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Feature

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Does *Fulton* Provide Relief for Colleges that Withheld Transcripts?

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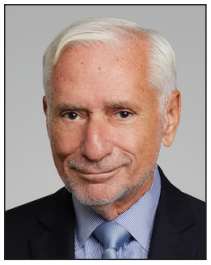

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Schools routinely withhold the transcripts of students who are unable or unwilling to pay their school tuition. To get around this limitation, some students have been using the bankruptcy system by filing for bankruptcy after not paying their tuition, then seek the release of their transcripts. Is the U.S. Supreme Court's *Fulton* decision[2] interpreting language in § 362(a)(3) of the Bankruptcy Code as requiring an affirmative act a game-changer for colleges (and other schools) in the contest over whether schools can withhold transcripts without violating the automatic stay?

Before *Fulton*, cases came out decidedly in favor of students, permitting them to obtain the full benefit of the student/school bargain without having to pay their tuition, and doing so even where the debtor could afford to pay.[3] *Fulton* might level the playing field for schools if § 362(a)(6) regarding debt collection is interpreted the same way *Fulton* interpreted the nearly identical language in § 362(a)(3), as at least one court has already done.[4]

Statutory Construction

Like any debtor/creditor dispute in bankruptcy, courts should look for guidance in the language of the applicable Code sections. In *Fulton*, the Court did that in the context of what the City of Chicago did in refusing to return automobiles that it impounded for unpaid fines. But while *Fulton* interpreted § 362(a)(3), the tuition cases hinge upon § 362(a)(6). The language used in these subsections is virtually the same, and other applicable Code provisions support extending *Fulton* to § 362(a)(6).[5]

Fulton was expressly a narrow decision[6] and addressed different facts. In *Fulton*, the Supreme Court reversed the Seventh Circuit decision that the City of Chicago violated the stay by refusing to return vehicles after the owners filed chapter 13 petitions. The Court focused on § 362(a)(3), which prohibits "any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate."

Specifically, the Court addressed whether a mere refusal to turn over the vehicles was an act to exercise control over property of the estate: "[T]aken together, the most natural reading of these terms — 'stay,' 'act,' and 'exercise control' — is that § 362(a)(3) prohibits affirmative acts that would disturb the *status quo* of estate property as of the time when the bankruptcy petition was filed."[7] The Court further observed that "the combination of these terms is that § 362(a)(3) halts any affirmative act that would alter the *status quo* as of the time of the filing of the bankruptcy petition."[8]

The Court found that any ambiguity in § 362(a)(3) was resolved "by the existence of a separate provision, § 542, that expressly governs the turnover of estate property."[9] The Court explained that reading "act" in § 362(a)(3) to include an omission renders § 542 superfluous (*i.e.*, why would § 542 be needed if § 362(a)(3) did the job?). The Court also found that if read to include

1 The authors and their firm represent creditors and debtors in their national and international Bankruptcy and Creditors' Rights Practice. The firm's Higher Education Practice Group is a multi-disciplinary team committed to helping colleges and universities navigate the ever-changing higher education landscape.
2 *City of Chicago v. Fulton*, 141 S. Ct. 585 (2021).
3 *See In re Kuehn*, 563 F.3d 289, 290-91 (7th Cir. 2009).
4 *See Margavitch v. Southlake Holdings LLC, et al. (In re Margavitch)*, Case No. 5:19-05353-NJC, Adv. No. 5:20-00014-MJC, 2021 WL 4597760, at *6 (Bankr. M.D. Pa. Oct. 6, 2020).
5 As discussed herein, *Fulton*'s rationale should also apply to the interpretation of the term "act" in § 524, the discharge section of the Bankruptcy Code. Among other things, § 524 provides that a "discharge in a case under this title ... operates as an injunction against ... an act, to collect, recover or offset any [discharged] debt as a personal liability of the debtor."
6 *Fulton*, 141 S. Ct. at 593 (Sotomayor, J. concurring).
7 *Id.* at 587.
8 *Id.* at 590.
9 *Id.*

inaction, § 362(a)(3) would contradict § 542's exception for property that is of "inconsequential value or benefit to the estate."[10] Although not addressed in *Fulton* — but addressed by the Court in an analogous situation in *Citizens Bank of Md. v. Strumpf* — construing § 362(a)(3) as an affirmative turnover provision would render such right to adequate protection a nullity.[11]

Fulton's holding and rationale raise the obvious question of why "act" as used in § 362(a)(6) — the stay section on which findings of college stay violations are based — should be given any meaning different from neighboring § 362(a)(3). Colleges can use the maxim of statutory construction that presumes identity of meanings of a word used in different parts of a statute.[12] The proximity of subsections using identical words further supports this interpretation.[13]

As previously noted, the *Fulton* Court looked to other parts of the Bankruptcy Code to inform its interpretation and concluded that § 542 supported that § 362(a)(3) requires an affirmative act. *Fulton* involved the concept of turnover of property, which is arguably inapplicable to the tuition scenario. Rather, in the tuition scenario, executory contract provisions of § 365 support the identical interpretation.

An implied contract exists between a student and a school,[14] which is executory if the school has not provided the transcript and the student has not paid tuition.[15] The school's obligation to provide a transcript is material; many cases have awarded significant damages for a school's refusal to provide one.[16]

Thus, if the contract is executory, § 365 gives the school certain rights and protections, such as requiring a student to pay the tuition as a condition to assuming the contract.[17] Rejection excuses the school from further performance to the extent that the student's breach would excuse such performance.[18]

If § 362(a)(6)'s use of the term "act" was interpreted to include merely maintaining the *status quo*, that interpretation would vitiate these rights. Such an interpretation would allow exactly what § 365 is meant to prevent: a debtor obtaining the benefits of an executory contract without accepting its burdens. If a school was compelled to provide the transcript immediately or be found in violation of the stay, a motion to compel the student to either assume or reject the contract would instantly be moot, rendering § 365 protections a nullity. Similarly, the *Strumpf* Court held that a bank placing an administrative hold on a debtor's bank account to protect its setoff rights did not violate the stay because to rule otherwise would render such protections a nullity.[19]

Furthermore, interpreting the term "act" in the school's favor to exclude withholding a transcript would not prejudice the student debtor, who would have all rights — *just not enhanced rights*. If the student was not in breach of contract, the school would have to perform its obligations or face damages or injunctive relief. Conversely, there is nothing in the Code that states that the school must perform where the student's payment breach would excuse performance.[20] Considering *Fulton*, and in view of how such an interpretation would change the status quo by vitiating important rights provided to the counterparty, any contrary holdings based on § 362(a)(6) appear to have lost their foundation.

Policy Considerations

A contrary view not only destroys important rights under § 365, it opens up an avenue for abuse. As one case demonstrates, a student who can afford to pay tuition could choose to use funds for other purposes.[21] A lawyer tells a student that she can file for bankruptcy, threaten the school with a stay violation and obtain the transcript in short order using § 362(a)(6).[22] She could then simply dismiss her case as of right if it were filed under chapter 13, or "fail" to fulfill routine debtor requirements and likely have her case dismissed if it were filed under chapter 7. Such abuse would not be possible if the student had to assume the burdens along with the benefits, rather than use the stay to compel immediate performance.

However, as Justice Sonia Sotomayor raised policy concerns about keeping debtors from their cars when needed to get to jobs,[23] a similar catch-22 may arise in the tuition situation: How can a student get the money to repay tuition if she cannot obtain employment dependent on the transcript? As Justice Sotomayor also pointed out, this policy issue is one for the legislature. She suggested the possibility of Congress permitting turnover proceedings to be contested matters rather than slow-moving adversary proceedings. She did not suggest that Congress erase adequate protection rights under § 542. Similarly, if Congress considers any Code changes in the tuition context, it should tread lightly in eliminating important creditors' rights under § 365 and account for financial hardships faced both students and colleges.

Conclusion

How can schools use *Fulton* to avoid getting slapped with a stay violation? Many courts find that there is no "willful" violation of the stay where the school believes in good faith that it was not violating the stay and can point to supporting authority.[24] *Fulton* and the burgeoning case law[25] applying it to alleged § 362(a)(6) violations should fulfill the requirement for such authority.

10 *Id.*
11 *See* 516 U.S. 16, 20 (1995).
12 *See IBP Inc. v. Alvarez*, 546 U.S. 21, 34 (2005).
13 *See C.I.R. v. Lundy*, 516 U.S. 235, 250 (1996).
14 *See Ferdele v. Marist Coll.*, Case Nos. CV 3559 (VB), 20 CV 3584 (VB), 2021 WL 3540432, at *3 (S.D.N.Y. Aug. 10, 2021); *Flatschef v. Manhattan Sch. of Music*, Case No. 20 CIV. 4496 (KPF), 2021 WL 3077500, at *5 (S.D.N.Y. July 20, 2021); *Thiele v. Bd. of Trs. of Ill. State Univ.*, Case No. 1:20-cv-01197-SLD-TSH, 2021 WL 4496941, at *6 (C.D. Ill. Sept. 30, 2021); *Doe v. Brandeis Univ.*, 177 F. Supp. 3d 561, 593 (D. Mass. 2016).
15 *See, e.g., Spyglass Media Grp. LLC v. Bruce Cohen Prod. (In re Weinstein Co. Holdings LLC)*, 997 F.3d 497, 504 (3d Cir. 2021). Material breaches are those that go "to the root or essence of the contract." *Lewis Bros. Bakeries Corp. v. Interstate Brands Corp. (In re Interstate Bakeries Corp.)*, 751 F.3d 955, 963 (8th Cir. 2014) (citing 15 *Williston on Contracts* § 44:55).
16 *See, e.g., Aleckna*, 13 F.4th at 341; *see also Nw. Airlines Inc. v. Klinger (In re Knutson)*, 563 F.2d 916, 917 (8th Cir. 1977).
17 11 U.S.C. § 365(b)(1)(a); *see NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 531-32 (1984); *In re Fleming Co. Inc.*, 499 F.3d 300, 308 (3d Cir. 2007); *In re New York Skyline Inc.*, 432 B.R. 66, 77 (Bankr. S.D.N.Y. 2010); *In re Buffets Holdings Inc.*, 387 B.R. 115, 119 (Bankr. D. Del. 2008).
18 The nondebtor's rights in light of such breach will be determined in accordance with state law. *See Med. Malpractice Ins. Ass'n v. Hirsch (In re Lavigne)*, 114 F.3d 379, 387 (2d Cir. 1997); *Abboud v. Ground Round Inc. (In re The Ground Round)*, 335 B.R. 253, 261 (B.A.P. 1st Cir. 2005). Many courts have held that if a debtor has until confirmation to assume or reject an executory contract but does neither under a confirmed plan, the contract will "ride through" the bankruptcy and continue to govern the parties' rights. *See Bildisco & Bildisco*, 465 U.S. at 546 n.12 (Brennan, J. concurring).
19 *Supra* n.11.
20 *In re Lucre Inc.*, 339 B.R. 648, 658-59, 662 (Bankr. W.D. Mich. 2006); *In re Billingsley*, 276 B.R. 48, 53 (Bankr. D.N.J. 2002).
21 *Supra* n.3.
22 *Id.*
23 *See Fulton*, 141 S. Ct. at 593.
24 *See In re Univ. Med. Ctr.*, 973 F.2d 1065, 1088 (3d Cir. 1992)); *see also Stancil v. Bradley Invs. LLC (In re Stancil)*, 487 B.R. 331, 343 (Bankr. D.D.C. 2013).
25 *Supra* n.4.

If handled properly, the worst-case scenario should be that the court orders that the transcript be delivered (with the possibility for a stay pending appeal). One thing that a school should probably not do is communicate expressly and affirmatively to the student that if he/she pays the tuition, it will release the transcript. That message should be conveyed through a motion in the bankruptcy court, which would not constitute a stay violation.[26] The school should move for a ruling that the stay does not apply.[27] If the student has already obtained the discharge, the approach would be similar except that the school should defend any motion for sanctions for a discharge violation by arguing that the term "act" in § 524 should be read the same as in § 362. A debtor is always free to pay a discharged debt,[28] or reaffirm a discharged debt.[29] If a student pays the tuition, the college could then provide the transcript, but it should not take the risk of "acting" by making that offer. abi

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26 *See Nelson v. Providian Nat'l Bank (In re Nelson)*, 234 B.R. 528, 534 (Bankr. M.D. Fla. 1999); *Armco Inc. v. N. Atl. Ins. Co. (In re Bird)*, 229 B.R. 90, 94 (Bankr. S.D.N.Y. 1999).
27 *See In re Mu'min*, 374 B.R. 149, 163 (Bankr. E.D. Pa. 2007).
28 *See* 11 U.S.C. § 524(f).
29 *See* 11 U.S.C. § 524(c).