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KEY DIFFERENCES BETWEEN INDIVIDUAL CHAPTER 11 CASES AND CHAPTER 13 CASES[1]

Revised and amended by Thomas J. Raftery, Esq.

(CAUTION: Most of the statutes cited in the PDF version of this document link to Cornell University Law School, Legal Information Institute's presentation of the U.S. Code. It is incumbent upon the reader to make sure that the information there is up to date. This document is also not intended to give legal advice, rather to point out areas where there are significant differences between chapter 11 and chapter 13 and encourage you to do the research. This document does not list every instance of difference; those you must ascertain for yourself.)

	CHAPTER 11	CHAPTER 13
Eligibility		
Debt amounts.	None. However, see § 101(51D) for definition of a small business debtor which may affect the timing of events in your case. (The current dollar amount to determine whether a debtor is a small business debtor is $2,190,000 or less).	Not eligible if the amount of secured and unsecured debt exceeds certain limits. § 109 (The dollar amounts change every three years with the last change having taken effect on April 1, 2010. § 104(a) The current dollar limits are unsecured debts less than $360,475 and secured debts less than $1,081,400).
Fees		
Filing Fees	$1,046 (as of Nov. 1, 2011)	$281 (as of Nov. 1, 2011)
Trustee's Compensation	None unless trustee appointed. If appointed, compensation based on "commission" set by Code §§ 326(a), 330(a)(7).	Up to 10% of plan payments made by the trustee. 28 U.S.C. § 586(e)(1)(B)(I).
UST Fees	Minimum $325 per quarter; increases as disbursements increase.	None.
Attorney's Fees	Depends on complexity: $15,000 to $25,000+, but a detailed fee application is required.	In chapter 13s presumptive fees vary by jurisdiction, but generally range from $2,500 to $4,500. Higher fees may be obtained in the atypical case by fee application. If presumptive, then a fee application may not be required.

[1] Adapted and updated from materials originally prepared by the Honorable Michael S. McManus, E.D. Cal.

	CHAPTER 11	CHAPTER 13
Committee Fees	Committee authorized to employ attorney and other professionals at estate's expense, Code §§ 330(a), 503(b)(2), 1103(a). Small business debtors may ask that no committee be appointed.	No committees, no fees.
Financial Reporting		
Prepetition Counseling	All individual debtors must go through credit counseling prior to filing a prepetition. Code § 109 (b)(1)	All individual debtors must go through credit counseling prior to filing a prepetition. Code § 109 (b)(1)
Prepetition Tax Returns	If requested by the UST, court, or party in interest, federal income tax returns for the 3 years prior to the petition and unfiled when the case was commenced must be filed with the court. Code § 521 (f)(2), (g)(2).	Same requirement. **Plus**, not later than 7 days before the first date set for the creditors' meeting, a chapter 13 debtor must provide the trustee, and any creditor making a timely request, with a copy of the federal income tax return or transcript for the most recent prepetition tax year for which a return was required. Code § 521 (e); Rule 4002(b)(3) & (4). Plus, Code § 1308(a) requires that all delinquent tax returns due for tax periods ending during the 4-year period prior to the filing of the petition be filed with the appropriate tax entity no later than the day before the first scheduled date for the meeting of creditors.
Statements & Schedules	Code § 521 (a)(1) requires all debtors to file a list of creditors, schedule of assets and liabilities, schedule of current income and current expenditures, statement of financial affairs, Code § 342(b) certificate (only if debts are primarily consumer debts), copies of employer payment advices, statement of monthly net income, and statement of reasonably anticipated increases in income or expenditures.	Same requirement. **But**, in chapter 13 cases, if these documents are not filed within 45 days of the filing of the petition, the case is "automatically" dismissed on the 46th day. Code § 521 (l). Not so in chapter 11 cases.

	CHAPTER 11	CHAPTER 13
Disclosure Statement	If the debtor is not a small business debtor, the plan must be accompanied by a disclosure statement. It must be approved as including "adequate information" necessary for a "hypothetical investor" to make an informed judgment about the plan before acceptances to the plan are solicited. Code § 1125. In Central District of California, the form plan and disclosure statement should be used (and certain judges have individual forms). In a small business case, the court may permit a combined plan and disclosure statement; or use of a form disclosure statement. The court may also conditionally approve the disclosure statement, subject to final approval at the confirmation hearing. Code § 1125(f); Rules 3016(b), 3017.1.	None.
Financial Reports	Code § 308 requires small business debtors to report their current and recent financial status, profitability, cash flow projections, comparisons of actual and projected receipts and disbursements, compliance with the postpetition requirements imposed by the Bankruptcy Code and the Bankruptcy Rules, filing of tax returns, and payment of all administrative expenses and taxes. To a degree, this information is included in the monthly operating reports required by the Office of the United States Trustee.	Section 308 does not apply in chapter 13 cases.
Disposable Income	Official Form 22B must be filed. Rule 1007(b)(5). This form is much less detailed than Official Form 22C. Means test deductions required by Code § 1325(b)(3) are not applicable in a chapter 11.	Official Form 22C must be filed. Rule 1007(b)(6)
Property of the Estate	All property is included in the bankruptcy estate. Code § 541 (a). The estate includes property acquired after the petition is filed as well as an individual debtor's earnings from services. Code § 1115 (a) and (b).	Same requirement.

	CHAPTER 11	CHAPTER 13
The Plan		
Who May File a Plan and When it Must Be Filed	In a small business case, only the debtor may propose a plan in the first 180 days of the case. Thereafter, any party may file a plan. All plans must be proposed by the 300th day. Code § 1121 (e). In all other cases without trustees, only the debtor may file the plan in the first 120 days. If filed, the debtor has until the 180th day to solicit acceptances of the plan. If a trustee is appointed and no plan is filed in the first 120 days, or if the debtor fails to obtain the acceptance of the plan by the 180th day, any party in interest may propose a plan Code § 1121(a), (c), & (d). These time periods can be extended for up to 18 months after petition date (to file a plan) and 20 months after petition date (for acceptances).	Only the debtor may propose a plan. § 1321. It must be filed within 14 days of the filing of the petition. Rule 3015(b).

	CHAPTER 11	CHAPTER 13
Earliest Confirmation Date	A meeting of creditors may occur no earlier than 21 days and no later than 40 days after the order for relief. Rule 2003(a). However, nothing in chapter 11requires that the meeting occur or be completed prior to confirmation. If the debtor solicited prepetition acceptances to a "prepackaged" plan, the court may even dispense with the meeting Code § 341 (e). 28 days' notice of a hearing on disclosure statement and deadline to object to disclosure statement and 28 days' notice of a confirmation hearing and deadline to object to confirmation must be given. (Total process = 60 to 90 days). Rule 2002(b). If a small business debtor files a plan with the petition, if conditional approval is given to the disclosure statement on the 1st day of the case, and if objections may be raised at the confirmation hearing, the hearing could take place as early as the 28th day. Code § 1129(e) requires that the plan of a small business debtor be confirmed no later than 45 days after the plan is filed.	A meeting of creditors may occur no earlier than 21 days and no later than 50 days after the order for relief. Rule 2003(a). Parties must receive 21 days' notice of the meeting. Rule 2002(a)(1). 28 days' notice of a confirmation hearing and deadline to object to confirmation must be given. Rule 2002(b). Confirmation hearing may take place no earlier than 21 days and no later than 45 after meeting of creditors. Code § 1324(b) Assuming: notice of the meeting served on the first day of the case; a meeting on the 21st day; notice of the confirmation hearing served on 14th day; and objections raised at the confirmation hearing, confirmation could occur as early as the 40th day
Confirmation Standards		
Priority Debt	Must be paid in full. Code § 1129(a)(9). Tax priority claims may be paid in installments. If so, interest must be paid, the installments must be regular, and be over a period ending not later than 5 years after the order for relief. Code § 1129(a)(9)(C). Nontax priority claims must be paid on the effective date unless the class accepts deferred cash payments. When paid deferred cash payments, interest must be paid. Code § 1129(a)(9)(B) Debtor must be current on all post-petition domestic support obligations in order to confirm plan. Code § 1129(a)(14).	Must be paid in full, but if the plan has a term of 5 years and provides for the payment of all disposable income to creditors, the plan may provide for less than full payment of a domestic support obligation assigned to, owed directly to, or recoverable by, a governmental unit. Code §§ 507(a)(1)(B), 1322(a)(4). Code § 1322(a)(2) does not require that interest be paid on priority claims when they are paid in installments. No restrictions on the debtor's ability to pay over the length of the plan.

	CHAPTER 11	CHAPTER 13
Voting	Creditors with impaired claims may vote. A class of claims accepts the plan when ½ in number and 2/3 in amount of the claims voting accept the plan. Code §§ 1124, 1126, 1129(a)(8).	Creditors may not vote.
Absolute Priority Rule	If at least one impaired class of claims accepts the plan, it may be confirmed over the rejection of a class of unsecured claims if all claim holders in the rejecting class will be paid in full, or if no holder of a claim or interest junior to the rejecting class will receive or retain anything on account of such claim or interest. Code § 1129(b)(2)(B)(ii). Code § 1129(b)(2)(B)(ii) carves out an exception to the absolute priority rule permitting individual chapter 11 debtors to retain postpetition earnings except to the extent necessary to pay postpetition domestic support obligations.	Because creditors may not vote, there is no absolute priority rule.
Best Interests	Unless the claim holder makes an election under code § 1111(b), a chapter 11 plan must provide to each holder of a claim in an impaired class not less than the present value of the amount that would be paid on such claim if the estate were liquidated under chapter 7. Code § 1129(a)(7).	A chapter 13 plan must provide to each allowed unsecured claim not less than the present value of the amount that would be paid on such claim if the estate were liquidated under chapter 7. Code § 1325(a)(4).

	CHAPTER 11	CHAPTER 13
Best Efforts	If the holder of an allowed unsecured claim objects to confirmation, the plan must either pay unsecured claims in full, or the value of the property distributed under the plan must be no less than the projected disposable income of the debtor. Code § 1129(a)(15). Disposable income must be projected over the longer of the 5-year period following the first plan payment, or the entire period the plan provides for payments. Code § 1129(a)(15). To project disposable income, the debtor's actual expenses, provided they are reasonably necessary for the maintenance or livelihood of the debtor, are deducted from current monthly income. The "presumed expenses" deducted from current monthly income under code § 1325(a)(3) are not applicable. Code §§ 1129(a)(15)(B) & 1325(b)(2).	If the holder of an .allowed unsecured claim or the trustee objects to confirmation, the plan must either pay the unsecured claims in full, or all projected disposable income must be applied to make payments to unsecured creditors. Code § 1325(b)(1). Disposable income projected over 3 years must be devoted to the payment of unsecured creditors if the debtor's annualized current monthly income is less than median family income. If it is more, the commitment period increases to 5 years. §§ 1322(d), 1325(b)(1)(B) & (b)(4). The method of projecting disposable income hinges on whether the debtor's annualized current monthly income is greater than median family income. If greater, the expenses deductible from debtor, current monthly income are limited by the presumed expenses used in the means test. Code § 707(b)(2), 1325(a)(3). If less than or equal to median family income, actual expenses that are reasonably necessary for the maintenance or livelihood of the debtor are deductible from current monthly income as under code § 1129(a)(15)(8). Code § 1325(b)(2).

	CHAPTER 11	CHAPTER 13
Treatment of Certain Claims		
Home Mortgages	The plan may provide for the cure of any arrears on a home mortgage. Code § 1123(a)(5)(G), (b) & (d). ·"Curing" a default is distinct from modification of a claim. *In re Lennington*, 288 B.R. 802 (Bankr C.D. Ill. 2003). Unmatured, unaccelerated claims secured only by the debtor's home cannot be modified. Code § 1123(b)(5). The exception to the anti-modification rule in chapter 13, Code § 1322(c), is not applicable in chapter 11. As a result, it does not appear that a matured or accelerated home loan can be extended unless such is permitted by applicable nonbankruptcy law. A principal residence mortgage or trust deed may be stripped from the home if the creditor is totally unsecured based on senior liens and collateral value.	The plan may provide for the cure of any arrears on a home mortgage. Code § 1322(b)(3). Unmatured, unaccelerated claims secured only by the debtor's home cannot be modified. Code § 1322(b)(2). Section 1322(c) permits chapter 13 debtors to cure defaults under a home mortgage unless and until the home is sold at a foreclosure sale. Also, notwithstanding the maturity of a home loan, the plan may provide for payment of the home loan through the plan pursuant to Code § 1325(a)(5)(8). A principal residence mortgage or trust deed may be stripped from the home if the creditor is totally unsecured based on senior liens and collateral value.
Other Secured Claims	Unlike chapter 13, nothing in chapter 11 prevents an individual debtor from stripping down an undersecured claim into its secured and unsecured parts, and treating each part as a separate and distinct claim. Code § 1129(b)(1)(A). Periodic payments to secured creditors need not be in equal installments. But see secured tax claims below.	Plan may not bifurcate certain undersecured claims into secured and unsecured constituent parts. Code § 1325(a)(5). This prohibition extends to claims secured by purchase money debt incurred within 910 days of the petition and secured by motor vehicles acquired for the personal use of the debtor or incurred during the 1-year period preceding the petition and secured by any other thing at value. If a secured claim is being paid through the plan in periodic payments, "such payments shall be in equal installments." Code § 1325(a)(5)(B)(iii)(I).
Secured Tax Claims	Secured tax claims that would otherwise be priority tax claims under code § 507(a)(8) were they not secured must be paid regular installments over a period ending 5 years after the order for relief and "in a manner not less favorable than the most favored nonpriority unsecured claim provided for by the plan." Code § 1129(a)(9)(D).	No similar limitations.

	CHAPTER 11	CHAPTER 13
Long Term Debt	There is no limitation on the maximum duration of a chapter 11 plan. Consequently, it is possible to provide in the plan for the conversion of short-term debt to long-term debt. However, unless court orders otherwise, an individual chapter 11 debtor is not entitled to a discharge until the "completion of all payments under the plan."· Code § 1141(d)(5)(A). Second, if an unsecured creditor objects, Code § 1129(a)(15)(B) requires an individual chapter 11 debtor to commit all projected disposable income "during the period for which the plan provides payments."	The only debt that may be treated as long-term debt is a debt that matures after the completion of the plan and is not modified by the chapter 13 plan. (Cure permissible.) Provided a chapter 13 plan seeks only to cure an arrearage, long-term debt may continue beyond the length of the plan. Code § 1322(b)(3) & (5).
Duration of Plan		
Minimum Length	There is no mandatory minimum chapter 11 plan length. However, if the holder of an allowed unsecured claim objects to a plan that does not pay unsecured claims in full, "the value of the property distributed under the plan [must be] not less than the projected disposable income of the debtor (as defined in § 1325(b)(2)) to be received during the 5-year period beginning on the date that the first payment is due under the plan, or during the period for which the plan provides payments, whichever is longer." Code § 1129(a)(15)(B).	There is no mandatory minimum chapter 13 plan length. But if the plan does not provide for payment of unsecured claims in full and if the trustee or an unsecured creditor objects, the plan must run 3 to 5 years depending on whether annualized current monthly income exceeds state median family income. Code§§ 1322(d), 1325(b)(4)(A)(ii).

	CHAPTER 11	CHAPTER 13
Maximum Length	Chapter 11 does not limit the length of chapter 11 plans. However, if an unsecured creditor objects, Bankruptcy Code § 1129(a)(15)(B) requires-an individual chapter 11 debtor to commit all projected disposable income for 5 years or, if longer, "during the period for which the plan provides payments." Also, unless the court orders otherwise, no discharge will be issued until the "completion of all payments under the plan." Code § 1141(d)(5)(A).	Absent good cause, a plan cannot require payments for more than 3 years if annualized current monthly income is less than the state median family income. Code § 1322(d)(2). If there is good cause to exceed 3 years, the plan's length may not exceed 5 years. Code § 1322(d)(1)(C). If annualized current monthly income is equal to or more than median family income, a chapter 13 plan may not require payments for more than 5 years. Code § 1322(d)(1).
Modification of Plan		
Pre-Confirmation	Only the proponent of the plan may modify it prior to confirmation. Bankruptcy Code § 1127(a).	Only the debtor may modify the plan prior to confirmation. Code § 1323(a).
Post-Confirmation	If the debtor is an individual, after confirmation of the plan, and whether or not the plan has been substantially consummated, the debtor, any trustee, the United States Trustee, or the holder of an unsecured claim may propose a modification. This right ends when the plan payments have been completed. Code § 1121(e).	After confirmation, the debtor, the trustee, or the holder of an unsecured claim may propose a modification. This right ends when the plan payments have been completed. Code § 1329(a).
Discharge		
Timing	After completion of plan payments. Code § 1141 (d)(5)(A). But the court may order otherwise.	After completion of plan payments. Code § 1328(a)
Domestic Support Obligations	Individual chapter 11 debtor with a "domestic support obligation" is not required to certify currency on all required payments.	Debtor with a "domestic support obligation" also must certify that he or she is current on all required payments before the discharge will be entered. Code § 1328(a).
Financial Management Course	Individual chapter 11 debtor is required to take course to obtain discharge. Code § 1141(d)(3) which references Code § 727(a). See Code § 727(a)(11).	Debtor must complete a financial management course. Code § 1328(g).

	CHAPTER 11	CHAPTER 13
Hardship Discharge	After confirmation but before completion of plan payments, Code § 1141(d)(5)(B) permits an individual debtor to request a hardship discharge.	After confirmation but before completion of plan payments, Code § 1328(b) permits an individual debtor to request a hardship discharge.
Super Discharge	Not available.	Available but watered down. May discharge a debt for willful and malicious injury, *see* Code § 523(a)(6), as well as domestic nonsupport obligations, *see* Code § 523(a)(15). But Code § 1328(a)(4) excepts for restitution or damages awarded in a civil action against the debtor as a result of “willful or malicious injury” that caused personal injury or death.
Consequences When Case is Unsuccessful		
Small Business Debtor Exception to Automatic Stay	The automatic stay does not apply to cases filed by a small business debtor if the debtor was a debtor in an earlier small business, case that remains pending, or it was previously a debtor in a small business that was dismissed or had a plan confirmed within the 2 years preceding the latest petition. Also, an entity that acquires substantially all of the assets of a small business having a petition dismissed or plan confirmed in the preceding 2 years cannot acquire the automatic stay in its own bankruptcy case petition unless it proves by a preponderance of the evidence that the acquisition was not for the purpose of evading Code § 362(n).	Nothing similar in chapter 13.

	CHAPTER 11	CHAPTER 13
Case Pending in Prior Years	If an individual was a debtor in a prior case under chapter 7, 11, or 13, if that prior petition was dismissed, and if the prior petition was pending within 1 year of the new petition, the automatic stay with respect to a debt, property securing such debt, or any lease terminates as to the debtor (but not the estate) on the 30th day after the filing of new case. However, Code § 362(c)(3) does not apply if the new case was filed under a chapter other than chapter 7 after the prior case was dismissed pursuant to Code § 707(b). Code § 362(c)(3)(B) permits any party in interest to file a motion to extend the stay as to all or some creditors. Such a request must be made with notice and a hearing and must be made within 30 days of the filing of the petition.	If an individual was a debtor in a prior case under chapter 7, 11, or 13, if that prior petition was dismissed, and if the prior petition was pending within 1 year of the new petition, the automatic stay with respect to a debt, property securing such debt, or any lease terminates as to the debtor (but not the estate) on the 30th day after the filing of new case. However, Code § 362(c)(3) does not apply if the new case was filed under a chapter other than chapter 7 after the prior case was dismissed pursuant to section 707(b). Code § 362(c)(3)(B) permits any party in interest to file a motion to extend the stay as to all or some creditors. Such a request must be made with notice and a hearing and must be made within 30 days of the filing of the petition.
More than One Case Pending in Prior Years	When an individual debtor has filed two or more prior cases that were pending during the previous year, but were dismissed, the automatic stay never goes into effect. Once again, there is an exception for a case "refiled" under code § 707(b). A party in interest may request that the court impose the automatic stay despite the filing and dismissal of multiple prior petitions. Code § 362(c)(4)(B). Such a request must be made with notice and a hearing and must be made within 30 days of the filing of the petition.	When an individual debtor has filed two or more prior cases that were pending during the previous year, but were dismissed, the automatic stay never goes into effect. Once again, there is an exception for a case "refiled" under code § 707(b). A party in interest may request that the court impose the automatic stay despite the filing and dismissal of multiple prior petitions. Code § 362(c)(4)(B). Such a request must be made with notice and a hearing and must be made within 30 days of the filing of the petition.
Other Issues		
Taxes	§ 1398 of the Internal Revenue Code treats the chapter 11 estate as a separate taxable entity for the debtor. Promptly after filing the chapter 11, the debtor must obtain an employer identification number (EIN). And the debtor (or trustee, if one has been appointed) must file a tax return for the bankruptcy estate. (IRC §6012(a)(9), §6012(b)(4))	§ 1398 is not applicable to chapter 13.

Are You In or Out? Chapter 20s

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Chapter 20 and Its Formation

In Johnson v. Home State Bank, 501 U.S. 78 (1991), the Supreme Court of the United States held that a mortgage surviving a Chapter 7 discharge of debtor's personal liability was a "claim" subject to inclusion in approved Chapter 13 reorganization plan.[1] In essence, the SCOTUS held that a debtor could include a mortgage claim in a subsequent Chapter 13 case despite having already filed a Chapter 7 case and received a discharge. The SCOTUS further discussed that while Congress fashioned express prohibitions from filings and serial filings,[2] Congress did not intend categorically to foreclose the benefit of Chapter 13 reorganization to a debtor who previously has filed a Chapter 7 relief.[3]

Specifically, Chapter 20 consists of a filing of a Chapter 7 case, once discharge is received, the debtor thereafter either files a Chapter 13 or otherwise, converts their Chapter 7 to a Chapter 13 prior to the closing of the case. This process allows for the debtor to (1) prevent creditors from collecting against the debtors personally and (2) allows for secured debts to ride through bankruptcy and become non-recourse against the debtor.

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[1] *Id.* at 78, 7.

[2] 11 U.S.C Section 109(g) - No filings within 180 days of dismissal; 11 U.S.C §727(a)(8) - No Chapter 7 filing within six years of a Chapter 7 or Chapter 11 filing; 11 U.S.C Section 727(a)(9) - limitation on Chapter 7 filing within six years of Chapter 12 or Chapter 13 filing.

[3] United States v. Smith, 499 U.S. 160, 167 (1991)

Chapter 20 - Benefits

Importantly, the discharge in the Chapter 7 case provides the opportunity for an ineligible debtor to otherwise be eligible for a Chapter 13 reorganization.[4] This provides a huge relief from debtors who would otherwise be subject to much higher filing and attorney fees in a Chapter 11.[5] Further, once a discharge is received, the debtor's reorganization plan can focus on the debts that survived the Chapter 7 such as tax debts and secured debts.

Chapter 20 - Limitations

While the debtor is not specifically liable for debts, debtor's estate would be subject to any remaining liability for debts that would survive the Chapter 7 filing.[6] Important to note is that the debtor, who has already received a discharge in a Chapter 7, is precluded from another discharge in the subsequent Chapter 13.[7]

Further, in order to be successful in a Chapter 13 reorganization, the debtor

[4] 11 U.S.C. §109(e) - Secured debts are limited to $1,080,400 and unsecured debts are limited to $360,475

[5] Effective 1, 2011 - Chapter 7 filing fee $306, Chapter 11 filing fee $1046 and Chapter 13 filing fee $281. WWW.USCOURTS.GOV

[6] *Johnson v. Home State Bank*, 501 U.S 78, 87 (1991).

[7] 11 U.S.C §1328(f)(2) - The court shall not grant a discharge of all debts provided for in this plan or disallowed under section 502, if the debtor has received a discharge in a case filed under chapter 13 of this title during the 2-year period preceding the date of such order.

would need to proposed a confirmable plan of reorganization.[8] Even after the Chapter 7 discharge, debtor's income would need to be sufficient or regular to fund a plan, otherwise, a Chapter 20 situation would not be possible and the debtor's estate will not be afforded the ability to address other claims that have survived the previous Chapter 7 discharge.

Chapter 20 and Real Property

Under 11 U.S.C. §506(a), a debtor can have the bankruptcy court determine whether a claim is secured. The court can bifurcate an allowed claim in to both secured and unsecured parts based on the value of the collateral. Under 11 U.S.C. §506(d), the debtor's estate can void an undersecured lien on real property subject to certain limitations.[9] [10] [11]

Lien Stripping in Chapter 20

While Nobleman restricted debtor's ability to avoid or "strip-off" claims against undersecured home mortgages in a Chapter 13,[12] bankruptcy courts and circuit

[8] 11 U.S.C Sections 1322 and 1325.

[9] Dewsnup v. Timm, 502 U.S. 410 (1987) - Prohibited Chapter 7 Debtors from using 11 U.S.C. Section 506(d) to avoid secured liens on real property.

[10] In re Talbert, 344 F.3d 555 (6th Cir. 2003).

[11] Nobleman v. American Savings Bank, 508 U.S. 324 (1993). The SCOTUS held that under 11 U.S.C Sections 1322(b)(2) and 506, an undersecured home mortgage lien could be not avoided or "stripped-off" in a chapter 13 case on a claim secured by debtor's principal residence.

[12] *Id.*

courts through the United States have come to a general consensuses about how that applies two second or third wholly unsecured mortgages in a Chapter 20 context. Under 11 U.S.C. §1322(b), a debtor is restricted from changing the rights of creditors whose claims are secured by debtor's principal residence. However, since Nobleman, §1322 protections are not available to creditors whose lien is junior and wholly unsecured. Instead, this type of creditor's claims can be treated as an unsecured claim and treated similarly to all other unsecured general creditors. This has been accepted by a majority of bankruptcy courts and circuits, with a minority of bankruptcy courts holding that a properly perfected mortgage claims is a security interest in real property irrespective of whether the claim is wholly or partially secured.[13]

While courts have in majority held that a wholly unsecured mortgage can be avoided or "stripped-off" in a Chapter 13 context, there is currently a split within bankruptcy courts and circuit courts about whether a discharge is required in order to avoid a lien under 11 U.S.C. §§1322 and 506 in a Chapter 20. This distinction has come due to debtor's ability to receive a discharge under 11 USC §1328(f) and whether that discharge is required in order to properly avoid a secured claim.[14] [15]

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[13] Pond v. Farm Specialist Realty (In re Pond), 252 F.3d 122 (2nd Cir. 2001); McDonald v. Master Fin., Inc. (In re McDonald), 205 F.3d 606 (3d Cir. 2000); Lane v. W. Interstate Bankcorp (In re Lane), 280 F.3d. 1663 (6th Cir. 2002); Zimmer v. PSB Lending Corp. (In re Zimmer), 313 F.3d 1220 (9th Cir. 2002); Griffy v. U.S. Bank (In re Griffey), 335 B.R. 166 (B.A.P. 10th Cir. 2005); Tanner v. FirstPlus Fin., Inc. (In re Tanner), 217 F.3d 1357 (11th Cir. 2000).

[14] **Holding Unsecured Mortgage Cannot Be Permanently Avoided Without Discharge** - Bank of

Are You In or Out?

Based on the various jurisdictions and understanding of the Bankruptcy Code, Chapter 20s have become common practice. By understanding the jurisdictional variations and limitations of this process, this unique method can be a strong tool to address tax debts in a reorganization and keep debtors in their homes while reducing wholly unsecured liens.

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the Prairie v. Picht (In re Picht), 428 B.R. 885 (B.A.P. 10th Cir. 2010); In re Gerardin, 447 B.R. 342 (Bankr. S.D. Fla. 2011); In re Jarvis, 390 B.R. 600 (Bankr. C.D. Ill. 2008); In re Mendoza, 2010 Bankr. LEXIS 664 (Bankr. D. Colo. Jan. 21, 2010); In re Victorio, 454 B.R. 759 (Bankr. S.D. Cal. 2011), Aff'd sub. nom. Victorio v. Billingslea, 470 B.R. 545 (S.D. Cal. 2012)

[15] **Holding Unsecured Mortgage Can Be Permanently Avoided Without Discharge -** Fisette v. Keller (In re Fisette), No. 11-6012 (B.A.P. 8th Cir. Aug. 29, 2011); In re Jennings, 2011 Bankr. LEXIS 2693 (Bankr. N.D. Ga. July 11, 2011); Davis v. TD Bank (In re Davis), 447 B.R. 738 (Bankr. D. Md. 2011);In re Fair, 450 B.R. 853 (Bankr.E.D. Wis. 2011); In re Waterman, 447 B.R. 324 (Bankr. D. Colo. 2011); In re Tran, 431 B.R. 230 (Bankr. N.D. Cal. 2010); In re Hill, 440 B.R. 176 (Bankr. S.D. Cal. 2010);

POST-PETITION AND POST-CONFIRMATION EARNINGS IN INDIVIDUAL CHAPTER 11 CASES

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Before BAPCPA, 11 U.S.C. §541(a)(6) applied equally to Chapter 7 and Chapter 11 cases and excluded "earnings from services performed by an individual debtor after the commencement of the case" from an individual Chapter 11 debtor's bankruptcy estate. Now, §1115 expressly includes, as property of the estate, all property acquired after the commencement of a bankruptcy case, including earnings from services performed during the Chapter 11. Section 1115(a) provides:

> (a) In a case in which the debtor is an individual, property of the estate includes, in addition to the property specified in section 541—
>
> > (1) all property of the kind specified in section 541 that the debtor acquires after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7, 12, or 13, whichever occurs first; and
> >
> > (2) earnings from services performed by the debtor after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7, 12, or 13, whichever occurs first.

While the addition of *post-petition* earnings into the estate of an individual Chapter 11 substantially changed aspects of individual Chapter 11 case administration, amendments to §1129(a) took matters a step further. Now, an individual Chapter 11 debtor may be required to devote *post-confirmation* earnings to repayment of unsecured creditor under certain circumstances.

An individual Chapter 11 case is by no means simply a mega-Chapter 13 case. Although 11 U.S.C. §1129(a)(15) imports certain concepts from Chapter 13 into individual Chapter 11

reorganization cases, the precise extent to which those concepts are imported has generated substantial debate. One such debate centers around how much of a debtor's disposable income must be devoted to the plan, and how that income is calculated. Similar to a Chapter 13, under §1129(a)(15)(B), an individual Chapter 11 debtor whose plan does not pay all allowed unsecured claims in full may be required to devote all of their "projected disposable income" to the payment of unsecured creditors for 5-years post-confirmation in order to confirm a Chapter 11 plan. Section 1129(a)(15), which is only triggered and applicable upon the objection of an unsecured creditor, provides:

> In a case in which the debtor is an individual and in which the holder of an allowed unsecured claim objects to the confirmation of the plan-
>
> (A) the value, as of the effective date of the plan, of the property to be distributed under the plan on account of such claim is not less than the amount of such claim; or
>
> (B) the value of the property to be distributed under the plan is not less than the projected disposable income of the debtor (as defined in section 1325(b)(2) to be received during the 5-year period beginning on the date that the first payment is due under the plan, or during the period for which the plan provides payments, whichever is longer.

By contrast, Section 1325(b)(2) allows an individual debtor to include as a deduction against disposable income those costs that are reasonably necessary for the "maintenance or support of the debtor or a dependent of the debtor" and, if the debtor is engaged in business, necessary business expenses. Specifically, "disposable income" is defined by §1325(b)(2) as:

> [C]urrent monthly income received by the debtor (other than child support payments, foster care payments, or disability payments for a dependent child made in accordance with applicable nonbankruptcy law to the extent reasonably necessary to be expended for such child) less amounts reasonably necessary to be expended-
>
> (A) (i) for the maintenance or support of the debtor or a dependent of the debtor, or for a domestic support obligation, that first becomes payable after the date the petition is filed; and

(ii) for charitable contributions (that meet the definition of "charitable contribution" under section 548(d)(3)) to a qualified religious or charitable entity or organization (as defined in section 548(d)(4)) in an amount not to exceed 15 percent of gross income of the debtor for the year in which the contributions are made; and

(B) If the debtor is engaged in business, for the payment of expenditures necessary for the continuation, preservation, and operation of such business.

Thus, while §1325(b)(2) defines "disposable monthly income" using a debtor's current monthly income as a starting point, it does not define "projected disposable monthly income," the five-years forward-looking concept of disposable monthly income referred to in §1129(a)(15). This raises the question: is there a difference between *disposable monthly income* under a Chapter 13, and *projected disposable monthly income* in an individual Chapter 11?

In a chapter 13 case, the "means test" is utilized to calculate the amount of disposable income that a debtor must devote to creditor repayment pursuant to a court approved plan that typically lasts from three to five years. The "means test" is set forth on Official Form 22C, where the debtor uses their average gross monthly income, calculated using the average income of the past six months. The debtor then subtracts a mix of IRS standard allowance deductions and the debtor's actual monthly expenditures. The IRS guidelines are used for such expenses as food, clothing, household supplies, fuel, automobile costs and utilities. Form 22C allows the debtor's to use actual expense deductions for such things as health insurance, taxes, child care and car payments. If a chapter 13 debtor rents a home, the IRS guidelines are used to determine their monthly housing allowance. However, if the debtor owns a home, the amount of the monthly mortgage payment is used. After subtracting these allowed expense from the debtor's average monthly income over the past six-months, the resulting figure is deemed to be the debtor's *disposable monthly income*.

There was much post-BAPCPA debate in Chapter 13 case law over whether the means test's disposable-income calculation controlled for all purposes, or whether a bankruptcy court could consider relevant information about a debtor's future income or expenses that varied from the income or expenses utilized in the means test. The debate was over whether "projected disposable income" is calculated by a *mechanical application* of the definition of disposable income using the "means test," or whether courts may deviate from the means test calculation using a *forward looking approach* in order to project the debtor's actual ability to pay.

In 2008, the Ninth Circuit adopted the mechanical approach in In re Kagenveama, 541 F.3d 868 (9th Cir. 2008). The Kagenveama court held that BAPCPA's new definition of disposable income requires a "mechanical approach" to calculation of a debtor's projected disposable income whereby "disposable income" and "projected disposable income" are synonymous. regardless of whether that figure accurately represents a debtor's ability to adhere to a payment plan. Conversely, numerous other courts adopted a "forward looking approach." See In re Lanning, 545 F.3d 1269, 1270 (10th Cir. 2008); In re Frederickson, 545 F.3d 652 (8th Cir. 2008). Under the forward-looking approach, the debtor's disposable income, as defined by the means test, is presumed to be the debtor's projected disposable income. However, under the forward-looking approach, the court may deviate from that figure if it does not accurately reflect the debtor's ability to pay.

The Supreme Court put this issue to rest in the Chapter 13 context in Hamilton v. Lanning, 560 U.S. ___ , 130 S.Ct. 2464, 177 L.Ed.2d 23 (2010), where it adopted the forward looking approach to calculating projected disposable monthly income in a Chapter 13 case, and soundly rejected the mechanical approach. The Supreme Court held that the forward looking approach is supported by the ordinary meaning of the term "projected." Hamilton, 130 S.Ct. at

2471. Noting the term "projected" is not defined by the Code, the Court explained that "in ordinary usage future occurrences are not 'projected' based on the assumption that the past will necessarily repeat itself." Id. "While a projection takes past events into account, adjustments are often made based on other factors that may affect the final outcome." Id., at 2472.

The Hamilton Court also examined pre-BAPCPA case law that points in favor of the "forward-looking" approach. Prior to BAPCPA, the general rule was that courts would multiply a debtor's current monthly income by the number of months in the commitment period as the first step in determining projected disposable income. See, e.g., In re Killough, 900 F.2d 61 (5th Cir. 1990) (per curiam); In re Anderson, 21 F.3d 355 (9th Cir. 1994); In re Solomon, 67 F.3d 1128 (4th Cir. 1995). But courts also had discretion to account for known or virtually certain changes in the debtor's income. See, In re Heath, 182 B.R. 557 (9th Cir. B.A.P. 1995); In re Richardson, 283 B.R. 783 (Bankr. D. Kan 2002); In re James, 260 B.R. 498 (Bankr. D. Idaho 2001); In re Jobe, 197 B.R. 823 (Bankr. W.D. Tex. 1996); In re Crompton, 73 B.R. 800 (Bankr. E.D. Pa. 1987). This judicial discretion was well documented in contemporary bankruptcy treatises. See, 8 Collier on Bankruptcy ¶ 1325.08[4][a], p. 1325-50 (15th ed. rev. 2004) ("As a practical matter, unless there are changes which can be clearly foreseen, the court must simply multiply the debtor's known monthly income by 36 and determine whether the amount to be paid under the plan equals or exceeds that amount"; 3 W. Norton, Bankruptcy Law and Practice § 75.10, p. 64 (1991) ("It has been held that the court should focus upon present monthly income and expenditures and, absent extraordinary circumstances, project these current amounts over the life of the plan to determine projected disposable income.").

Rejecting the mechanical view, the Supreme Court found it clashes repeatedly with the terms of 11 U.S.C. § 1325. First, § 1325(b)(1)(B)'s reference to projected disposable income "to

be received in the applicable commitment period" strongly favors the forward-looking approach. Hamilton, at 2474. The mechanical approach effectively reads "income to be received" out of the statute when a debtor's current disposable income is substantially higher than the income that the debtor predictably will receive during the plan period. Second, § 1325(b)(1) directs courts to determine projected disposable income "as of the effective date of the plan," which is the date on which the plan is confirmed and becomes binding. See, 11 U.S.C. § 1327(a). Id. "Had Congress intended for projected disposable income to be nothing more than a multiple of disposable income in all cases, we see no reason why Congress would not have required courts to determine that value as of the filing date of the plan." Id. "Third, the requirement that projected disposable income "will be applied to make payments" is most naturally read to contemplate that the debtor will actually pay creditors in the calculated monthly amounts." Id. "But when, as of the effective date of a plan, the debtor lacks the means to do so, this language is rendered a hollow command." Id.

Further discrediting the mechanical approach, the Court explained that "in cases in which a debtor's disposable income during the 6-month look-back period is either substantially lower or higher than the debtor's disposable income during the plan period, the mechanical approach would produce senseless results that we do not think Congress intended." Hamilton, at 2475-76.

Following Hamilton, courts now start with the mechanical approach, being the means test results, absent evidence that it is not a reliable projection of future earnings and/or expenses. If such evidence is produced, bankruptcy courts have the discretion to deviate from the mean test to consider and more accurately project future disposable monthly income.

In the case of individual Chapter 11 debtors, Chapter 11 is silent on how projected disposable monthly income is calculated. Although Chapter 11 refers to §1325(b)(2), there is no

standard "means test" used in Chapter 11 cases, or any other standard calculation of disposable monthly income.

The case of In re Roedemeier, 374 B.R. 264, 272 (Bankr. D. Kan. 2007) was the first to address this issue holding that the section 707(b) "means test" expense allowances are not incorporated into the calculation of disposable income for individual chapter 11 debtors. Instead, a chapter 11 debtor's "projected disposable income" under §1129(a)(15) is calculated by the court through "a judicial determination of the expenses that are reasonably necessary for the support of the debtor and his or her dependents." Since the means test applies to the calculation of "projected disposable income" in chapter 13 cases, this decision noted a difference between the two chapters. Although §1129(a)(15) refers to chapter 13 for its projected disposable income calculation, the cross reference is to §1325(b)(2), which merely requires expenses to be "reasonably necessary." Section 1325(b)(2) does not incorporate the §707(b) means test. That test is brought into chapter 13 by section §1325(b)(3), which says that the "reasonably necessary" determination in (b)(2) for above-median income debtors shall be based on the means test.

In Roedemeier, the creditor's argument was that the reference in §1129(a)(15) to §1325(b)(2) and its discussion of "disposable income" impliedly cross-references paragraph (3) of the section as well. The Roedemeier Court rejected this and reasoned that Congress would have made the cross reference explicit if that were its intention, and the lack of such specification indicates that the section 707(b) means test is inapplicable in a chapter 11. In re Roedemeier, 374 B.R. at 272. The Rodemeier, court concluded: "[T]hat in calculating an individual [c]hapter 11 debtor's projected disposable income, §1129(a)(15)(B) must be read to allow a judicial

determination of the expense that are reasonable necessary for the support of the debtor and his or her dependents". Id. at 272-73.

Given the rejection of a strict mechanical approach in Chapter 13, together with the lack of any reference or incorporation of a mechanical approach in Chapter 11, it seems courts are limited to a forward looking in the case of an individual Chapter 11 when the provisions of §1129(a)(15) are triggered. The lack of a mechanical approach in an individual Chapter 11 gives the bankruptcy courts more discretion to examine the unique aspects of an individual debtor's income and expenses. The lack of a mechanical approach also emphasizes the burden on the debtor to offer acceptable income projections, and to establish the reasonableness and necessity of his or her various monthly expenses. With that said, it can be expected that some courts will still resort to the IRS guidelines for expenses, as used on Chapter 13's Form 22C, to gauge the reasonableness of an individual Chapter 11 debtor's proposed monthly expenditures.

While the determination of *projected disposable monthly income* may be based on a forward looking approach, additional changes to the Code softened the consequences of inaccurate projections by providing individual Chapter 11 debtors wide latitude in amending his or her plan post-confirmation.

Business entity Chapter 11 debtors face strict limitations on modifying a confirmed Chapter 11 plan. A business chapter 11 debtor may modify its plan under § 1127(b), which reads:

> The proponent of a plan or the reorganized debtor may modify such plan at any time after confirmation of such plan and before substantial consummation of such plan, but may not modify such plan so that such plan as modified fails to meet the requirements of sections 1122 and 1123 of this title. Such plan as modified under this subsection becomes the plan only if circumstances warrant such modification and the court, after notice and a hearing, confirms such plan as modified, under section 1129 of this title.

11 U.S.C. § 1127(b). Thus, in a business entity Chapter 11, a plan proponent or the reorganized debtor must propose modification before substantial consummation of the plan, and the modification must comply with the requirements of 11 U.S.C. §§ 1122 – 1129.

An individual Chapter 11 debtor has far greater ability to amend his or her plan after confirmation (but before plan payments are complete) under section 1127(e), whether or not the plan has been substantially consummated. An individual debtor or party in interest may seek to modify a plan to provide for an increase or reduction in payment, length of plan payments, or amount of distribution to a creditor whose claim is provided for under the plan so long as other confirmation requirements (as found in sections 1121 through 1129) are met. 11 U.S.C. § 1127(e).

Federal Rule of Bankruptcy Procedure 3019(b) governs requests to modify under section 1127(e). Such requests may be made by any party in interest, not just the proponent. The clerk shall provide not less than twenty-one (21) days' notice of the objection deadline to the debtor, trustee, and all creditors, unless the court orders otherwise with respect to creditors who are not affected by the proposed modification. An objection, which shall be governed by Rule 9014, must be filed and served on the debtor, the proponent of the modification, and the U.S. trustee. If an objection is filed, the hearing is held to consider the proposed modification. Fed. R. Bankr. P. 3019(b).

Similar to Section 1127(e), Section 1329(a) provides a confirmed Chapter 13 plan may be modified prior to the completion of payments under the confirmed plan. The proposed modification may increase or decrease the amount of payments to a particular class of claims, extend or reduce the time for such payments, or alter the amount of a distribution to a creditor provided for in the confirmed plan to the extent necessary to take into account payments from

another source." 11 U.S.C. §1329(a)(1), (2) and (3). To the extent the modification proposes to extend the time for payments, the extension period may not exceed five years after the first payment was due under the original plan. 11 U.S.C. §1329(c). The modified plan must satisfy §§ 1322(a) and 1325(a).

The Ninth Circuit Bankruptcy Appellate Panel has held the disposable income test from §1325(b) is not applicable to post-confirmation plan modifications. In re Sunahara, 326 B.R. 768 (9th Cir. B.A.P. 2005). Instead, the court must generally determine whether the modification has been proposed in good faith. Id. The BAP has explained its holding in Sunahara should not lead to subjective and unpredictable results because the bankruptcy court has an independent duty to determine whether the plan proponent has met his or her burden of proving that the post-confirmation plan modification has been proposed in good faith on a case-by-case basis based on the totality of circumstances. In re Mattson, _____ B.R. _____, 2012 WL 1499824 (9th Cir. B.A.P. 2012).

The projected disposable income test was added to Chapter 13 in 1984. Before the amendment bankruptcy courts were divided on whether a Chapter 13 plan could be confirmed absent a substantial repayment to unsecured creditors. In Mattson, to illustrate the meaning of the good faith test in Chapter 13, the BAP cited In re Goeb, 675 F.2d 1386 (9th Cir. 1982). The Ninth Circuit decided the Goeb case before the disposable income test was added to Chapter 13 in 1984. The issue in Goeb was whether Chapter 13 requires a "substantial" repayment to unsecured claims. The Ninth Circuit held that there was no "substantial" repayment requirement but that the bankruptcy court must nevertheless determine whether the plan was proposed in good faith on a case by case basis based on the totality of circumstances. The Ninth Circuit declined to compile a complete list of relevant considerations but it did indicate that the

bankruptcy court may consider the substantiality of the proposed payment as well as other factors to determine whether the plan is proposed in good faith. Id. In a footnote, the Ninth Circuit emphasized that the good faith "inquiry is directed to whether or not there has been an abuse of the provisions, purpose or sprit of Chapter XIII in the proposed plan." Id. at 1390, n. 9.

In Ransom v. FIA Card Services, N.A., 562 U.S. _____, 131 S.Ct. 716, 178 L.Ed.2d 603 (2011), the Supreme Court held deductions for vehicle payments that would not actually be paid cannot be deducted to calculate projected disposable income. In reaching its conclusion, the Court observed that one of the primary purposes of Congress when it enacted BAPCPA was to ensure that Chapter 13 debtors repay to their creditors the maximum they can afford. Id. See also In re Ransom, 562 U.S. ____, _____, Slip Opinion, Page 17 (2011) (a change in debt service requirements during the term of a confirmed plan may result in a creditor seeking a plan modification under § 1329 to increase the amount a debtor must repay).

While the projected disposable income test of § 1329(b) does not apply to a proposed plan modification, the BAP opinions in Sunahara and Mattson clarify the proposed plan modification should be evaluated based on the debtors' ability to repay his or her creditors. The adequacy of plan payments remains an important factor that the court must evaluate to determine whether the plan modification has been proposed in good faith.

These principles developed in Chapter 13 case law may provide guidance to courts addressing similar issues in individual Chapter 11 cases.

Absolute Roulette:
The Absolute Priority Rule in Individual Chapter 11 Cases

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ABSOLUTE ROULETTE

Right now, the odds of the "fixed principle" of the Absolute Priority Rule (the "Rule")[1] applying in an individual chapter 11 case are roughly the same as landing on red or black on the Roulette Table. Although the Rule was articulated by the Supreme Court during the Taft Administration[2] and the Great Depression,[3] some bankruptcy courts believe that it has been written out of individual chapter 11 cases by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005[4] ("BAPCPA"), while others believe that it still applies. In most instances, a bankruptcy attorney will not know in advance who their client's bankruptcy judge will be, so there is currently no way to pre-determine how the future judge has ruled on the application of the Rule post-BAPCPA. For those attorneys who file individual chapter 11 cases, or represent creditors in those cases, it is therefore vitally important to understand the Rule as well the arguments for and against its application in individual cases.

WHAT IS THE ABSOLUTE PRIORITY RULE?

The requirements for chapter 11 plan confirmation are set forth at 11 U.S.C. Section 1129. Many successful chapter 11 cases result from the use of these requirements as guidelines in negotiations with creditors, ultimately producing a plan that has been consented to by each class of creditors.[5] Even in these consensual cases, however, the requirements of Section 1129(a)(1) through (16) must be met. For the most part, these requirements protect creditors,

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[1] The Rule is currently codified at 11 U.S.C. § 1129(b)(1)-(2). The label "fixed principle" comes from *Case v. Los Angeles Lumber Case*, *infra*.

[2] *Northern Pacific Railroad v. Boyd*, 228 U.S. 482 (1913); The genesis of the Rule appears in post-Civil War railroad cases, where it was held that stockholders could retain no equity or dividends until "all debts of the corporation are paid." *Chicago Rock Island and Pacific Railroad v. Howard*, 74 U.S. 392, 409-410 (1868).

[3] *Case v. Los Angeles Lumber Products Co*., 308 U.S. 106 (1939).

[4] The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Public Law 109-8, 119 Stat 23.

[5] A class of claims accepts a chapter 11 plan if creditors holding at least 2/3 in amount, and ½ in number of claims vote to accept the plan (11 U.S.C. §1126(c)); a class of claims that is not impaired is deemed to have accepted a chapter 11 plan (11 U.S.C. §1124).

for example, by requiring that a plan be feasible[6] (not likely to be followed by another reorganization or liquidation), that the plan is in the "best interest of creditors"[7] (creditors receive at least as much as would be received on liquidation) and by requiring that the each class of creditors consent to the plan.[8]

However, if all of the requirements of chapter 11 plan confirmation contained in Section 1129 are met – except that the plan proponent has not obtained consent from each class, the plan may nonetheless be confirmed if the remaining requirements of Section 1129(a) are satisfied and the plan is does not "discriminate unfairly"[9] and is "fair and equitable." Section 1129(b)(2)(B) defines *fair and equitable* as to unsecured creditors as:

(i) the plan provides that each holder of a claim of such class receive or retain on account of such claim property of a value, as of the effective date of the plan, equal to the allowed amount of such claim; or

(ii) the holder of any claim or interest that is junior to the claims of such class will not receive or retain under the plan on account of such junior claim or interest any property, **except that in the case which the debtor is an individual, the debtor may retain property included in the estate under section 1115, subject to the requirements of subsection (a)(14) of this section.**[10]

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[6] 11 U.S.C. §1129(a)(11).
[7] 11 U.S.C. §1129(a)(7)(B).
[8] 11 U.S.C. §1129(a)(8).
[9] Unfair discrimination may be determine by considering whether the proposed discrimination has a reasonable basis and whether the discrimination is necessary for the reorganization: "The Code does not prohibit unequal treatment of claims that are properly classified in different classes so long as the discrimination is not unfair." *In re Cypresswood Land Partners, I*, 409 B.R. 396, 434 (Bankr. S.D. Tex. 2009); or by a four factor test: (1) whether the discrimination has a reasonable basis; (2) whether the plan can be confirmed without the discrimination; (3) whether the discrimination is proposed in good faith; and (4) how the discriminated classes are treated under the plan. *In re Snyders Drug Stores, Inc.*, 307 B.R. 889, 894-95 (Bankr. N.D. Ohio 2004).
[10] The emphasis is added and refers to the portion of Section 1129(b)(2)(B) which were added by BAPCPA.

This is the codification of the Absolute Priority Rule, which in a nut shell means that senior classes of creditors may require payment in full before a class of creditors or interests junior to them receives anything under the chapter 11 plan. Traditionally, when a chapter 11 plan proponent did not obtain consent from all classes, plan confirmation over the dissenting class would only occur when either the dissenting class was paid in full or – via *cram down* – where no class junior to the dissenting class retained anything under the plan.

An important twist to the Rule, the "New Value Exception," allows a chapter 11 debtor to confirm a plan over a dissenting class of unsecured creditors while still retaining an interest in the reorganized debtor if the debtor offers value that is "(1) new, (2) substantial, (3) money or money's worth, (4) necessary for a successful reorganization, and (5) reasonably equivalent to the value or interest received."[11] Therefore, if the Rule applies in individual chapter 11 cases, in order to overcome a dissenting class of creditors that is not paid in full, the debtor would be required to make a valuable contribution in order to retain property that existed on the instant of the chapter 11 filing.

THE BAPCPA AMENDMENTS

In addition to the aforementioned changes to Section 1129(b)(2)(B)(ii), BAPCPA also added Section 1115 to define property of the bankruptcy estate for individual chapter 11 debtors.

This new section provides:

(a) In a case in which the debtor is an individual, property of the estate includes, in addition to the property specified in section 541 -

[11] *In re Bonner Mall Partnership*, 2 F.3d 899, 908-09 (9th Cir. 1993).

(1) all property of the kind specified in section 541 that the debtor acquires after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7, 12, or 13, whichever occurs first; and

(2) earnings from services performed by the debtor after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7, 12, or 13, whichever occurs first.

The results of the current crap shoot of whether or not the Absolute Priority Rule will apply in an individual chapter 11 case is determined by one of two views: whether (a) the bankruptcy court believes that the newly added language of section 1129(b)(2)(B)(ii) and Section 1115 means that the debtor may keep all pre-bankruptcy property (as defined by Section 541) and all post-bankruptcy petition property (as defined by Section 1115), without adhering to the Rule (the "Broad View"), or (b) the bankruptcy judge believes that the individual Debtor may only retain post-bankruptcy petition property – leaving the Rule intact and requiring either payment in full to the dissenting senior class, or no retention of pre-Petition property absent compliance with the New Value Exception (the "Narrow View"). The published decisions come to their conclusions using differing grammatical interpretations of the new sections, they disagree over whether the amendments to Sections 1115 and 1129(b)(2)(B are *plain and unambiguous*[12] and they offer divergent views over how much Congress intended individual 11s to be akin to chapter 13 cases.

[12] Hence, invoking the Plain Meaning Rule as set forth in *Lamie v. U.S. Trustee,* 540 U.S. 526, 534 (2004).

THE BROAD VIEW

The Broad View gets its moniker from the conclusion that Congress intended that an individual Chapter 11 Debtor keep both pre and post-Petition property through the reorganization process, without the requirement that senior classes be paid in full. But courts that adhere to the Broad View arrive at this conclusion for different reasons. For example, the Bankruptcy Appellate Panel in *In re Friedman*[13] based its decision on what it believed is the plain meaning of newly added portions of Section 1129(b)(2)(B)(ii) and Section 1115:

> Section 1115's identification of estate property consists of the property contained in §541 and the two post-petition acquired assets – newly acquired property and income. The so-called disputes over what "included" means in § 1129 (b) (2) (B) (ii) and "in addition to" in § 1115 arise from misinterpretation of the words. "Included" is not a word of limitation. To limit the scope of the estate property in §§ 1129 and 1115 would require the statute to read "included, except for the property set out in Section 541" (in the case of § 1129 (b) (2) (B) (ii)), and "in addition to, but not inclusive of the property described in Section 541" (in the case of § 1115).
>
> A plain reading of §§ 1129 (b) (2) (B) (ii) and 1115 together mandates that the absolute priority rule is not applicable in individual chapter 11 debtors cases. [14]

Other Broad View decisions agree with courts that do not see a plain meaning in the new provisions, but nonetheless find congressional intent to abrogate the Rule and make individual chapter 11 cases much like *Chapter13s on steroids*. One of the earlier bankruptcy court decisions on the subject[15] reasoned:

> The broader view of the exception, on the other hand, helps to explain why a number of changes, including the exception, were made to Chapter 11, namely, so that it could function for individual debtors much like Chapter 13 does. Many of the BAPCPA's changes to Chapter 11 apply only to individual debtors and are clearly drawn from the Chapter 13 model:

[13] 466 B.R. 471 (9th Cir BAP 2012).
[14] *Id.* at 482 (internal citations omitted). *Plain Meaning* was also found by the courts in *SPCP Group, LLC v. Biggins*, 465 B.R. 316 (M.D. Fla. 2011); *In re Tegeder*, 369 B.R. 477 (Bankr. D. Neb 2007).
[15] *In re Roedemier,* 374 B.R. 264 (Bankr. D. Kan. 2007)

1. § 1115 brings property the debtor acquires postpetition into the estate;

2. § 1123(a)(8) calls for the debtor's plan to provide for payment to creditors from the debtor's postpetition earnings from services or other future income;

3. the exception in § 1129(b)(2)(B)(ii) allows the debtor to keep property included in the estate under § 1115, without paying in full a class of unsecured creditors that rejected his or her plan;

4. § 1129(a)(15) authorizes the debtor to overcome an objection to the plan made by a single unsecured creditor by proposing to distribute under the plan property worth at least as much as the debtor's projected disposable income for a five-year period;

5. § 1141(d)(5) ordinarily delays the entry of the debtor's discharge until completion of all payments under the plan; and

6. § 1127(e) permits modification of a confirmed plan even after substantial consummation for certain purposes.

Significantly, Chapter 13 does not impose the absolute priority rule on debtors. Taken together, these changes indicate Congress intended to extend the exemption from the absolute priority rule to individual Chapter 11 debtors as well.[16]

Not surprisingly, courts that disagree with the Broad View are not convinced that the foregoing evidences intent by Congress to abrogate the Rule.

THE NARROW VIEW

The most recent, and the highest Court to date to publish a decision on the application of the Rule to individual chapter 11 cases, found (as many courts have[17]) ambiguity in the newly added language. In the *Maharaj*[18] decision, the Fourth Circuit Court of Appeals stated that:

> There are two competing constructions of the "included in the estate" language. On one view, the phrase "included in" means the equivalent of "added to," since property of the estate has long been defined under § 541. On another view, however, this language "included in" means something close to "referenced" in § 1115, in which case § 541 was

[16] *Id.* at 275, 276.

[17] See *Friedman*, 466 B.R. at 485, (Jury, J. Dissenting opinion); *In re Lindsey,* 453 B.R. 886 (Bankr. E.D. Tenn, 2011); *In re Kamell*, *451 B.R. 505* (Bankr. C.D. Cal. 2011). *In re Gelin*, 437 B.R. 435 (Bankr. M.D. Fla 2010).

[18] *In re Maharaj*, 681 F.3d 558 (4th Cir. 2012).

merely "absorbed" and "superseded" into § 1115 for individual Chapter 11 debtors . *See, e.g., Kamell,* 451 B.R. at 509. On the face of the statute, either construction is plausible.

The same is true with respect to the "in addition to the property specified in section 541" language found in §1115. Court-Assigned Amicus-in this case asks us to treat that language as a signpost, used only to note that § 541 property is already included in the bankruptcy estate, because it is set aside from the rest of § 1115 by a comma and a dash, indicating that it is "not essential" to the statute's meaning. Stated differently, because §541 independently includes all § 541 property in the estate, it would be a redundancy to "reinclude" that property through the § 1115 language. On the other hand, several bankruptcy courts have noted that a plausible reading of that language (coupled with the "included in the estate" language) indicates that § 541 operates in § 1115 as a subset of § 1115. *See, e.g., Friedman,* 466 B.R. at 482. By that construction, § 541 property, which is referenced by § 1115, is literally "property included in the estate under § 1115."[19]

Finding no plain meaning, the Fourth Circuit Court of Appeals first relies on the statutory interpretation set forth by the California bankruptcy court in *Karlovic*[20] in favor of keeping the Rule intact:

> [P]rior to BAPCPA, property of the estate did not include post-petition acquired property and earnings for individuals and non-individuals alike. Hence, post-petition acquired property and earnings could be retained by a Chapter 11 debtor, individual and non-individual alike, without running afoul of the [absolute priority rule]. The addition of § 1115 potentially changed that by adding to the property of the estate of an individual post-petition acquired property and earnings. Without a corresponding change to § 1129(b)(2)(B)(ii), individual debtors could no longer retain post-petition acquired property and earnings if they wished to "cram down" a plan. By adding the language excepting the § 1115 property from the [absolute priority rule] of § 1129(b)(2)(B)(ii), Congress merely ensured that the [absolute priority rule] would be the same as it had been prior to BAPCPA and be the same for all Chapter 11 debtors. In other words, what Congress took from the individual debtor with its § 1115-hand, it returned for application of the [absolute priority rule] with its § 1129(b)(2)(B)(ii)-hand.[21]

Next, the Appellate Court in *Maharah*, like many of the Narrow View decisions, finds no clear indication that Congress intended to abrogate the Rule for individual debtors, holding that "to the contrary we are in agreement with those courts that have concluded that, if Congress

[19] *Id*., at 569.
[20] *In re Karlovich*, 456 B.R. 677 (Bankr. S.D. Cal. 2010).
[21] *Maharaj*, 681 F.3d at 569 - 570 (citing *Karlovich*, 456 B.R. 677, 681).

intended to abrogate such a well-established rule of bankruptcy jurisprudence, it could have done so in a far less convoluted manner."[22] In fact, the Court contrasts the legislative history of BAPCPA with the 1952 amendment to the Bankruptcy Act that eliminated the "fair and equitable" requirement from small business cases:

> When Congress amended the Act in 1952 to eliminate the "fair and equitable" requirement, it clearly explained its actions in the accompanying legislative history. Not only did Congress amend the Act to state that plan confirmation shall not be refused because "the interest of a debtor . . . will be preserved under the arrangement," but Congress explained itself in the Congressional Record: "[T]he fair and equitable rule . . . cannot realistically be applied[.] *See* H.R. Rep. 82-2320. History shows that Congress knows how to abrogate the absolute priority rule, and it has not done so here.[23]

Finally, the Mahara Court simply did not buy into the *Chapter 13 on steroids* argument. The Court instead agreed with courts that reason that although Congress may have intended to harmonize chapter 11 and 13 in some respects, the overall legislative history of BAPCPA evidences intent that individual debtors pay creditors more, not less. Since the elimination of the Rule for individual chapter11 cases would allow debtors to retain all pre and post Petition property without payment in full to senior classes, or a new value contribution, the Court believed such a result runs contrary to congressional intent of BAPCPA.[24]

In a similar fashion, and notwithstanding the Bankruptcy Appellate Panel's decision in *Friedman*, some bankruptcy courts within the Ninth Circuit find that the Rule still applies in individual Chapter 11 cases.[25] As one post-*Friedman* bankruptcy court decision points out, negotiations that occur as a result of the "fine-tuned balance between the rights of a Chapter 11 debtor and the creditors" created by the Rule would be eliminated by the Broad View, resulting

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[22] *Maharaj*, 681 F.3d at 571.
[23] *Id. at* 572.
[24] *Id. at* 574.
[25] *In re Arnold*, 471 B.R. 578, 590 (Bankr. C.D. Cal. 2012)(bankruptcy court held that it was "not bound by, the decision of the BAP in *Friedman* ….").

in a lack of incentive for an individual chapter 11 debtor to bargain with creditors.[26] Conversely, the Narrow View retains the bargaining process via the Rule's creditor protections, reducing the danger of "too good a deal" for debtors. [27]

WHO WINS?

Having never left Vegas a financial winner, the author is remiss to make any attempt at predicting whether the *Broad View* or *Narrow View* will ultimately prevail. However, odds are certain that the outcome of the debate will be closely monitored by practitioners in the individual chapter 11 space.

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[26] *Id.*at 611.
[27] *Id.*