Consumer Track

Consumer Issues through the Eyes of the Trustee

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LIFE AFTER CONFIRMATION IN THESE BLEAK ECONOMIC TIMES

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Alejandro Oliveras Rivera

I- INTRODUCTION

Our hard times, as evidenced by high numbers of unemployment, divorce, aging population, migration, six-year recession, criminal activity, real estate declining values, and other varied factors, pose a serious challenge to those who strive to achieve a decent some degree of progress for themselves and their families here in Puerto Rico and elsewhere. "There is no dignity quite so impressive and no independence quite so important as living within your means." [1] But the times that we live in make this aspiration unachievable for thousands of our fellow citizens.

A tool used by a considerable number of individuals and companies to deal with the financial challenges they face is to file for bankruptcy, be it a liquidation process or reorganization.[2] In 2011, 1.35 million Americans entered Chapter 7 or 13.[3] As bankruptcy practitioners, the role we undertake is eponymous with the view held by a giant of the 20th Century: "As I see it, there are two great forces of human nature: self-interest and caring for others."[4] It is still undeniable that bankruptcy has a certain stigma to it.[5] Most probably

[1] President Calvin Coolidge quoted by Annise Parker Mayor of Houston in her first state of the city address (Apr. 2010). Time's May 10, 2010 Special Issue on The 100 Most Influential People in the World.
[2] 11 U.S.C. §101 et.seq. The bankruptcy code was amended significantly in 2005 by an act of congress titled the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) 119 Stat.23.
[3] Study by Columbia Law School professor Ronald Mann for the National Bankruptcy Research Center.
[4] Bill Gates Time Magazine August 11, 2009. More down to home, every attorney has a dilemma between his business and his profession. The dilemma is considered by the ABA's Model Rules of Professional Conduct (Preamble) [9] In the nature of law practice, however, conflicting responsibilities are encountered. Virtually all difficult ethical problems arise from conflict between a lawyer's responsibilities to clients, to the legal system and to the lawyer's own interest in remaining an ethical person while earning a satisfactory living. The Rules of Professional Conduct often prescribe terms for resolving such conflicts.
[5] "The dreaded word bankruptcy…had cut through the air like a bullet and landed like a mortar." Clay, pondering options when his tort kingdom was coming apart. John Grisham's, The King of Torts.

ecause, people hold a firm conviction in the moral obligation to pay their debts. "Honor is a harder matter than the law."[6]

And yet, even Jamie Dimon, CEO of J.P. Morgan Chase in his capitalist world allows room for the cases where that is not possible: "… "upholding the essential principle that individuals, businesses and corporations should repay their loans if they can afford to do so."[7]

In filing a bankruptcy, an individual seeks primarily, debt relief. Two features of the bankruptcy code that have great importance in this effort are the immediate stay of collection efforts[8] against debtors and the discharge.[9] In this paper we will take a look at the discharge, mostly from the perspective of Chapter 13 and what debtors can do to obtain it, when their confirmed plans are challenged by our bleak economic times.

II- THE DISCHARGE GENERALLY

"Ultimately, the principal goal of most bankruptcies is the discharge, which frees the debtor from personal liability on almost all debts. It is the clean slate that normally gives debtors the fresh start that bankruptcy is meant to provide."[10] A "…discharge is a privilege granted the honest debtor and is not a right accorded all bankrupts."[11] Sections 727, 1141, 1228 and 1328 are the bankruptcy code provisions that deal with the discharge. Within

[6] Mark Twain when facing financial difficulties and resolving to make enough money himself, writing and lecturing to pay back every cent. It is said that it was actually his wife, supported by Henry H. Rogers, an otherwise ruthless Standard Oil Executive who had volunteered to manage Twains money, who insisted he not take an easy way out. Time Magazine July 14, 2008.
[7] March 23, 2009, Annual Report, (Our underline).
[8] 11 U.S.C. §362.
[9] 11 U.S.C. §727; 1141; 1228 and; 1328.
[10] Consumer Bankruptcy Law and Practice. National Consumer Law Center, Ninth Ed., Vol. One Chapter 15, p. 451.
[11] In re Robinson 506 F2d. 1184, 1189 (2d Cir. 1974) as quoted in Bankruptcy Litigation Second Edition Sec. 14:1 p. 14-6 West.

sections 727, 1228 and 1328 we will find the phrase, "…the court shall grant the debtor a discharge..." and in section 1141(d)(1) we find language to the effect that the confirmation of a plan "…discharges the debtor from any debt…" and then we have a myriad of circumstances, which if present, will impede the concession of the discharge. In section 727, for example, we have 12 such circumstances. "Section 1328 cross-references the non dischargeability of certain debts in §523(a). Of particular importance in Chapter 13 practice are the exceptions for alimony, maintenance and support in §523(a)(5) and student loans in §523(a)(8). All of the §523(a) exceptions to discharge apply if the debtor seeks a discharge before completion of payments under the plan."[12]

III- PROBLEMS AND ALTERNATIVES

A- What happens to a Chapter 13 debtor with a confirmed plan if they lose their job? Can you get a hardship discharge upon being unemployed? Or underemployed?

Let us star t with the law. Paragraph (b) of section 1328 states:

Subject to subsection (d), at any time after the confirmation of the plan and after notice and a hearing, the court may grant a discharge to a debtor that has not completed payments under the plan only if—
(1) the debtor's failure to complete such payments is due to circumstances for which the debtor should not justly be held accountable;
(2) the value, as of the effective date of the plan, of property actually distributed under the plan on account of each allowed unsecured claim is not less than the amount that would have been paid on such claim if the estate of the debtor had been liquidated under chapter 7 of this title on such date; and
(3) modification of the plan under section 1329 of this title is not practicable.

[12] Keith. M. Lundin Chapter 13 Bankruptcy, 3d ed. §342-1 (2000 & Supp 2004). Internal footnotes omitted.

In re Marrero 7 B.R. 589 (Bankr. D.P.R. 1980) calls these three elements as standards for a hardship discharge. Generally speaking a debtor with a confirmed plan who later loses his employment or becomes underemployed might be able to obtain a hardship discharge. Debtor's advocate must put forth evidence on the three elements contained in the above quoted paragraph (b). Element number two (2) would appear to be pretty much a straightforward mathematical exercise, taking as the base of the computation the liquidation value of the estate that was previously established for confirmation purposes.

Elements number one (1) and three (3) is where he advocates earns the fee. A showing must be made that Debtor's unemployment was not of his or her own making. In the scenario of the underemployment, evidence must be brought forth to show that in spite of the Debtor's best efforts the job that pays less, was the only alternative readily available. Likewise Debtor should be prepared to answer a creditor, the Court's or a Trustee's question as to the prospects of obtaining a job of similar pay as the one had before in a relatively short period of time or not.

"Every Chapter 13 debtor experiences difficulties during the years of payments under the plan. If the "not justly…accountable" standard means anything, then bankruptcy courts must reserve hardship discharge for circumstances exceeding the normal or ordinary range of mishaps that befall Chapter 13 debtors. It has been said that justly accountable standard for hardship discharge in §1328(b) does not require proof of "catastrophic" circumstances, rather, the bankruptcy court must exercise "special vigilance".[13]

With respect to element number three (3), a debtor should be able to rule out other possible amendments to the confirmed plan, such as reduced payments and a proposal for a

[13] Keith. M. Lundin Chapter 13 Bankruptcy, 3d ed. §353-1 (2000 & Supp 2004) citing In re Bandilli, 23 B.R. 836, 839-41 (BAP 1st Cir. 1999).

lump sum, say for example to come from the proceeds of a grievance for unjust employment termination.

The ultimate evidentiary burden to establish entitlement to a hardship discharge under code § 1328(b)(1) rests upon the debtors. See In re Roberts, 279 F.3d 91, 94 (1st Cir. 2002); In re Rivera-Torres, 2007 U.S. Dist. LEXIS 12864 (D.P.R. Feb. 22, 2007).

B- Hardship discharge of student loans under §523(a)(8)

There are a number of debts excepted from a discharge granted under sections 727, 1141, 1228(a), 1228(b), or 1328(b). Among the debts listed as exempt are student loans, unless excepting such debt from discharge would impose an undue hardship on the debtor and the debtor's dependents, for:

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

an obligation to repay funds received as an educational benefit, scholarship, or stipend; or

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.

The key operating phrase is "undue hardship". In the words of Justice Thomas, "Sections 1328(a) and 523(a)(8) provide that student loan debt *is* dischargeable in a Chapter 13 proceeding if a court makes a finding of undue hardship."[14]

[14] UNITED STUDENT AID FUNDS, INC. *v.* ESPINOSA 130 S. Ct. 1367 March 23, 2010 Judge Thomas, footnote 10.

The Federal Rules of Bankruptcy Procedure require bankruptcy courts to make the undue hardship finding for the discharge of student loans thru an adversary proceeding, see Rule 7001(6). In the Espinosa case the Supreme Court ruled on a disagreement among the Courts of Appeals as to whether an order that confirms the discharge of a student loan debt in the absence of an undue hardship finding or an adversary proceeding, or both, is a void judgment for Rule 60(b)(4) purposes. It answered in the negative. " Where, as here, a party is notified of a plan's contents and fails to object to confirmation of the plan before the time for appeal expires, that party has been afforded a full and fair opportunity to litigate, and the party's failure to avail itself of that opportunity will not justify Rule 60(b)(4) relief."[15] The Court went on to review the issue of "… whether a bankruptcy court presented with a debtor's plan that proposes to discharge a student loan debt, in the absence of an adversary proceeding to determine undue hardship, should confirm the plan despite its failure to comply with the Code and Rules." It decided: "But, to comply with §523(a)(8)'s directive, the bankruptcy court must make an independent determination of undue hardship before a plan is confirmed, even if the creditor fails to object or appear in the adversary proceeding."

From the case of In re Bronsdon 435 B.R. 791 (2010) United States Bankruptcy Appellate Panel of the First Circuit in an Opinion written by Judge Lamoutte (Judge Tester was also on the Panel)

we gleam the following:

1. The creditor bears the initial burden of establishing that the debt is of the type excepted from discharge under § 523(a)(8). Once the showing is made, the burden shifts to the debtor to prove that excepting the student loan debt from discharge will cause the debtor and her dependents "undue hardship.

[15] Espinosa at p.14.

2. The debtor bears the ultimate burden of proving undue hardship by a preponderance of the evidence.

3. The Panel adopts the "totality of the circumstances" analysis which requires a debtor to prove by a preponderance of evidence that (1) his past, present, and reasonably reliable future financial resources; (2) his and his dependents' reasonably necessary living expenses; and (3) other relevant facts or circumstances unique to the case, prevent him from paying the student loans in question while still maintaining a minimal standard of living, even when aided by a discharge of other prepetition debts.

4. The party opposing the discharge of a student loan has the burden of presenting evidence of any disqualifying factor, such as bad faith.

5. Undue hardship is measured as of trial date and is a forward-looking concept. The finding of undue hardship following the totality of the circumstances test rests on one basic question: "Can the debtor now, and in the foreseeable near future, maintain a reasonable, minimal standard of living for the debtor and the debtor's dependents and still afford to make payments on the debtor's student loans?"

For a case from this District where you can find an example of an opposition by the Chapter 13 Trustee to debtors' request for a hardship discharge and debtors' reply (loss of income in about 25%), see In re Cardwood, 05-12157 , docket numbers 73 and 75.

C- <u>Mortgage loan modification; what is the effect of a mortgage loan modification on a confirmed chapter 13 plan?</u>

We are all aware of the fact that federal and state Governments have crafted several programs to aid in the problem of individuals losing their homes to foreclosure. One such program, sponsored by the federal Government, is known as the Home Affordable Modification Program (HAMP). The banking institutions, in varying degrees, have adopted what is commonly known as Loss Mitigation Programs. These programs may include residential mortgage modifications.

The U.S. Treasury Department issued Supplemental Directive 10-02 on March 24, 2010 to disclose significant changes to the program of which we highlight two: 1) prohibition against referral to foreclosure until either: (i) a borrower has been evaluated and determined to be ineligible for HAMP; or (ii) reasonable solicitation efforts have failed and; 2) a requirement that servicers must consider borrowers in active bankruptcy for HAMP if a request is received from the borrower, borrower's counsel or bankruptcy trustee.

Consequently we may see a Chapter 13 petition where the Debtor has an ongoing loan modification application and incorporates language into the plan to that effect. Likewise, we may have confirmed plans where afterwards, the Debtor seeks to modify the loan. If the plan provided for the payment of pre-petition arrears the subsequent loan modification may take care of those arrears. Consequently a modified plan would be in order. Typically, the modification will entail a reduction in the total funding of the plan. The modification of the loan does not necessarily mean that debtor has additional projected disposable income.

Motions are filed to allow modification or loss mitigation dialogue, to either commence or continue between debtor and a banking institution. We have expressed the following view:

"We ask that you please include in the motion to be filed with the court, an averment (and that it be part of the prayer) as to what is to be done with the payments that I, as Trustee, would otherwise send to the secured lender. Two instances where this averment can be made: a) in the motion seeking authority to initiate or continue modification talks with the lender and b) in the motion asking for approval of an agreement already reached with the lender. I ask that you inform whether you want the Trustee to hold the payment in reserve, simply not make any further payments to the lender or that we continue with such payments.

Another item to consider when the loan modification is approved is the filing of a modified plan to deal with the elimination of the pre-petition arrearage to the secured lender. The modified plan, however, should disclose the amount paid by Trustee prior the modification request. If a

prior motion, as described in the first paragraph, has not dealt with the situation, I shall continue making payments to the secured lender, based on the confirmed plan.

Some of you might consider saving time and expense of filing a modified plan post modification by dealing with it in the motion above referred.

I share, a text for your consideration:

Motion to Allow Debtor to Pursue Mortgage Loan Modification With Plan Amendment

Since the mortgage loan modification contemplated by Debtor will manage the pre-petition arrears, and any post-petition arrears now existing or that may accrue while this modification is achieved, the Debtor asks that the Trustee not make [RESERVE OR CONTINUE) payments under the plan to the secured lender [PROVIDE NAME]. In the event the mortgage loan is modified, the order approving the same will have the effect of realizing a modification of the confirmed plan, without the need of further notice or hearing, by superseding the provision relative to payment of arrears to secured lender [PROVIDE NAME]. If the modification is not approved by lender, Debtor will inform the Court." [16]

Lastly, caution must be exercised by debtor(s) when evaluating loss mitigation alternatives, in particular mortgage modifications, so that either in the mid or long-term, they do not end worse off than what they are presently. Anecdotal evidence tells us that loss mitigation programs, locally and nationally, have not had the positive impact in stemming the foreclosure wave as was hoped for.

D- The deceased discharge

No, you will not find this one in the code. The proposition is interesting. It can happen in either a joint or single petition scenario. Debtor (or a joint debtor) dies yet, the particulars of the case allow for the ability to continue with the administration of the case.

The Bankruptcy Rules provide that bankruptcy estate administration may continue despite the death of the debtor, but neither the applicable rule nor the Advisory Committee

[16] Message sent to the Bankruptcy Bar on October 17, 2011.

Notes state whether "administration" includes the granting of a discharge to the debtor. *See* Fed.R.Bankr.P. 1016. However, the case law, as well as *Collier* and the legislative history to the Code, all support the conclusion that even a dead debtor can get a discharge. *See In re Perkins,* 2007 WL 4191950 (Bankr.S.D.Ill. Nov. 21, 2007); *In re Cummins,* 266 B.R. 852 (Bankr.N.D.Iowa 2001); *In re Doyle,* 209 B.R. 897, 906-07 (Bankr.S.D.Ill.1997); *see also* H.R. Rep. NO. 595, 95th Cong, 1st Sess 367-68 (1978); *see generally* 1 R. Ginsberg & R. Martin, *Ginsberg & Martin on Bankruptcy,* § 5.03[B] at 5-26 (4th ed.1995); 9 L. King, *Collier on Bankruptcy,* ¶ 1016.04 (15th ed. rev.2006).

Hijacked or *Ransom*ed: Trustees Cope with a Confusing Supreme Court Decision

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Most consumer bankruptcy practitioners are already aware of the holding of the Supreme Court in *Ransom v. FIA Card Services NA*,[1] and its impact on the way they calculate chapter 13 plans. Justice Elena Kagan, writing for an eight-member majority, held that an above-median-income chapter 13 debtor was not entitled to take the ownership allowance for an automobile as specified in the Internal Revenue Service's (IRS) Local Standards unless the debtor actually had a car payment. The IRS created these allowances (the "Collection Financial Standards") as a means of analyzing whether it should accept an offer in compromise from a taxpayer. The standards' sole function is to assist in the collection of delinquent taxes.

Henry E. Hildebrand

The facts of the case are straightforward. When the debtor filed his chapter 13 petition, he owned a 2004 Toyota Camry outright, free of any debt; he had no car payment. For purposes of calculating his projected disposable income, the debtor claimed a "car ownership deduction" of $471 for the Camry, the amount specified in the IRS' ownership cost table of local Collection Financial Standards.[2] Based on this calculation, he proposed a five-year plan that would pay approximately 25 percent of his unsecured debt. An objection by a credit card claimholder asserted that Ransom was not entitled to take the ownership allowance in the standards because *Ransom* did not make a loan or lease payment for the car. The *Internal Revenue Manual* guides the IRS in applying the standards: "If a taxpayer has a car but no car payment, only the operating costs portion of the transportation standard is used to figure the allowable transportation expense."[3] Without this allowance, his disposable income over 60 months of the plan would increase by approximately $28,000.

The decision gives clear instruction to debtors and trustees: If a debtor does not have a car payment, the debtor cannot deduct the amount of the allowance. However, a Supreme Court decision is not important so much for the actual holding in the debtor's case. It provides the direction to practitioners, including trustees, for cases to come. Trustees, authorized to enforce the disposable-income test of 11 U.S.C. § 1325(b), will carefully parse through the language of the decision to determine what instruction or direction the Court is giving to the practitioners for application applying the disposable-income test in the future.

Trustee Talk I

After careful examination, chapter 13 trustees have every right to be concerned over the lack of clarity in the opinion.

Traditionally, in nearly every recent Supreme Court decision, the Court has recognized a fundamental bankruptcy concept—that a debtor is entitled to a "fresh start."[4] Judicial examination of the Bankruptcy Code has always been through the prism of a debtor's fresh start. Nowhere in Justice Kagan's opinion is the concept of a "fresh start" even mentioned. The long-held view of bankruptcy—balancing the equitable distribution of property among the debtor's creditors and the discharge that gives a debtor a fresh start—appears to have been abandoned. The view has apparently been replaced with Justice Kagan's reference to the legislative history of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA): "Congress designed the means test to measure debtors' disposable income and, in that way, 'to ensure that [they] repay creditors the maximum they can afford.'" Viewed through this position, it is clear that the Supreme Court is directing bankruptcy constituents to interpret the Bankruptcy Code in such a way as to compel debtors to repay their creditors the maximum that they can afford.

Starting with this view, it is no surprise that the debtor, who had no payment on a car, should not be allowed to shelter $28,000 of future income from his creditors. This type of "imaginary" expense runs directly counter to the reality that the debtor could afford to pay more back to his creditors.

With this in mind, a trustee is left with several major questions. If an above-median-income chapter 13 debtor has a car note payment of *less* than the IRS' allowance, is the expense deduction permitted under § 707(b) limited to the debtor's actual expense, or is the debtor entitled to the full allowance (now about $30,000 over 60 months)? The Supreme Court specifically ducked this issue.[5] Justice Kagan invites litigation on this issue, noting that a debtor's out-of-pocket costs "may well not control the amount of the deduction. If a debtor's actual expenses exceed the amounts listed on the tables, for example, the debtor may claim an allowance only for the specified sum, rather than for his real expenditures."[6] Since the Court has directed us to consult the Internal Revenue Manual, and since the Code should be interpreted to "ensure that [debtors] repay creditors the maximum they can afford," it is not a stretch to see courts denying a deduction for an ownership allowance that exceeds the amount the debtor is actually paying.

If a trustee is directed to apply the disposable-income test with an eye on the IRS' own interpretation of the Collection Financial Standards, many trustees will

1 131 S.Ct. 716 (2011).
2 This amount has since increased to $496 per month.
3 *Internal Revenue Manual* § 5.15.1.9(1)(B).
4 *Schwab v. Reilly*, 130 S.Ct. 2652, 2667 (2010); *Marrama v. Citizens Bank of Massachusetts*, 549 U.S. 365, 367, 127 S.Ct. 1105 (2007); *Central Virginia Community College v. Katz*, 546 U.S. 356, 126 S.Ct. 990, 996 (2006); *Rousey v. Jacoway*, 544 U.S. 320, 125 S.Ct. 1561 (2005); *Tennessee Student Assistance Corp. v. Hood*, 541 U.S. 440, 124 S.Ct. 1905, 1906 (2004); *FCC v. NextWave Personal Communications Inc.*, 537 U.S. 293, 123 S.Ct. 832, 840 (2003); *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 114 S.Ct. 1757, 1774 (1994); *Dewsnup v. Timm*, 502 U.S. 410, 112 S.Ct. 773, 777 (1992).
5 "FIA, relying on the IRS' practice, contends...that a debtor may claim only his actual expenditures in this circumstance...we decline to resolve this issue. Because [the debtor] incurs no ownership expenses at all, the car-ownership allowance is not applicable to him in the first instance." 131 S.Ct. at 727, n.8.
6 *Id.* at 727.

seek to "cap" the applicable ownership allowance to the amount that the debtor actually must pay. Thus, for a debtor who has 10 months of automobile payments remaining on their car at $250 per month, the maximum allowance would be $2,500, rather than $30,000 as permitted by 60 months of the local standard.

To be fair, Justice Kagan mentioned that the Court *did not* incorporate the IRS guidelines into the statute. In so doing, she did direct bankruptcy courts to "consult this material in interpreting the National and Local Standards; after all, the IRS uses those tables for a similar purpose—to determine how much money a delinquent taxpayer can afford to pay the Government." As Justice Antonin Scalia noted in his dissent, it is somewhat incongruous for Justice Kagan's decision to hold that the statute does *not* incorporate the IRS' guidelines but directs courts to consult the *Internal Revenue Manual* in interpreting the national and local standards. As Justice Scalia noted, "in the present context, the real-world difference between finding the guidelines incorporated and finding it appropriate to consult them escapes me, since I can imagine no basis for consulting them unless Congress meant them to be consulted, which would mean they are incorporated."[7]

Also confusing is Justice Kagan's reference to a remedy for the situation of a debtor whose automobile payments "cease during the life of the plan." The hypothetical raised by the Court is one where the debtor files a chapter 13 petition with only one payment remaining on a car. Justice Kagan apparently assumes that a car note that ends before the plan completes somehow increases funds from that point on. If a debtor is entitled to a full allowance when the plan is confirmed, and the chapter 13 plan proposes to treat the auto loan pursuant to § 1325(a)(5)(B), what change of financial circumstances exist? If a debtor enters chapter 13 with a Mercedes Benz, paying $600 per month for the vehicle, but there is only one payment remaining on the Mercedes, there is absolutely no change in the debtor's financial circumstances from confirmation to the end of the plan. The plan that pays this secured claim—$600—over five years would present no change.

In the overwhelming majority of cases, § 1325(b) issues are not raised by creditors—they are raised by the trustee... It seems we have gone full circle: from discretion of the court, to a fixed allowance, to the discretion of the trustee. Most trustees will welcome that responsibility.

Since chapter 13 trustees are expected to be the wielders of the § 1329 modification tool, Justice Kagan and the majority have not clarified when such a modification would be appropriate. It does appear that the Court agrees with the Seventh Circuit decision in the matter of *In re Witkowski*[8] by holding that to pursue a plan modification, there does not have to be an unforeseen change in the debtor's circumstances.

In the hypothetical cited by Justice Kagan, there is no change presented subsequent to the confirmation of a plan where the original contract would see an end to the automobile installment payments. Again, the only fair way of reading the opinion is that the contractual auto payments, divided by 60, cap the standards ownership allowance.

The Supreme Court rejected all of the legal and practical arguments of the debtor in the *Ransom* case. The argument that Congress intended to provide a "sinking fund" with which a debtor could purchase an automobile during the pendency of a case was not accepted.

BAPCPA has often been referred to as legislation designed to remove the discretion of bankruptcy judges in dealing with issues of a debtor's disposable income and how much chapter 13 debtors must repay to creditors. What *Ransom* has done is replaced the discretion of the Court with the discretion of the trustee. After all, § 1325(b) is only applicable if there is an objection raised by an unsecured creditor (as was the case in *Ransom*) or by the chapter 13 trustee. In the overwhelming majority of cases, § 1325(b) issues are not raised by creditors—they are raised by the trustee. If the trustee has the discretion to exercise a view of what is appropriate for a debtor to expend, that trustee may elect to forego objecting to a debtor's proposed plan or to raise an objection to allowances. It seems we have gone full circle: from discretion of the court, to a fixed allowance, to the discretion of the trustee. Most trustees will welcome that responsibility. ■

7 *Id.* at 732, n* (Scalia, J., dissenting).

8 16 F.3d 739 (7th Cir 1994).

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Can The Applicable Commitment Period Be Reduced Through A Post Confirmation Plan Modification?

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[ABI Caribbean Insolvency Symposium
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I. Introduction:

If a Chapter 13 plan is proposed and never objected, § 1325(b) would not apply and the plan may be confirmed if all the requirements of §§ 1322 and 1325(a) are met. In that case the plan commitment period would be the one proposed and approved by the court. The terms of the plan would bind the debtor and each creditor [11 U.S.C. § 1327(a)] and could only be modified under the conditions established by §§ 1328(b) or 1329.

Pursuant to 11 U.S.C. § 1325(b)(1) if the Chapter 13 trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, it's confirmation would require that the debtor either provide for the payment in full all allowed unsecured claims or he must provide for the application of all his "projected disposable income" to be received within the "applicable commitment period" to make payments to unsecured allowed claims. Subsection (b)(4) provides that the plan "applicable commitment period" should be 36 months if the current monthly income of the debtor and the debtor's spouse combined, when multiplied by 12, is less than the median income of a family of the same size. If the current monthly income of the debtor and the debtor's spouse combined, when multiplied by 12, is more than the median income of a family of the same size, the "applicable commitment period" should be 60 months.

Bankruptcy Code amendments of 1984 added subsection 1325(b) codifying the case law "best efforts" test which required the debtor to use his "projected disposable income" to make payments for the period of "three years". Code amendments of 2005 substituted the minimum period of "three years" in § 1325(b)(1)(B) with a period equal to the "applicable commitment" defined in subsection (b)(4). Contrary to some interpretations, when § 1325(b) applies, the applicable commitment period is a "minimum" plan period if all allowed unsecured claims are not paid in full earlier. The plan "maximum" period is determined by § 1322(d)(2)(C) and § 1329(c).

> Section 1325(b)(1) is not a formula for determining how much a below median debtor must pay under a chapter 13 plan. Rather, the section serves to set the minimum term of a chapter 13 plan. If a chapter 13 plan does not propose to pay unsecured creditors in full, it must have a term of at least the applicable commitment period. For above median income debtors, that period is five years. 11 U.S.C. § 1325(b)(4)(A)(ii). For below median debtors, that period is three years. 11 U.S.C. § 1325(b)(4)(A)(i). While § 1325(b)(1) does set the minimum term for chapter 13 plans that do not propose to pay unsecured creditors in full, it does not set the maximum term of a chapter 13 plan. Instead, the maximum term for a chapter 13 plan is determined under § 1322(d). For an above median debtor, the maximum term is five years, which is also the applicable commitment period. 11 U.S.C. § 1322(d)(1). For a below median debtor, the maximum term is three years, unless the Court,

> for [**6] cause, approves a longer period with the term of the plan not to exceed five years. 11 U.S.C. § 1322(d)(2).
>
> ***In re Roudger***, 2010 BNH 5 (Bankr. D.N.H. 2010) [Emphasis added.]

Courts disagree on whether the "applicable commitment period" is even relevant when the "disposable income" determined according to subsection (b)(2) is zero or when it is more than zero but its estimated projection could be pay before the end of the commitment period. There is the "monetary" view which sustain that the applicable commitment period is a multiplier that determines a fixed amount that the debtor must pay, regardless of when it is paid. According to this view an above median debtor with a monthly disposable income of $100, computed pursuant to subsection (b)(2), could "buy" his discharge by paying $6,000 the day after the plan is confirmed. The majority view is the "temporal" view[1], which sustain that the "applicable commitment period" determines the time over which the debtor must make payments under a plan. Under this interpretation, the debtor must make payments for the number of months in the applicable commitment period, and the plan cannot end prior to that time.

> " The temporal view is also supported by the Supreme Court of the United States' decision in *Hamilton v. Lanning*. In *Lanning,* the Court rejected a "mechanical" approach to calculating the projected disposable income component of the 11 U.S.C. § 1325 calculation, instead adopting a "forward-looking" approach whereby the court may account for changes in the debtor's income or expenses that are "known or virtually certain" at the time of confirmation."
>
> ***In re Filion***, 452 B.R. 329, 333 (Bankr. D. Mass. 2011)

Notwithstanding the binding effect of the confirmation, if during the applicable commitment period the debtor's financial condition deteriorates to the point that affects his ability to comply with the stipulated payments under a confirmed plan, the Code provides limited exceptions to the finality of the confirmation order. Depending on the nature of debtor's financial situation he may be allow to modify the confirmed plan, limited by what section 1329 provides. *([P]arties requesting modifications of Chapter 13 plans must advance a legitimate reason for doing so, and they must strictly conform to the three limited circumstances set forth in § 1329*.) ***Barbosa v. Solomon***, 235 F.3d 31, 41 (1st Cir. 2000)

If a plan modification is not practicable, then the debtor may be entitled to a hardship discharge under section 1328(b).

To determine if the debtor can reduce the "applicable commitment" period after confirmation we must start on the language of sections 1329 and 1328(b). These sections are interdependent as they are the alternated remedies provided by the Code for the

[1] *Baud v. Carroll,* 634 F.3d 327, 338 (6th Cir.2011); *Whaley v. Tennyson (In re Tennyson),* 611 F.3d 873 (11th Cir.2010); *Coop v. Frederickson (In re Frederickson),* 545 F.3d 652 (8th Cir.2008); *Timothy v. Anderson (In re Timothy),* 442 B.R. 28 (10th Cir. BAP 2010); *In re Filion*, 452 B.R. 329, 332 (Bankr. D. Mass. 2011); *In re Fridley,* 380 B.R. at 538; *In re King,* No. 10–18139, 2010 WL 4363173 (Bankr.D.Colo. Oct.27, 2010); *Baxter v. Turner (In re Turner),* 425 B.R. 918, 920–21 (Bankr.S.D.Ga.2010); *In re Moose,* 419 B.R. 632, 635–36 (Bankr.E.D.Va.2009); *In re Meadows,* 410 B.R. 242, 245–47 (Bankr.N.D.Tex.2009); *In re Brown,* 396 B.R. 551, 554–55 (Bankr.D.Colo.2008); *In re Nance,* 371 B.R. 358 (Bankr.S.D.Ill.2007).

honest debtor to reach the goal of a fresh start when he cannot comply with his confirmed plan payments.

II. Cannon of Statutory Interpretation

Settled principles of statutory construction require that we must first determine whether the statutory text is plain and unambiguous. The starting point for all statutory interpretation is the language of the statute itself. We must assume that Congress used the words in a statute as they are commonly and ordinarily understood, and we read the statute to give full effect to each of its provisions. We do not look at one word or term in isolation, but instead we look to the entire statutory context. We will only look beyond the plain language of a statute at extrinsic materials to determine the congressional intent if: (1) the statute's language is ambiguous; (2) applying it according to its plain meaning would lead to an absurd result; or (3) there is clear evidence of contrary legislative intent. If the statutory text is plain and unambiguous, then the statute must be applied according to its terms. [***Lamie v. U.S. Trustee***, 540 U.S. 526, 534, 124 S. Ct. 1023, 1030, 157 L. Ed. 2d 1024 (2004); ***United States v. Gonzales,*** 520 U.S. 1, 4, 117 S.Ct. 1032, 137 L.Ed.2d 132 (1997); ***Carcieri v. Salazar***, 555 U.S. 379, 387, 129 S. Ct. 1058, 1063-64, 172 L. Ed. 2d 791 (2009).]

III. Section 1328(b) allows the debtor to reduce the "applicable commitment period"

Pursuant to Section 1328(b), if a debtor is unable to continue with the scheduled confirmed plan payments, a modification of the plan is not practicable, allowed unsecured creditors have received distribution equal or greater than what they would had received in a Chapter 7 liquidation case, and the reasons why he cannot complete the plan payments is due to circumstances for which the debtor should not justly be held accountable, the debtor would be entitled to a hardship discharge. Accordingly the plain language of section 1328(b) would allow a debtor to modify the applicable commitment period to end on the date of the request for hardship discharge under section 1328(b).

Through Section 1328(b) the Bankruptcy Code provides a limited discharge to a debtor who's financial condition, does not allow the proposal of a practicable modified plan under § 1329. A debtor attempt to obtain a full discharge through a § 1329 modification of the confirmed plan proposing to make no prospectively modified payments and to declare the "plan complete" is not proposed in good faith.

> A modification to reduce payments to creditors can be an effort by the debtor to declare the plan completed. One reported decision allowed a debtor to modify a 70 percent plan to become a 25 percent plan when, after five years of effort, payments had been sufficient to retire only 25 percent of the unsecured claims. [See, *In re Eves,* 67 B.R. 964 (Bankr. N.D. Ohio 1986)] Several other reported decisions refuse motions to modify near the end of the original repayment period, when the effect is to declare the plan completed by reducing payments to whatever the debtor has been able to pay. [*See, e.g., In re Debing,* 202 B.R. 291 (Bankr. D. Minn. 1996); *In re Richardson,* 192 B.R. 224, 226 (Bankr. S.D. Cal. 1996); *In re Guernsey,* 189 B.R. 477 (Bankr. D. Minn. 1995)] In *In re Vasquez,* [261

B.R. 654 (Bankr. N.D. Tex. 2001)] the court found a lack of good faith when the debtors sought to modify the plan in the 46th month to reduce payments to unsecured creditors and declare the plan completed based on an injury that reduced the debtors' earning capacity. The court found that the modification probably fit within § 1329(a)(1), but "[b]y seeking a modification rather than a hardship discharge, the Debtors are . . . manipulating the provisions of the Code and thus the court must question the Debtors' motivation and sincerity in proposing the modification." [Id. 261 B.R. at 659]

Keith M. Lundin & William H. Brown, **CHAPTER 13 BANKRUPTCY, 4TH EDITION**, § 265.1, at ¶ 10, Sec. Rev. June 9, 2004, www.Ch13online.com. [Emphasis added.]

IV. **What can be modify under Section 1329?**

Section 1329 provides:

(a) At any time after confirmation of the plan but **before the completion of payments** under such plan, the plan may be modified, upon request of the debtor, the trustee, or the holder of an allowed unsecured claim, to--

(1) increase or reduce the amount of payments on claims of a particular class provided for by the plan;
(2) extend or reduce the time for such payments;
(3) alter the amount of the distribution to a creditor whose claim is provided for by the plan to the extent necessary to take account of any payment of such claim other than under the plan; or
(4) reduce amounts to be paid under the plan by the actual amount expended by the debtor to purchase health insurance for the debtor (and for any dependent of the debtor if such dependent does not otherwise have health insurance coverage) if the debtor documents the cost of such insurance and demonstrates that--
(A) such expenses are reasonable and necessary;
(B)(i) if the debtor previously paid for health insurance, the amount is not materially larger than the cost the debtor previously paid or the cost necessary to maintain the lapsed policy; or
(ii) if the debtor did not have health insurance, the amount is not materially larger than the reasonable cost that would be incurred by a debtor who purchases health insurance, who has similar income, expenses, age, and health status, and who lives in the same geographical location with the same number of dependents who do not otherwise have health insurance coverage; and
(C) the amount is not otherwise allowed for purposes of determining disposable income under section 1325(b) of this title; and upon request of any party in interest, files proof that a health insurance policy was purchased.

(b)(1) Sections 1322(a), 1322(b), and 1323(c) of this title and the requirements of section 1325(a) of this title apply to any modification under subsection (a) of this section.
(2) The plan as modified becomes the plan unless, after notice and a hearing, such modification is disapproved.
(c) A plan modified under this section may not provide for payments over a period that expires after the **applicable commitment period** under section 1325(b)(1)(B) after the time that the first payment under the original confirmed plan was due, unless the court, for cause, approves a longer period, but the court may not approve a period that expires after five years after such time.

11 U.S.C.A. § 1329 (West) [Emphasis added.]

The term "applicable commitment period" is mentioned only once in subsection "(c)" of section 1329 to limit debtor's ability to propose a plan with a term beyond the applicable commitment period provided in section 1325(b)(1)(B), unless cause exist, but never beyond five years. Since the "applicable commitment period" for above income debtors is 60 months, this subsection would be inapplicable to above median debtors. Under median debtors would be able to propose payments beyond their 36 months "applicable commitment period" if cause is shown.

According to this section a debtor, before the completion of his confirmed plan payments, can request and the court may approve a modification of the plan. Courts have place substantial weight on the interpretation of § 1329(b)(1). This section provides that sections 1322(a), 1322(b), and 1323(c) of the Code and the requirements of section 1325(a) would apply to any modification under its subsection (a).

V. **Applicability of the subsection (b) of Section 1325 in the context of a request of modification under Section 1329**.

The applicability of the subsection (b) of section 1325 in the context of a modification under section 1329 has been the subject of conflicting case law. The vast majority of courts deciding the issue have held that post-confirmation modifications are not governed by 11 U.S.C. § 1325(b), particularly because by specifying only four provisions [1322(a), 1322(b), 1323(c) and 1325(a)] § 1329(b) implicitly excludes other provisions, under the maxim *expressio unius est exclusio alterius.* [*In re Davis*, 439 B.R. 863, 867 (Bankr. N.D. Ill. 2010)] Hence no "best effort" test is necessary, projected disposable income within an "applicable commitment period" is not an issue, is not applicable. The approval of a modified plan would be like the confirmation of an original plan without any objections, only §§ 1322(a)-(b), 1323(c) and 1325(a) would apply. This interpretation of § 1329 would also render meaningless the minimum applicable commitment period required by § 1325(b) upon an objection, depriving creditors of the opportunity to receive the maximum possible repayment under a plan. Only the good faith requirement of § 1325(a)(3) would deter every debtor to reduce the "applicable commitment period" the day after obtaining the confirmation of his first plan. *In re Grutsch*, 453 B.R. 420 (Bankr. D. Kan. 2011)

> S*ee, e.g., In re Hall,* 442 B.R. 754, 761 (Bankr.D.Idaho 2010) (holding because § 1329 does not include any reference to § 1325(b), even though § 1329 includes specific reference to several other Code sections, the requirements of § 1325(b) should not be applicable to § 1329 modifications, and further noting that "§ 1329 was not amended to include the provisions of § 1325(b) when the 'disposable income' test was significantly amended by Congress in 1984. *See* Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98–353, 98 Stat. 333. When the Bankruptcy Code was significantly amended in 2005, and though there was a considerable existing division in the case law on this issue, § 1329, while amended in other ways, was not changed by Congress to include any reference to § 1325(b));" *In re Davis,* supra. (Bankr.N.D.Ill.2010); *In re Walker,* 2010 WL 4259274, *9–10 (Bankr.C.D.Ill.2010); *In re White,* 411 B.R. 268, 272–73 (Bankr.W.D.N.C.2008); *In re McCully,* 398 B.R. 590, 593 (Bankr.N.D.Ohio 2008); *In re Hill,* 386 B.R. 670 (Bankr.S.D.Ohio, 2008); *In re Wetzel,* 381 B.R. 247, 251–52 (Bankr.E.D.Wis.2008) (holding that "[b]ecause the current definition of projected disposable income results in a calculation that is, in large part, fixed by pre-petition

> circumstances, reviewing that calculation at the time of a post-confirmation modification may not be particularly meaningful. Because of its statutory definition, 'current monthly income' once correctly calculated should not change over time. Thus, attempting to apply § 1325(b) to a § 1329 modification is not favored by post-BAPCPA cases"); *In re Ewers,* 366 B.R. 139, 141 and 142 (Bankr.D.Nev.2007) (noting that if the trustee's position were correct, then § 1329(a)(2) would be rendered meaningless for above median income debtors, as they would be prohibited from doing either of the options noted—reducing or extending their plan length); *In re Ireland,* 366 B.R. 27, 34 (Bankr.W.D.Ark.2007); *In re McCollum,* 363 B.R. 789, 798 (E.D.La.2007); *In re Howell,* 2007 WL 4124476 (Bankr.W.D.La.2007); *In re Sunahara,* 326 B.R. 768 (9th Cir.BAP2005); and *In re Golek,* 308 B.R. 332, 336–37 (Bankr.N.D.Ill.2004).

The minority decisions holds that the list of applicable provisions in § 1325(b)(1) is not exclusive. The first argument is that because § 1329(b)(1) expressly makes applicable to plan modification "the requirements of section 1325(a)," and because § 1325(a) itself states that it applies "[e]xcept as provided in subsection(b)," § 1325(b) must be one of the "requirements" of § 1325(a). *In re King*, 439 B.R. 129, 134 (Bankr.S.D.Ill.2010). *See*; also *In re Heyward,* 386 B.R. 919, 924–26 (Bankr.S.D.Ga.2008); *In re Slusher,* 359 B.R. 290, 301 (Bankr.D.Nev.2007); *In re Baxter,* 374 B.R. 292, 296 (Bankr.M.D.Ala.2007). In re Buck, 443 B.R. 463 (Bankr. N.D. Ga. 2010); *In re Stretcher*, BR 07-51221, 2011 WL 6210525 (Bankr. W.D. Tex. Dec. 14, 2011); *In re Heideker*, 455 B.R. 263 (Bankr. M.D. Fla. 2011) (held that requirement that debtors must either pay their unsecured creditors in full or propose plans that extend for entire term of their applicable commitment periods, was equally applicable to modified plans, and prevented debtors from modifying plan post confirmation to reduce payment term without providing a 100% distribution on unsecured claims]. If under applicable § 1325(a)(1) an objection by the trustee or an unsecured creditor triggers the application of subsection (b), then under § 1329(b)(1), section 1325(b) would apply upon an objection to a proposed plan modification.

> "The heart of [BAPCPA's] consumer bankruptcy reforms ... is intended to ensure that debtors repay creditors the maximum they can afford." As the Tennyson[2] court explained, that intent "would be contravened by permitting confirmation of a bankruptcy plan for less than five years when unsecured claims have not been paid in full." For that reason, the Tennyson court held that an above-median income debtor "must submit to Chapter 13 bankruptcy for a minimum of five years." As the court in In re King [439 B.R. 129] recognized, "[t]here would be little point in requiring an above-median income debtor to propose a five-year plan for purposes of confirmation if that same debtor could simply turn around and modify their plan to provide for a lesser term." After all, the same Congressional intent articulated in Tennyson would likewise be contravened by permitting debtors to modify a plan to reduce the term to less than the applicable commitment period when unsecured claims have not been paid in full."
>
> ***In re Heideker***, 455 B.R. 263, 271 (Bankr. M.D. Fla. 2011)

VI. **Another Approach**

For the sake of argument, assume, like the majority does, that subsection (b) of section 1325 does not apply to modifications under section 1329. It is undisputed that the plain language of section 1329(a)(1) allows the debtor, the trustee or an unsecured

[2] *Whaley v. Tennyson (In re Tennyson),* 611 F.3d 873 (11th Cir.2010)

allowed claim holder to "**reduce the amount of payments** on claims of a particular class provided for by the plan". This would have the effect to reduce the minimum amount payment to unsecured creditors pursuant to the "disposable income" resulted from the means test.

Subsection (a)(2) allows the debtor, the trustee or an unsecured allowed claim holder to "**extend or reduce the time for such payments".** Which payments can be extended or reduced? The plain language of this subsection identifies those payments, as the ones that could be increased or reduced under subsection (a)(1). The subsection reference to "such payments" immediately after subsection (a)(1) can only be referring to the payments that could be modified under subsection (a)(1). According to the text, subsection (a)(2) is dependent of subsection (a)(1), i.e. if payments are modified under the first subsection then the time of such modified payments could be extended or reduced.

If the first plan, was confirmed after an objection, which triggered the application of § 1325(b), then the order of confirmation presumes a determination that the plan complied with the "applicable commitment period", order that is final. Remember that modification of the finality of the confirmation order is restricted and limited to what is allow under §§ 1328(b) and 1329. Accordingly without any mention to the "applicable commitment period" in § 1329(a)(2), as it is mentioned in subsection (c), it cannot be reasonable interpreted that it allow the "applicable commitment period" to be reduced. [*expressio unius est exclusio alterius*] Since §1325(b) is not applicable, then the previous determination by the Court of an "applicable commitment period" which resulted in a final confirmation order could not be modify under § 1329. If Congress intention was to allow the modification of the "applicable commitment period" it could have clearly said in § 1329(a)(2), to "reduce the applicable commitment period. A more reasonable and holistic interpretation of subsection (a)(2) is that it allows the debtor to extend or reduce the time of those payments modified under subsection (a)(1) within the applicable commitment period, unless extended for cause pursuant to § 1329(c). This restrictive interpretation is consistent with the principles of judgment finality. Congress deliberate exclusion of § 1325(b) as one of the applicable section under § 1329 is unambiguous, modification of payments should be limited to expressed applicable sections, i.e. §§ 1322(a)-(b), 1323(c) and 1325(a).