IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

NO. 34944

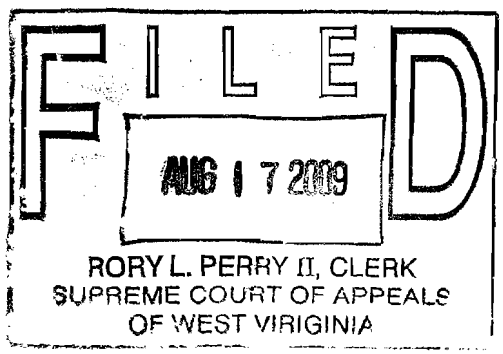
JAMES G. CLAY and
MICHAEL R. CORBETT

Appellants

vs.

STATE OF WEST VIRGINIA CONSOLIDATED
PUBLIC RETIREMENT BOARD

Appellee



APPEAL FROM THE CIRCUIT COURT OF KANAWHA COUNTY
Civil Action No. 05-MISC-371
Honorable James C. Stucky, Judge

REPLY BRIEF OF APPELLANTS JAMES G. CLAY AND MICHAEL R. CORBETT

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The Appellants, James G. Clay and Michael R. Corbett, submit this Reply Brief in response to the brief of the Appellee.

There are several factual errors in the recitation of the facts in the Consolidated Public Retirement Board's brief which require correction or clarification.[1] It is also appropriate, in view of the Appellee's arguments, to revisit briefly and clarify certain issues addressed by Appellee.

A. The Lack of Notification by TRS to the Appellants.

The TRS asserts that the Appellants Clay and Corbett were "sent notice" by "memorandum dated January 22, 1990" . . . "that although the bankruptcy filing caused payroll deductions to stop, it did not discharge the balance owed and that any balance would be collected when he retired or withdrew his contributions." Appellee's Brief at 3, 5, 10. Appellee's counsel is apparently referring to the memorandum written by James Swart, which is dated January 22, 1990, discussed in Appellant's Brief at 4-6. The Swart memorandum did not exist until some three years after the bankruptcy proceedings of the Appellants. There is no evidence that it was ever sent to Clay and Corbett, nor was anything else until 2003.

A copy of the Swart memo was apparently placed in their files maintained by the TRS at some point, but there is no evidence of when it was placed in the file, nor was there any evidence it was sent to the Appellants at any time. Both denied under oath that they had ever seen it. There is no cover letter, note, return receipt, or anything else in their files or elsewhere indicating that it had been mailed to the Appellants at any time.

The memo itself is clearly an internal memorandum, addressed to the director of the TRS by

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[1]The Consolidated Public Retirement Board administers the Teachers' Retirement Fund, the specific pension plan at issue. For consistency with the Appellants principle brief, both entities will be designated herein as the "TRS."

its legal counsel, discussing how to handle bankruptcy situations. On its face, it is highly unlikely that the internal memo was a document that would be sent to participants without at least a cover letter or some further explanation that would be comprehensible to a participant. The Administrative Law Judge made no finding that the Swart memo was ever sent to the Appellants.

See, Appellants' Brief at 5, n.7.

Not only is there no evidence that the Appellants received the Swart memo in 1990, there is no evidence that Clay or Corbett received any notice from the time of the bankruptcy in 1986 until 2003 that the TRS took the position that the debt was still owed and accruing interest notwithstanding the bankruptcy. Appellants' Brief at 2-9. A two-sentence letter at the time of the bankruptcy would have avoided this entire situation. The absence of such a communication suggests that the TRS either did not have such a position and presumed, as did the Appellants, that the debt was discharged or negligently failed to assert its position in the bankruptcy case.

B. The Appellants Do Contend that the Debt Was Discharged.

The TRS's statement that the Appellant's do not contend that the loans were discharged is also a misstatement. The Appellants do contend that the debt was in fact discharged, because the loans were listed in the petition as a debt, the TRS was notified, the bankruptcy court issued a discharge to the debtors, and the TRS failed to object to the discharge. See, Appellant's Brief at 10-15. Under the Bankruptcy Code and rules, the debt was discharged. There was no statutory provision making pension loans nondischargeable at the time of their bankruptcies.

It is quite possible that had the TRS objected to the discharge, it might have prevailed at the time on based upon In re Villarie, 648 F.2d 810 (2d Cir. 1980), although there are factual differences

which may have produced a different result and subsequent case law has undermined the reasoning of the Villarie decision. The pension fund in Villarie, unlike the TRS, objected to the discharge, and Villarie decision was an appeal from the bankruptcy's court's ruling that the claim was dischargeable. The holding in Villarie holding depended upon specific provisions of the New York City Administrative Code which apparently did not give the pension fund any remedy to recover the loan other than payroll deduction. That option was blocked by the bankruptcy judge's ruling that the debt was discharged. There was no such obstacle in this case, since the TRS could have resumed the mandatory payroll deductions once the bankruptcy cases were closed and the stay lifted, and could have filed suit on the promissory notes which the Appellants had signed.

Although the debts were discharged by the TRS' failure to object in the bankruptcy cases, the Appellants have always been willing to repay the money they borrowed, since they were first notified in 2003 that the TRS claimed that the debt was still owed. In fact Mr. Clay has already done so. They agree that they borrowed the money, and since they are seeking equitable relief, it is fair and equitable that they repay what they borrowed. What they object to is the demand of the TRS that they also pay sixteen years of interest, enforced by the TRS' control of their pensions, which was entirely the result of the neglect and failures of the TRS to assert its position or even notify the Appellants, to whom the TRS owed a fiduciary duty, that the debt was still owed during that sixteen years. It is unfair and inequitable, where the actions, inaction, and silence of the TRS reasonably led the Appellants to believe that the debts were discharged, to require the Appellants to pay for the failures and neglect of the TRS for those sixteen years.

C. The TRS Loans Were "Debts" and "Claims" Under the Bankruptcy Code.

The TRS continues to argue that the loans obtained by the Appellants were not "debts" subject to discharge in bankruptcy and for which "there is no obligation to pay it back." The TRS' assertion that the loans were not enforceable relies entirely on the Villarie case, a three-page, per curiam decision issued soon after the enactment of the Bankruptcy Code and before the scope of the definition of "claim" and "debt" had been construed by the Supreme Court and lower courts.[2] The Supreme Court in Johnson v. Home State Bank, 501 U.S. 78, 111 S.Ct. 2150, 115 L.Ed.2d 66, 59 (1991) stated that:

> We have previously explained that Congress intended by this language to adopt the broadest available definition of "claim." See Pennsylvania Dept. of Public Welfare v. Davenport, 495 U.S. 552, 558, 563-564, 110 S.Ct. 2126, 2130-2131, 2133-2134, 109 L.Ed.2d 588 (1990); see also Ohio v. Kovacs, 469 U.S. 274, 279, 105 S.Ct. 705, 707, 83 L.Ed.2d 649 (1985). In Davenport, we concluded that "right to payment' [means] nothing more nor less than an enforceable obligation . . . " 495 U.S., at 559, 110 S.Ct., at 2131.

See, the analysis of these decisions in In re Buchferer, 216 B.R. 332, 335-351 (Bankr. E.D.N.Y. 1997).

The language of the statute itself, as well as the loan agreement makes it clear that there is an

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[2] The Bankrupcy Code defines the term "claim" as

(A) right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured; or

(B) right to an equitable remedy for breach of performance if such breach gives rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured."

enforceable obligation. The borrower is required to repay the loan within five years, and the TRS can clearly enforce that obligation if the borrower fails to do so:

> (5) From his or her monthly salary as a teacher or a nonteacher the member shall pay the loan and interest by deductions which will pay the loan and interest in substantially level payments in not more than sixty nor less than six months. *Upon notice of loan granted and payment due, the employer is responsible for making the salary deductions and reporting them to the Retirement Board. At the option of the board, loan deductions may be collected as prescribed herein for the collection of members' contribution, or may be collected through issuance of warrant by employer. If the borrower is no longer employed as a teacher or nonteaching member, the borrower must make monthly loan payments directly to the Consolidated Public Retirement Board and the Board must accept the payments.*
>
> (6) *The entire unpaid balance of any loan, and interest due thereon, shall, at the option of the retirement board, become due and payable without further notice or demand upon the occurrence with respect to the borrowing member of any of the following events of default: (A) Any payment of principal and accrued interest on a loan remains unpaid after the same becomes due and payable under the terms of the loan or after such grace period as may be established in the discretion of the retirement board;* (B) the borrowing member attempts to make an assignment for the benefit of creditors of his or her refund or benefit under the retirement system; or (C) any other event of default set forth in rules promulgated by the board in accordance with the authority granted pursuant to section one, article ten-d, chapter five of this code: Provided, That any refund or offset of an unpaid loan balance shall be made only at the time the member is entitled to receive a distribution under the retirement system.
>
> West Virginia Code § 18-7A-34(a)(5), (6).

The loan agreement is a promissory note, and nothing in the statute prohibits the TRS from enforcing the note like any other promissory note:

> This note evidences a loan obtained by me in pursuance of the provisions of [18-7A-34], and the provisions of that section are made a part hereof. In installments, for value received, I promise to pay to the TEACHERS RETIREMENT BOARD, an instrumentality of the State of West Virginia, created by [18-7a] of the West Virginia Code, the principal sum of ___, with interest from the date hereof at the rate of __% per annum, add on method of calculation, not to exceed an annual actuarial percentage rate of 14.68% based on term of loan.

The argument of the TRS that the its loan was not a "claim" within the meaning of the

Bankruptcy Code because it was not an "enforceable obligation" is untenable in view of the Supreme Court's rulings in Johnson v. Home State Bank, *supra*, Ohio v. Kovacs, 469 U.S. 274, 105 S.Ct. 705, 83 L.Ed.2d 649 (1985), and other rulings. Even if the ruling in Villarie was correct on the specific facts in that case, it is clearly distinguishable from the situation in this case.

The loans to the Appellants were enforceable obligations and therefore "claims." Nothing in the statute prevented the TRS from reinstating the mandatory payroll deduction, collecting the debt by warrant, or suing them on the notes. The only restriction on its right to enforce the loan obligation is the proviso in 18-7A-34(a)(6) that it cannot offset the debt against the TRS account until the member is entitled to receive a distribution. There is no restriction against collecting the loan from the member's wages. Both Clay and Corbett remained in the system for more than sixteen years, and the TRS could have collected the debt at any time. The failure to do so, coupled with the failure to even advise the Appellants that the TRS contended that the debt was still owed, contributed to the reasonable belief of the Appellants that the debt had been discharged.

D. The Actions of the TRS Compelled the Appellants to Exhaust the TRS' Administrative Procedures.

The Appellee suggests that the Appellants lack faith in their argument that the loans were discharged because they have not sought to reactivate a pair of 23-year-old bankruptcy cases, in two different districts, and seek a contempt citation from the bankruptcy courts.

The Appellants brought this proceeding because they were required to exhaust the administrative remedies provided by the statute. The Appellee chose the forum because it controls the payment of the Appellants pensions, and initiated this action by insisting that the Appellants pay sixteen years of interest or have their pensions held hostage and reduced. If the Appellants had failed

to exhaust their administrative remedies under the CPRB and TRS, Appellants are confident that the Appellee would be seeking dismissal for failure to exhaust those remedies.

E. The TSR's Submission of Facts Not in the Records Should be Disregarded.

The TRS asserts for the first time in Appellee's Brief that there are 111 members of the TRS who have filed bankruptcy and later discovered that their loans were not discharged and are repaying their loans, apparently when the TRS first took this position.[3] That evidence was not introduced in the record below, and the Appellant's have no information and had no opportunity to investigate such a claim. The crux of the matter in this proceeding was the failure of the TRS to tell the Appellants that the loan obligation was not discharged for a period of 16 years. Their bankruptcies were in 1986, some three years before the Swart memorandum, when the first documentation that the TRS took that position appeared. There is evidence in the administrative record that at some point in the 1990s, attorneys representing the TRS (including Kit Francis) appeared in bankruptcy cases and asserted the position that the debts were not dischargeable. To the extent that later members who filed for bankruptcy were notified by TRS counsel that loans were not dischargeable, they were at least on notice, unlike the Appellants. By 2003, the TRS was sending to loan applicants a document reasonably notified the recipients of the TRS' position, and since the amendment to the Bankruptcy Code in 2005, everyone is on notice that such a loan is not dischargeable. Those who were on notice are in a very different situation. We do not know how many TRS members were in situations similar to those of the Appellants.

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[3]The TRS indicates that there are 92 others, and perhaps more, with loans on which interest was erroneously calculated, although apparently in non-bankruptcy situations.

The TRS also submits calculations of the amount of the reduction implemented in the pension benefit of Mr. Clay, and a calculation of that which Mr. Corbett might expect if he retired. Appellee contends that Clay's benefit was reduced from $2,134.60 to $2,077.27, and Corbett's would be reduced from from $2,673.52 to $2,408,56 if he retired now.[4] A $265 reduction of a $2673 pension for the rest of his life is not a trivial matter. Appellants are not privy to the methodology by which the TRS reached those figures, particularly since the pension benefit is based upon service and salary, not directly on the participant's contributions.[5] Appellants therefore do not necessarily agree that the amounts are correct, and depending on the Court's ruling further proceedings may be necessary.

With respect to the other issues, Appellants believe that those issues are sufficiently set forth in the Appellants' Brief, and further discussion of those issues would be redundant.

CONCLUSION

For the reasons set forth herein, and the arguments in Appellant's Brief, the Appellants respectfully submit that the decision of the Circuit Court of Kanawha County was erroneous and should be reversed. The Appellants should be allowed to repay the debts, consistent with their long-standing proposals to pay the principal and only the interest which would have accumulated had they been advised at the time that their debts had not been discharged.

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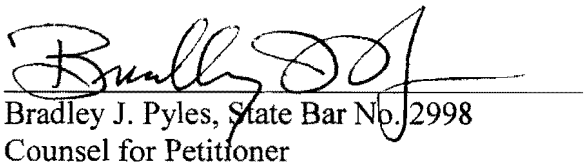
[4]It should be noted that Clay has already repaid the principal and some of the interest in response to the demand letter in 2003, before the interest was recalculated and the amount claimed more than quadrupled, but still will lose $57 a month for the rest of his life.

[5]See Appellant's Brief at 12, n. 13.

JAMES G. CLAY
MICHAEL R. CORBETT
Appellants, by Counsel



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CERTIFICATE OF SERVICE

I hereby certify that copies of the Brief of Appellants James G. Clay and Michael R. Corbett were served upon all parties to this appeal on July 14, 2009, as follows:

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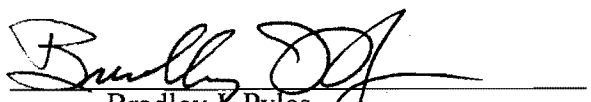

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