrying a concealed firearm in our state. Both are effective Sept. 30, 2009.

### EMPLOYERS CAN'T PROHIBIT FIREARMS IN EMPLOYEE VEHICLES

This law affects any employer wishing to restrict their employees' transportation or storage of firearms in the employees' vehicles. With only a few narrow exceptions, employers can't prohibit a person from lawfully transporting or storing a firearm in the employee's private vehicle in the employer's parking lot, so long as the firearm is in a locked vehicle and is not visible from outside the car or motorcycle.

Employers can impose restrictions on vehicles owned or leased by the employer and used by employees in the course of their employment, unless their employment requires employees to store or transport a firearm for their work.

### CARRYING FIREARMS INTO BARS & RESTAURANTS

The second new law allows concealed weapon permit holders to carry their firearms into a bar or restaurant as long as 1) the bar or restaurant owner does not prohibit permit holders from doing so by posting a specific sign prohibiting firearms, 2) the firearm remains



concealed, and 3) the permit holder does not consume any alcohol. It is unlawful for a permit holder to consume alcohol in a bar or restaurant while carrying a firearm.

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