Honorable Mike K. Nakagawa
United States Bankruptcy Judge

Entered on Docket
May 09, 2025

UNITED STATES BANKRUPTCY COURT

DISTRICT OF NEVADA

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In re: EVELYN VALENCIA, Debtor.	Case No. 24-12313-mkn Chapter 7
L MAKEUP AGENCY AND INSTITUTE, LLC, Plaintiff, vs. EVELYN VALENCIA, Defendant.	Adv. Proc. No. 24-01070-mkn Date: April 2, 2025 Time: 9:30 a.m.

ORDER ON MOTION FOR DEFAULT JUDGMENT AND MOTION TO SET ASIDE THE ENTRY OF DEFAULT[1]

[1] In this Order, all references to "ECF" are to the documents filed in the above-captioned Chapter 7 proceeding. All references to "AECF No." are to the documents filed in the above-captioned adversary proceeding. All references to "Section" are to provisions of the Bankruptcy Code, 11 U.S.C. § 101, et seq. All references to "Bankruptcy Rule" are to the Federal Rules of Bankruptcy Procedure. All references to "Civil Rule" are to the Federal Rules of Civil Procedure. All references to "Local Rule" are to the Local Rules of Bankruptcy Practice for the District of Nevada.

On April 2, 2025, the court heard the plaintiff's Motion for Default Judgment and the defendant's Motion to Set Aside the Entry of Default in the above-captioned adversary proceeding ("Adversary Proceeding"). The appearances of counsel were noted on the record. After arguments were presented, the matters were taken under submission.

BACKGROUND[2]

On May 9, 2024, Evelyn Valencia ("Debtor") filed a voluntary Chapter 7 petition ("Petition") and was represented by law firm entitled Fair Fee Legal Services ("FFLS").[3] (ECF No. 1). The Petition attests that the Debtor lives at 956 Palmerston Street, Las Vegas, Nevada 89110 ("Residential Address"), but has a mailing address of 27 Rue De Degas, Henderson, Nevada 89074 ("Mailing Address"). The case was assigned for administration to Chapter 7 bankruptcy trustee Troy S. Fox. A notice of bankruptcy filing ("Bankruptcy Notice") was served by first class mail on all parties in interest. (ECF No. 5).[4]

On May 11, 2024, Debtor filed her schedules of assets and liabilities ("Schedules"), statement of financial affairs ("SOFA"), and other information required by Section 521(a). (ECF No. 8). On her unsecured creditor Schedule E/F, Debtor lists L Makeup Agency & Institute, LLC ("LMAI"), as having a claim in the amount of $19,836.94, described as a "Garnishment – 19CO36567."[5] Included in that information is a Disclosure of Compensation of Attorney for

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[2] Pursuant to Evidence Rule 201(b), the court takes judicial notice of the documents and information appearing on the docket maintained by the court clerk in the above-captioned case. See United States v. Wilson, 631 F.2d 118, 119 (9th Cir. 1980). See also In re Blas, 614 B.R. 334, 339 n.27 (Bankr. D. Alaska 2019) ("This court may take judicial notice of the docket of other courts.").

[3] The principal of FFLS appears to be attorney Seth D. Ballstaedt.

[4] The Bankruptcy Notice announced a meeting of creditors to be held on June 12, 2024, as well as a deadline of August 12, 2024, for creditors to object to the discharge of any debts.

[5] 19CO36567 apparently is the case number for a collection action by LMAI against the Debtor that was commenced in 2019 in the Las Vegas Justice Court ("Collection Action"). The same year, a co-borrower on the same loan named Estela Casas ("Casas") apparently filed a separate Chapter 7 proceeding denominated Case No. 19-16839-ABL. LMAI brought Adversary No. 20-01018-ABL against Casas seeking a determination that the same loan was nondischargeable under Section 523(a)(8). A default judgment was entered in that action against Casas on July 8, 2020. The default judgment contains no finding that repayment of the subject

Debtor(s) ("Compensation Disclosure") required under Section 329(a) and Bankruptcy Rule 2016(b). That document specifically discloses that FFLS does not represent the Debtor in, among other things, adversary proceedings. See Compensation Disclosure at ¶ 7.

On August 7, 2024, LMAI filed a complaint commencing the Adversary Proceeding against the Debtor ("Adversary Complaint"). (AECF No. 1). LMAI seeks a determination that its claim is based on an educational loan under Section 523(a)(8) that is not excepted from a bankruptcy discharge as an "undue hardship."[6] On August 8, 2024, a summons was issued requiring the Debtor to respond to the Adversary Complaint within 30 days ("Summons"). (AECF No. 4).

On August 13, 2024, an order of discharge was entered in the Chapter 7 proceeding ("Discharge Order"). (ECF No. 25).

On September 27, 2024, LMAI filed an affidavit of service ("COS") attesting that on August 8, 2024, the Adversary Complaint and Summons were served by first class mail to the Debtor at her Mailing Address as well as to her bankruptcy counsel, FFLS, at its mailing address.

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loan would constitute an undue hardship under Section 523(a)(8). In other words, Judge Landis made no factual finding on the undue hardship exception because it was never litigated. Casas did not oppose entry of a default judgment, nor did she seek to set aside her default. Meanwhile, in the Collection Action against the Debtor, a default judgment apparently was entered against the Debtor by the Las Vegas Justice Court on or about July 9, 2020.

[6] Section 523(a) lists 20 types of debts that are not dischargeable through Chapter 7. With respect to student loans, Section 523(a)(8) specifically provides that such debts are not discharged "unless excepting such debt from discharge…would impose an undue hardship on the debtor and the debtor's dependents, for—

> (A) (i) an educational benefit overpayment or loan made, insured or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution; or
> (ii) an obligation to repay funds received as an educational benefit, scholarship or stipend; or
> (B) any other educational loan that is a qualified education loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986, incurred by a debtor who is an individual."

11 U.S.C. § 523(a)(8) (emphasis added).

(AECF No. 5). On the same date, LMAI filed a Request for Entry of Default inasmuch as a response had not been received from the Debtor within 30 days of the issuance of the Summons. (AECF No. 6).

On October 15, 2024, counsel for LMAI filed an affidavit attesting that the Debtor had not responded to the Adversary Complaint and Summons, that FFLS had confirmed that it does not represent the Debtor in the Adversary Proceeding, and that the Debtor is authorized to be sued in the matter. (AECF No. 7).

On October 16, 2024, the Clerk of the Court entered an order of default ("Default Order") as permitted by Bankruptcy Rule 7055 and Local Rule 7055. (AECF No. 8).

On November 19, 2024, LMAI filed a motion for entry of default judgment ("Default Judgment Motion")[7] along with supporting declarations of its managing member, Kyle Waugh, and its bankruptcy counsel, Shlomo Sherman. (AECF Nos. 9, 10, and 11). On the same date, LMAI filed a notice that the Default Judgment Motion had been filed with the court, along with a certificate of service attesting that the Default Judgment Motion and supporting documents had been served on the Debtor at her Mailing Address. (AECF Nos. 12 and 13).

On December 5, 2024, LMAI filed a notice scheduling the Default Judgment Motion to be heard on January 8, 2025. (AECF No. 14).

At the January 8, 2025 hearing, Debtor appeared at the court in person and in pro se. Based ("Burke") on her representations to the court, the hearing was continued to February 12, 2025, to allow the Debtor to seek pro bono legal counsel.

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[7] LMAI maintains that it provided to Debtor's bankruptcy counsel "a judgment involving a different debtor under nearly identical circumstances in which the Court had recently confirmed that an identical loan by Plaintiff was a non-dischargeable student loan." See Default Judgment Motion at 5 n.3, referencing In re Luisiana Ortiz, Case No. 23-01127-nmc. Even a cursory review of the docket in that proceeding, however, reveals that the circumstances in the Ortiz proceeding were not close to being identical to the current matter. Instead, the Chapter 7 debtor in the Ortiz action was represented by experienced bankruptcy counsel and the matter was resolved on cross-motions for summary judgment. Judge Cox expressly concluded that the debtor had alleged but failed to establish a factual basis for her claim of undue hardship under Section 523(a)(8). In other words, there was no default judgment, and the court reached the merits of the claims based on the evidence presented by counsel.

On February 12, 2025, Debtor appeared through her pro bono counsel, Christopher Burke ("Burke"), and the hearing on the Default Judgment Motion was further continued to March 12, 2025, to allow counsel to respond.

On February 28, 2025, attorney Burke filed an opposition to the Default Judgment Motion that included a Motion to Set Aside the Default Order ("Set Aside Motion"). (AECF No. 21).[8] Counsel filed a separate notice for the latter to be heard on April 2, 2025. (AECF No. 22).

On March 12, 2025, the hearing on the Default Judgment Order was continued to April 2, 2025, so that it could be heard concurrently with the Set Aside Motion.

On March 19, 2025, LMAI filed a combined reply in support of its Default Judgment Motion as well as an opposition to the Set Aside Motion ("LMAI Combined Reply"), which was accompanied by another declaration of its counsel. (AECF Nos. 27 and 28).

On March 26, 2025, attorney Burke filed a reply in support of the Set Aside Motion ("Debtor Reply"). (AECF No. 29).[9]

On April 1, 2025, LMAI filed another declaration of its managing member in response to an issue raised in the Debtor's reply. (AECF No. 30).

DISCUSSION

The court has considered the written and oral arguments presented, as well as the declarations submitted by the parties. Based on those considerations, along with the record in this bankruptcy case, the court finds that cause exists to set aside the Default Order under Civil Rule 55(c). As a result, the Default Judgment Motion will be denied. Several reasons support this result.

First, there is no apparent disagreement that denial of relief under Civil Rule 55(c) requires the presence of at least one of three factors: (1) culpable conduct by the defendant that

[8] Attached in support of the Set Aside Motion is a copy of a declaration of Evelyn Valencia, signed under penalty of perjury on February 24, 2025. ("First Debtor Declaration").

[9] Attached to the Debtor Reply is a copy of another declaration of Evelyn Valencia, signed under penalty of perjury on March 26, 2025. ("Second Debtor Declaration").

led to entry of the default, (2) the absence of a meritorious defense to the plaintiff's claim, or (3) prejudice to the plaintiff. See LMAI Combined Reply at 8:23-9:7; Debtor Reply at 5:5-10,

Second, Debtor attests, *inter alia*, that she has no legal training, no understanding of the adversary proceeding process or the need to respond to LMAI's complaint, did not understand that attorney Ballstaedt would not be representing her in the matter, and did not understand the difference between a student loan and other loans. See First Debtor Declaration at ¶¶ 4, 5, 6, 7, 9, 10, 15, and 16. Debtor also attests, *inter alia*, that she has a G.E.D. rather than a high school diploma, that she does not have any post-high school education, that she is a single parent with one minor child, that she cannot afford to repay her student loans while meeting her living expenses, that she consulted attorney Ballstaedt and thought she could discharge her student loan debt, that she was not informed what an adversary proceeding is prior to filing for bankruptcy relief, and that she cannot otherwise afford to hire an attorney. See Second Debtor Declaration at ¶¶ 2, 3, 5, 6, 7, 9, 10, and 12.

Third, Debtor's testimony is unrefuted. The declarations submitted by LMAI offer copies of the underlying loan documents and account information, *inter alia,* but no evidence of the materials provided to the Debtor before entry of the Default Order and no evidence from Debtor's former counsel describing the information provided to the client.

Fourth, the Collection Action pursued by LMAI prior to commencement of the Chapter 7 proceeding resulted in a default judgment against the Debtor by the Las Vegas Justice Court, but without actual litigation of any facts underlying LMAI's claim. Because the facts were not actually litigated, any findings necessary for that judgment would not be entitled to issue preclusive effect under Nevada law. See In re Sandoval, 232 P.3d 422, 423 (Nev. 2010), citing Five Star Capital Corp. v. Ruby, 194 P.3d 709, 713-14 (Nev. 2008).

Fifth, the default judgment obtained on the same loan against the co-debtor in the Casas bankruptcy proceeding also would not have issue preclusive effect in the Debtor's proceeding under federal standards. See generally U.S. ex rel. Leckner v. General Dynamics Information Technology, 2022 WL 4280660, at *6 (S.D. Cal. Sep. 15, 2022).

Sixth, the court must consider the impact of the recent decision in In re Irigoyen, 659 B.R. 1 (B.A.P. 9th Cir. 2024). In that case, the Bankruptcy Appellate Panel for the Ninth Circuit ("BAP") distinguished between exceptions to nondischargeability under Section 523(a) that are self-executing and those that are not. Id. at 7.[10] The appellate court observed:

> If a debt clearly falls under one of the "self-executing" subsections of § 523(a), a creditor need not suffer the time and expense of litigation to enforce the debt post-discharge. However, if it be determined that a debt falls outside of one of the "self-executing" subsections of § 523(a), and is thus dischargeable, creditors will not be shielded from the reach of the discharge injunction and the bankruptcy court's power to impose contempt sanctions when appropriate. In those circumstances, bankruptcy courts may assess, as they would with any other discharged debts, whether creditors acted with a "fair ground of doubt" in their interpretations of the discharge injunction.

Id. (emphasis added). After discussing various case law, the BAP further observed:

> We think a more prudent interpretation is that §523(a)(8) is "self-executing" in the sense that neither party is required to file a lawsuit to determine the dischargeability of the debt. However, the lack of a determination does not change the nature of the debt. The debt is excepted from the general discharge order only if it is actually qualifies as the type of educational loan covered by § 523(a)(8). Otherwise, the debt is discharged with every other dischargeable debt. This interpretation harmonizes §§ 523, 524, and 727, such that only the specific debts enumerated by Congress are excepted from the general discharge.

Id. at 12 (emphasis added).[11] The BAP concluded that by attempting to collect a student loan debt before an undue hardship determination is made or even pursued by the debtor, the student lender risked being held in contempt for violating the discharge injunction. Id. at 14. To ameliorate that risk, the BAP also concluded:

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[10] That assumption that certain debts described in Section 523(a) are excepted from discharge without objection by the creditor flows from the language of Section 523(c). That provision specially requires a creditor to timely object to an individual debtor's discharge only of the debts described specifically under Sections 523(a)(2) [fraud], 523(a)(4) [fiduciary defalcation, larceny, embezzlement], and 523(a)(6) [willful and malicious injury]. Section 523(c) makes no mention of student loan debts under Section 523(a)(8).

[11] Sections 523(a)(8)(A) describes certain types of educational benefits while Section 523(a)(8)(B) describes "qualified education loans" as defined under the Internal Revenue Code. See note 6, supra.

> While it is true that the Senate Report reflects Congress's intent to relieve student loan lenders from the burden of filing a lawsuit, our interpretation does not conflict with that intent. If a debt is clearly within the § 523(a)(8) exception, lenders need not ever initiate a lawsuit; if there is a "fair ground of doubt" about whether the debt is excepted, lenders are protected from contempt sanctions by Taggart; and, in cases where the debt clearly falls outside of § 523(a)(8), lenders are appropriately subject to sanctions because Congress never intended to except those debts in the first place. In any event, a lender who wants a firm resolution may file a lawsuit and obtain a judgment at any time.

Id. at 13 (emphasis added).[12]

Finally, the court must determine the proper allocation of the burdens of proof in this proceeding. As LMAI voluntarily commenced this Adversary Proceeding, it has the burden of proving that the underlying loan is encompassed by Section 523(a)(8)(A) or Section 523(a)(8)(B). If it is not, then the Debtor's personal liability on the debt is encompassed by the Discharge Order and the Adversary Proceeding must be dismissed. If the underlying loan is encompassed by Section 523(a)(8)(A) or Section 523(a)(8)(B), the court must determine whether repayment of the underlying loan would be an undue hardship. This determination may be the equivalent of an affirmative defense for which Debtor apparently would have the burden of proof.[13]

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[12] Decisions of the BAP establish the law of the case for the particular appeal in which the controversy arises, but otherwise may not be binding on other bankruptcy courts. Because bankruptcy appellate panels were adopted in particular circuits to promote uniformity, however, BAP decisions generally are followed by bankruptcy courts within the particular circuit.

[13] Prior to Irigoyen, most student loan dischargeability actions were voluntarily commenced by a debtor who has the burden of proving the elements of undue hardship under prevailing legal standards. Except for objections under Sections 523(a)(2)(4) and (6), Bankruptcy Rule 4007(b) allows a complaint to determine dischargeability of debt to be commenced at any time. A debtor's ability to pay and effort to repay a student loan obligation can fluctuate over time, impacting when a debtor is in the best position to seek an undue hardship determination. When a student lender voluntarily commences a student loan dischargeability action under Section 523(a)(8), however, preemptive litigation may significantly affect the viability of the debtor's hardship defense at that time as well as in the future. In Irigoyen, the BAP did not address which party has the burden of proof on undue hardship when the claimant commences the action. At the hearing on the instant matters, counsel for LMAI and the Debtor appeared to agree that the Debtor should have the burden of proving the existence of undue hardship.

Based on the foregoing, the court concludes that the Debtor has not engaged in culpable conduct leading to the entry of default, has a possibly meritorious defense to the Complaint, and has not visited legal prejudice upon LMAI. As decisions on the merits of a dispute generally are favored, relief from the Default Order is appropriate under Civil Rule 55(c).

IT IS THEREFORE ORDERED that the Motion to Set Aside Default brought by Defendant Evelyn Valencia, Adversary Docket No. 9, be, and the same hereby is, **GRANTED.**

IT IS FURTHER ORDERED that the Motion for Default Judgment brought by Plaintiff L Makeup Agency and Institute, LLC, Adversary Docket No. 21, be, and the same hereby is, **DENIED**.

IT IS FURTHER ORDERED that an answer or other response to the Complaint shall be filed by Defendant **not later than May 30, 2025.**

IT IS FURTHER ORDERED that an initial scheduling conference in this adversary proceeding shall be held telephonically on **June 4, 2025, at 9:30 a.m.,** before U.S. Bankruptcy Judge Mike K. Nakagawa by telephonic appearance. Absent further order of the court, the parties must participate and appear telephonically by dialing (833) 435-1820; Meeting ID: 161-062-2560; Passcode: 029066#. Instructions for appearing via telephone are available on the court's website at: www.nvb.uscourts.gov/news-rss/announcements/2020/0319-court-hearing-participation/.

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