

*Business/Consumer Cross-Over Track*  
**Individual Chapter 11 Cases**

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**WARNING!**



**INDIVIDUAL CHAPTER 11s  
ARE NOT  
CHAPTER 13s ON STEROIDS**

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<b>Chapter 11 for Individuals v. Chapter 13: A Comparative Analysis</b>		
	<b>Chapter 11</b>	<b>Chapter 13</b>
<b>Effect of Bankruptcy Filing and Bankruptcy Basics</b>		
<b>Co-Debtor Stay</b>	There is no co-debtor stay; however, a stay of actions against third parties may be imposed in very limited circumstances. See 11 U.S.C. § 105.	11 U.S.C. § 1301.
<b>Property of the Estate</b>	Post-petition income of the debtor also is property of the estate. 11 U.S.C. § 1115(a).	Same. 11 U.S.C. § 1306(a).
<b>Debt Limits</b>	Chapter 11 has no debt limits	Chapter 13 has debt limits: no more than \$360,475 in unsecured debt, and no more than \$1,081,400 in secured debt.

	<b>Chapter 11</b>	<b>Chapter 13</b>
<b>Disposable Income</b>	Disposable income must be calculated pursuant to 11 U.S.C. § 1325(b)(2) rather than through a means test deduction (used for higher income chapter 13 debtors); <u>Official Form 22B</u> must be filed. 11 U.S.C. § 1129(a)(15).	If the debtor's income exceeds the applicable median for their state, then disposable income is determined in accordance with the means test of 11 U.S.C. § 707(b)(2) (A) and (B). <u>Official Form 22C</u> must be filed, which is more detailed than Official Form 22B required in an individual chapter 11 case. 11 U.S.C. § 1325(b)(2).
<b>Supervision of Debtor and Case</b>	The United States Trustee and a chapter 11 trustee, if one is appointed.	The standing chapter 13 trustee.

	Chapter 11	Chapter 13
<b>Financial Filings</b>		
<b>Financial Reports</b>	Monthly reports of the debtor's post-petition business operations are required.	Reports of increases in income and expenses may be required.
<b>Timeline for Filing Proof of Claims</b>	Set by order of the Court. <i>See</i> Bankruptcy Rule 3003(c)(3).	Set by Rule (generally within 90 days after the first date set for the meeting of creditors). <i>See</i> Bankruptcy Rule 3002(c).
<b>Split Year Tax Elections</b>	Pre-bankruptcy losses to be spread over the life of Plan  Post bankruptcy – hopefully no losses	

**Absolute Priority Rule  
in Chapter 11 vs. Chapter 13**

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	Chapter 11	Chapter 13
<b>Absolute Priority Rule</b>	<p>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, <u>except that in the case of an individual, the debtor may retain property included in the estate under section 1115</u>, 11 U.S.C. § 1129(b)(2)(B)(ii).</p> <p>The 4<sup>th</sup>, 5<sup>th</sup> and 10<sup>th</sup> Circuits hold the absolute priority rule applies to individuals in chapter 11 cases; the remaining circuits either hold the opposite (the 9<sup>th</sup> Circuit) or have not addressed the issue.</p> <p>Compare Section 1115 to Section 1306 of the Bankruptcy Code.</p>	Not applicable.

	Chapter 11	Chapter 13
<b>New Value Exception to the Absolute Priority Rule</b>	<p>Requires equity holders to make a <i>substantial</i> and <i>essential</i> contribution in exchange for their continued ownership of the debtor.</p> <p>To be substantial, most courts require that the contribution (i.e., new value) be: (1) a present contribution; (2) freely tradable in the market; and (3) money or money's worth.</p> <p>To be essential, the case law generally mandates that this new contribution be directly related to the success of the reorganization plan.</p>	Not applicable.

**Difference in Plan requirements for  
Chapter 11 vs. Chapter 13**

	Chapter 11	Chapter 13
<b>The Plan</b>		
<b>Who May File a Plan and When</b>	<p>In a small business case, only the debtor may propose a plan of reorganization in the first 180 days of the case. Thereafter, any party may file a plan. All plans must be proposed by the 300<sup>th</sup> day. 11 U.S.C. § 1121(e).</p> <p>In all other cases without a trustee, only the debtor may file the plan in the first 120 days. If filed, the debtor has until the 180<sup>th</sup> 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 180<sup>th</sup> day, any party in interest may propose a plan. 11 U.S.C. § 1121(a), (c) and (d).</p> <p>These time periods may be extended for up to 18 months after the petition date (to file a plan) and 20 months after the petition date (for acceptances).</p>	<p>Only the debtor may proposed a payment plan. 11 U.S.C. § 1321. The plan must be filed within 14 days of the filing of the petition. Bankruptcy Rule 3015(b).</p>

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	Chapter 11	Chapter 13
<b>Form of Plan Documents</b>	<p>Except in small business cases, where there is an optional official form (See Official Form 25A, 25B), there is no "standard" chapter 11 plan.</p> <p>The plan of reorganization must be accompanied by a disclosure statement, which must be approved by the court as including "adequate information" necessary for a "hypothetical investor" to make an informed judgment about the plan before acceptances to the plan are solicited. 11 U.S.C. § 1125.</p> <p>In a small business case, a separate disclosure statement is not required; the court may permit a combined plan and disclosure statement or the use of a form disclosure statement. The court also may approve the disclosure statement conditionally subject to the final approval at the confirmation hearing. 11 U.S.C. § 1125(f) and Fed. R. Bankr. P. 3016(b) and 3017.1.</p>	<p>Typically a form plan is used in Chapter 13 cases. The mandatory and permissive plan provisions for Chapter 11 are set forth in 11 U.S.C. § 1322.</p> <p>Disclosure Statements are not applicable in Chapter 13.</p>

	Chapter 11	Chapter 13
<b>Earliest Confirmation Date</b>	<p>28 day notices are required both for a hearing on approval of the disclosure statement and for the deadline to object to disclosure statement; a 28 day notice is required for the confirmation hearing; and the deadline to object to confirmation must be given. See Bankruptcy Rule 2002(b).</p> <p>In a small business case, the hearing could take place as early as the 25<sup>th</sup> day of the case, if certain pre-conditions are met. The plan of a small business debtor be confirmed no later than 45 days after the plan is filed. See 11 U.S.C. § 1129(e).</p>	<p>Parties must receive at least 21 days notice of the meeting. See Bankruptcy Rule 2002(a)(1).</p> <p>28 day notice of confirmation hearing and deadline to object to confirmation must be given. Bankruptcy Rule 2002(b).</p> <p>The confirmation hearing may take place no earlier than 20 days and no later than 45 days after the meeting of creditors. 11 U.S.C. § 1324(b).</p> <p>The confirmation hearing could occur as early as the 40<sup>th</sup> day of the case, if certain pre-conditions are met.</p>

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	Chapter 11	Chapter 13
<b>Special Treatment of Certain Claims</b>		
<b>Home Mortgages</b>	<p><u>Cure:</u> The plan may provide for the cure of any arrearages on a home mortgage. U.S.C. § 1123(a)(5)(G), (b) and (d).</p> <p><u>Modification:</u> Unmatured, unaccelerated claims secured only by the debtor's home cannot be modified. 11 U.S.C. § 1123(b)(5).</p> <p>The exception to the anti-modification rule in chapter 13 (11 U.S.C. § 1322(c)) is not applicable in chapter 11.</p>	<p><u>Cure:</u> The plan may provide for the cure of any arrearages on a home mortgage. 11 U.S.C. § 1322(b)(3).</p> <p><u>Modification:</u> Unmatured, unaccelerated claims secured only by the debtor's home cannot be modified. See 11 U.S.C. § 1322(b)(2).</p> <p>Notwithstanding the maturity of a home loan, the plan may provide for payment of the home loan through the plan pursuant to 11 U.S.C. § 1325(c)(2).</p>
<b>Other Secured Claims</b>	<p>No restrictions on strip downs. 11 U.S.C. § 1129(b)(1)(A).</p> <p>Periodic payments need not be in equal installments.</p>	<p>Vehicle loans limitation. 11 U.S.C. § 1325(a)(9).</p> <p>Periodic payments must be in equal installments. 11 U.S.C. § 1325(a)(5)(B)(iii)(I).</p>

	Chapter 11	Chapter 13
<b>Special Treatment of Certain Claims</b>		
<b>Priority Claims</b>	<p>Priority claims in Chapter 11 cases must be paid in full. 11 U.S.C. § 1129(a)(9). Claims allowed under 507(a)(2) and (a)(3) must be paid in cash on the effective date, unless the holder of such claims agrees otherwise.</p> <p>Claims allowed under sections 507(a)(1),(4),(5), (6), (7) may be paid under the plan (provided the class has accepted the plan) or in full on the effective date. Priority tax claims must bear interest and not exceed five years after the order for relief. 11 U.S.C. § 1129(a)(9)(C).</p> <p>All post-petition domestic support obligations must be current in order to confirm a plan. 11 U.S.C. § 1129(a)(14).</p>	<p>Priority claims may be paid over the length of the plan, unless the holder of a particular claim agrees to difference treatment. 11 U.S.C. § 1322(a)(2).</p>

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	Chapter 11	Chapter 13
<b>Special Treatment of Certain Claims</b>		
<b>Cosigned Debt</b>	Chapter 11 has no comparable provision, however, in chapter 11, all claims classed together must be substantially similar and, if the plan is not accepted by all classes, it must be "fair and equitable." 11 U.S.C. §§ 1122, 1129(b)(1).	A chapter 13 plan can separately classify cosigned consumer debt, and pay it differently from other debt, with the only requirement being that the claims classifications may not discriminate unfairly. 11 U.S.C. § 1322(b)(1).

	Chapter 11	Chapter 13
<b>Special Treatment of Certain Claims</b>		
<b>Student Loans</b>	<p>"Undue Hardship" 11 U.S.C. § 523(a)(8)(B)</p> <p><u>In re Brunner</u>, 46 B.R. 752, 753 (Bankr. S.D.N.Y. 1985) (Aff'd by 831 F.2d 395 (2d Cir. 1987))</p> <ol style="list-style-type: none"> <li>1. Minimal standard of living. <u>Brunner</u>, 831 F.2d at 396.</li> <li>2. Current state of affairs is likely to persist. <u>Brunner</u>, 831 F.2d at 396.</li> <li>3. Good faith effort of repayment. <u>Brunner</u>, 831 F.2d at 396.</li> </ol>	
<p><b>QUESTION:</b> Okay to separately classify and pay?</p> <p>Are there gerrymandering issues?</p>		

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	Chapter 11	Chapter 13
<b>Duration of Plan</b>		
<b>Minimum Length</b>	No mandatory minimum chapter 11 plan length, but see 11 U.S.C. § 1129(a)(15)(B).	No mandatory minimum chapter 13 plan length, but see 11 U.S.C. §§ 1322(d), 1325(b)(4)(A)(ii).
<b>Maximum Length</b>	No mandatory maximum chapter 11 plan length.	A chapter 13 plan may not require payments for more than 5 years. 11 U.S.C. § 1322(d)(1).
<b>Modification of Plan</b>		
<b>Pre-Confirmation</b>	Only the proponent of the plan may modify if prior to confirmation. 11 U.S.C. § 1127(a).	Only the debtor may modify the plan prior to confirmation. 11 U.S.C. § 1323(a).
<b>Post-Confirmation</b>	The debtor, any trustee, the United States Trustee, or the holder of an unsecured claim may propose a modification. 11 U.S.C. § 1121(e).	After confirmation, the debtor, the trustee or the holder of an unsecured claim may propose a modification. 11 U.S.C. § 1329(a).

	Chapter 11	Chapter 13
<b>Plan Voting and Objections</b>	Creditors may file objections to the confirmation if the plan does not comply with the requirements of the Bankruptcy Code. 11 U.S.C. § 1129. Creditors with impaired claims are given the opportunity to vote on a chapter 11 plan. 11 U.S.C. §§ 1125, 1126.	There is no voting in chapter 13, but creditors may file objections pursuant to 11 U.S.C. § 1325 and the Chapter 13 trustee files recommendations regarding plan confirmation.  Disposable income to be received in the applicable commitment period (three to five years). 11 U.S.C. §§ 1322(d), 1325(b)(1)(B) and (b)(4).

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	Chapter 11	Chapter 13
<b>Plan Payments</b>	Payments under the plan do not begin until the effective date of the plan.	The first plan payment is due 30 days after the petition is filed. 11 U.S.C. § 1326.
<b>Early Payout Prospects</b>	Shorten plan length	Shorten plan length
<b>Post-petition Income</b>	§ 1115(a)	§ 1306(a)
<b>Judge's View</b>	<ul style="list-style-type: none"><li>• Oversight Role</li><li>• § 1129</li><li>• Submission of Declarations</li><li>• Go With the Flow Where There is a Stipulated Order or No Creditor Objection?</li></ul>	

### Confirmation issues in Chapter 11 vs. Chapter 13

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	Chapter 11	Chapter 13
<b>Confirmation Standards</b>		
<b>Feasibility</b>	<p>To obtain confirmation of the Plan, the Debtor must demonstrate that the Plan satisfies the provisions of section 1129(a) of the Bankruptcy Code by a <b>preponderance of the evidence</b>.</p> <p>Confirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan, unless such liquidation or reorganization is proposed in the plan. 11 U.S.C. §1129(a)(11).</p>	<p>A debtor's resources are measured by the debtor's anticipated income over a three to five year time period as well as assets that a debtor may sell or liquidate under Section 363 during the life of a plan with proceeds contributed to the plan. 11 U.S.C. §1325(a)(4)</p>
<b>Good Faith</b>	<p>(a) The court shall confirm a plan only if . . . .                      (3) The plan has been proposed in good faith and not by any means forbidden by law. 11 U.S.C. §1129(a)(3).</p>	<p>Good faith is a test set forth in Section 1325(a)(3) which permits a Court to confirm a plan if "the plan has been proposed in good faith and not by any means forbidden by law."</p>

	Chapter 11	Chapter 13
<b>Best Interests of Creditors Test</b>	<p>Each holder of a claim in an impaired class must receive not less than the present value of the amount that would be paid on such a claim if the estate were liquidated under chapter 7. 11 U.S.C. § 1129(a)(7).</p>	<p>Each allowed unsecured claim must receive not less than the present value of the amount that would be paid on such claim if the estate were liquidated under chapter 7. 11 U.S.C. § 1325(a)(4).</p>
<b>Best Efforts</b>	<p>If the holder of an allowed unsecured claim objects to confirmation, the plan must 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. 11 U.S.C. § 1129(a)(15).</p> <p>Disposable income must be projected over at least a five year period following the first plan payment, or if longer than five years, over the entire period the plan provides for payments. 11 U.S.C. § 1129(a)(15).</p>	<p>If the holder of an allowed unsecured claim or the trustee objects to confirmation, the plan must pay the unsecured claims in full or all projected disposable income must be applied to make payments to unsecured creditors. 11 U.S.C. § 1325(b)(1).</p> <p>Disposable income projected over three to five years. 11 U.S.C. §§ 1322(d), 1325(b)(1)(B) and (b)(4).</p>

## THE SUB ROSA SUBCHAPTER: INDIVIDUAL DEBTORS IN CHAPTER 11 AFTER BAPCPA

Bruce A. Markell\*

*Reorganization under the Bankruptcy Code serves the public interest by providing worthy debtors a mechanism to gain relief from crushing debt while maintaining some measure of fidelity to creditors. The Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) of 2005 initiated fundamental changes to this mechanism in an effort to ensure the continued worthiness of bankruptcy applicants.*

*BAPCPA changes a number of provisions in the Code with respect to individual debtors. This article suggests that BAPCPA's provisions have created and will continue to create unexpected anomalies in individual chapter 11 cases, due in large part to the manner in which BAPCPA provisions affecting such individuals are scattered throughout the Code. The author contends that BAPCPA's reworking of chapter 11 created a hidden category of individual reorganization. As Congress was building this mystery, it unnecessarily masked the import of substantive changes to chapter 11. Attempting to shed light on the matter, the author explores the roots of the BAPCPA provisions and summarizes the five most significant adjustments relevant to individual debtors in chapter 11, contrasting chapter 11's operation with that of chapter 13.*

*Chapter 11 for individuals post-BAPCPA tends to work mischief at all stages in the reorganization process. New concerns arise with regard to the debtor's ability to pay expenses necessary to achieve confirmation of the reorganization plan. Uncertainties exist regarding the allocation of property into the estate, and as to who may have standing in postconfirmation plan modifications. As the article suggests, Congress could have avoided, or even discovered, many of these difficulties if BAPCPA's provisions had been grouped together as a separate subchapter to chapter 11.*

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\* United States Bankruptcy Judge, District of Nevada; Senior Fellow in Bankruptcy and Commercial Law, William S. Boyd School of Law, University of Nevada, Las Vegas. Thanks are due to Sally S. Neely and Elizabeth Perris, whose prior writing and subsequent guidance have kept me from making too many howlers. Errors that remain are, of course, mine alone.

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## I. INTRODUCTION

Individuals<sup>1</sup> and chapter 11<sup>2</sup> have a rocky history. It took a Supreme Court decision to confirm that individuals were eligible debtors under chapter 11.<sup>3</sup> Even when individuals were allowed to file, fights broke out over what property was theirs<sup>4</sup> and whether they could ever use the new value corollary to the absolute priority rule.<sup>5</sup>

This chafing is more than a mere annoyance. The number of individual chapter 11 cases is not small. Indeed, it far exceeds chapter 11 cases in which the debtor is a public company. By some counts, individual chapter 11 cases account for between 10 to 15%,<sup>6</sup> and perhaps as much as 36%,<sup>7</sup> of all chapter 11 bankruptcy cases. This means that in fiscal year 2005, which saw an all-time low of some 6800 chapter 11 filings,<sup>8</sup> at least 680 individuals, and maybe as many as 2448 individuals, filed

1. The term “individual” is not defined in the Bankruptcy Code, or for that matter, in the Uniform Commercial Code, even though both codes use the term extensively. When used in this article, I mean a flesh-and-blood, living human being, not some artificial juridical entity.

A good introductory examination of the new chapter 11 provisions for individuals is Sally S. Neely, *How BAPCPA Changes Chapter 11 for Individuals—or—No, This Is Not Your Mother’s Chapter 11!!* (unpublished materials prepared for New York University’s Workshop on Bankruptcy and Business Reorganizations on Sept. 14–16, 2005) (on file with author). See also Paul W. Bonapfel, *Individual Chapter 11 Cases Under BAPCPA*, AM. BANKR. INST. J., July–Aug. 2006, at 1. In addition, several other authors have begun to explore some of the more interesting ramifications of the changes discussed in this article. See, e.g., Robert J. Keach, *Dead Man Filing Redux: Is the New Individual Chapter Eleven Unconstitutional?*, 13 AM. BANKR. INST. L. REV. 483 (2005); G. Ray Warner, *Garnishment Restrictions and the Involuntary Chapter 11: Rethinking Kokoszka in a Means Test World*, 13 AM. BANKR. INST. L. REV. 733 (2005); Jack F. Williams & Jacob L. Todres, *Tax Consequences of Post-Petition Income as Property of the Estate in an Individual Debtor Chapter 11 Case and Tax Disclosure in Chapter 11*, 13 AM. BANKR. INST. L. REV. 701 (2005).

2. 11 U.S.C. §§ 1101–1174 (2000).

3. *Toibb v. Radloff*, 501 U.S. 157 (1991).

4. *Compare In re Herberman*, 122 B.R. 273 (Bankr. W.D. Tex. 1990), with *In re FitzSimmons*, 725 F.2d 1208 (9th Cir. 1984).

5. *Compare In re Gosman*, 282 B.R. 45 (Bankr. S.D. Fla. 2002) (holding that one may not use homestead as “new value” contribution; exempt property must be devoted to creditors’ claims in chapter 11 plan), with *In re Henderson*, 321 B.R. 550, 558–60 (Bankr. M.D. Fla. 2005) (holding that one may use exempt homestead as “new value” contribution), and *In re Henke*, 90 B.R. 451 (Bankr. D. Mont. 1988) (allowing an individual to contribute nonexempt property, income from a patent held in the name of the owner, for purposes of new value exception). For further discussion of this question, see Raymond T. Nimmer, *Negotiated Bankruptcy Reorganization Plans: Absolute Priority and New Value Contributions*, 36 EMORY L.J. 1009, 1068–82 (1987); Ralph A. Peeples, *Staying In: Chapter 11, Close Corporations and the Absolute Priority Rule*, 63 AM. BANKR. L.J. 65 (1989).

6. Ed Flynn, *Bankruptcy by the Numbers: Who Is Filing Chapter 11?*, 18 AM. BANKR. INSTITUTE L.J. 30 (Feb. 1999).

7. Elizabeth Warren & Jay L. Westbrook, *Financial Characteristics of Businesses in Bankruptcy*, 73 AM. BANKR. L.J. 499, 536–39 (1999).

8. Administrative Office of the U.S. Courts, Table F-2: U.S. Bankruptcy Courts, Business and Nonbusiness Bankruptcy Cases Commenced, by Chapter of the Bankruptcy Code, During the Twelve Month Period Ended Dec. 31, available at [http://www.uscourts.gov/bnrpctystats/bankrupt\\_f2table\\_dec2005.xls](http://www.uscourts.gov/bnrpctystats/bankrupt_f2table_dec2005.xls) (last visited Oct. 2, 2006). Compare this to the 20,783 chapter 11 filings in calendar year 1990. Administrative Office of the United States Courts, Table F-2: U.S. Bankruptcy Courts, Business and Nonbusiness Bankruptcy Code Petitions Commenced, by Chapter of the Bankruptcy Code, During the Twelve Month Period Ended Dec. 31, 1990, available at [http://www.uscourts.gov/bnrpctystats/BK2002\\_1990Calendar.pdf](http://www.uscourts.gov/bnrpctystats/BK2002_1990Calendar.pdf) (last visited Oct. 2, 2006).

chapter 11. Compare this to the eighty public companies that filed during all of calendar year 2005.<sup>9</sup>

As rocky as the relationship is, it is about to get rockier. The Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) of 2005<sup>10</sup> contains a host of changes for individual debtors under chapter 11. Driven in large part by Congress's desire to impose a means test in chapter 7 individual cases,<sup>11</sup> and to have bankruptcy relief keyed to a lack of future income rather than to a lack of current assets,<sup>12</sup> these amendments work fundamental changes in the way chapter 11 treats individuals.

This article attempts to summarize BAPCPA's major changes for individuals in chapter 11. As a heuristic for this examination, the article suggests that Congress underplayed the scope and import of these changes by the manner in which the changes were incorporated into existing chapter 11. A better way to achieve the changes sought—and to avoid many policy and implementation errors—would have been to create a separate subchapter, modeling it on the way chapter 11 now treats railroad reorganizations<sup>13</sup> or the way chapter 7 treats stockbrokers.<sup>14</sup> Had that drafting choice been made, many of the drafting ambiguities and infelicities might have been caught. As it is, however, one is left with a motley sub rosa subchapter, which will generate wasted effort for lawyers and pain for debtors.

## II. THE CONCEPT OF A SUBCHAPTER

As the title implies, this article will attempt to show that BAPCPA created a new type of reorganization applicable only to individuals. One way to understand BAPCPA's provisions is to think of how the amendments might have been incorporated in contexts already understood and used. One such context is the "subchapter."

### A. Legislative Drafting and the "Subchapter"

As noted in the House Legislative Counsel's *Manual on Drafting Style*:

9. Mark G. Douglas, *The Year in Bankruptcy: 2005*, BUS. RESTRUCTURING REV., Jan.–Feb. 2006, at 1, available at <http://www.jonesday.com/pubs/pubs.aspx> (keyword search "business restructuring"; then follow "January/February 2006 Business Restructuring Review" hyperlink). The same report indicates that 2004 had only 92 public company filings. The height of public company filings was 2001, with over 250 such filings. Alan Deaton, *Large and Small Companies Exhibit Diverging Bankruptcy Trends*, BANK TRENDS, Jan. 2002, at 1 chart 1, available at <http://www.fdic.gov/bank/analytical/bank/bt0201.pdf>.

10. Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) of 2005, Pub. L. No. 109-8, 119 Stat. 23 (codified as amended in scattered sections of 11 U.S.C.).

11. See H.R. REP. NO. 109-31, at 2 (2005), reprinted in 2005 U.S.C.C.A.N. 88, 89.

12. See *id.* at 37 (examining the forward-looking formula used in means-testing), reprinted in 2005 U.S.C.C.A.N. 88, 110.

13. See 11 U.S.C. §§ 1161–1174 (2000).

14. See 11 U.S.C. §§ 761–767 (2000 & Supp. III 2003).

To be a good tool, style should be defined clearly. It should be one of the steady, predictable elements that attorneys use to reduce chaos to order, and not one of the fluctuating factors that contribute to the chaos. A good uniform style is one that gives clearly defined, steady, and predictable guidance for the structure and expression of legislation.<sup>15</sup>

A subchapter is a designated segment lower than a chapter, but higher than a division.<sup>16</sup> Although not mandatory, the style guidelines indicate a subchapter is appropriate when the basic structure or functions of the chapter are applicable, but variation is required because of common features or elements of a particular class of cases.

### B. Existing Subchapters

This subchapter concept is already found in chapter 11. For example, though many are not familiar with subchapter IV of chapter 11, that subchapter governs the reorganization of railroads.<sup>17</sup> This subchapter's roots are the longest of any statutory provision related to reorganizations.<sup>18</sup> Based on the 1933 addition of section 77 to the Bankruptcy Act of 1898,<sup>19</sup> this subchapter retains the basic chapter 11 reorganization structure, but alters it in key ways to adapt the form to the needs of railroads. Among these alterations is the elimination of creditor committees, accomplished simply by stating, in the first section of the subchapter, that § 1104<sup>20</sup> of the general chapter does not apply.<sup>21</sup> In addition, the subchapter eliminates the “best interests” test of § 1129(a)(7).<sup>22</sup>

The subchapter adds as well as subtracts. Section 1171<sup>23</sup> of the subchapter supplements § 507's<sup>24</sup> priority scheme with additional priorities, based on practice in the equity receiverships that preceded section 77's enactment.<sup>25</sup> Additional requirements for confirmation apply, including

15. THE OFFICE OF THE LEGISLATIVE COUNSEL, U.S. HOUSE OF REPRESENTATIVES, HOUSE LEGISLATIVE COUNSEL'S MANUAL ON DRAFTING STYLE 7 (1995).

16. LEGISLATIVE COMPUTER SYS., U.S. HOUSE OF REPRESENTATIVES, DRAFTING LEGISLATIVE DOCUMENTS 63, 218 (2004).

17. See 11 U.S.C. §§ 1161–1174.

18. See S. REP. NO. 95-989, at 9, 11 (1978) (noting that subchapter IV of chapter 11 was an extension of railroad reorganization guidelines passed in the 1930s that had remained “essentially unchanged” since 1935, whereas the other reorganization subchapters were based primarily on later legislation passed as part of bankruptcy reforms in 1938), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5795, 5797.

19. Section 77 provided for relief for railroad corporations. Act of Mar. 3, 1933, ch. 204, § 77, 47 Stat. 1467, 1474 (1933).

20. 11 U.S.C. § 1104 (2000).

21. *Id.* § 1161.

22. *Id.*

23. *Id.* § 1171.

24. *Id.* § 507.

25. *Id.* § 1171; see Nicholas L. Georgakopoulos, *Bankruptcy Law for Productivity*, 37 WAKE FOREST L. REV. 51, 67–68 (2002) (discussing equitable receiverships in railroad bankruptcies prior to 1933).

references to specific factors, a different test for feasibility,<sup>26</sup> and a specific direction to consider the public interest.<sup>27</sup>

Similar uses of the subchapter format appear in chapter 7. Subchapter III of that chapter has special provisions for stockbroker liquidations,<sup>28</sup> and subchapter IV provides separately for the liquidation of commodity brokers.<sup>29</sup> Subchapter V contains provisions for the liquidation of clearing banks.<sup>30</sup> In each of these subchapters, the basic function of chapter 7—liquidation—is preserved; but, special treatment is given to certain types of creditors,<sup>31</sup> or direction is given that other laws may control the ultimate liquidation.<sup>32</sup>

Under this logic, chapter 12, which covers family farmers and fishermen, could and probably should have been a subchapter of chapter 13. As with subchapter IV of chapter 11, which deals with railroad reorganizations, chapter 12 makes only a few variations from the main provisions of chapter 13, but these variations are significant. A chapter 12 plan, for example, may modify a claim secured by the debtor's principal residence.<sup>33</sup> The plan is not limited to five years.<sup>34</sup> Further, while there is the possibility of dispossessing the debtor as debtor in possession, there is also the possibility that a debtor may regain his position as estate fiduciary.<sup>35</sup> These changes do not run all in one direction; a chapter 13 discharge is broader than the chapter 12 discharge. For example, the chapter 12 debtor is subject to all of the nondischargeability claims found in § 523.<sup>36</sup>

The point here is that structure can aid function. Lawyers and judges can give better effect to a statute's purpose when the structure used within the statute clarifies that purpose. Especially with respect to subchapters, Congress can signal its intent that similar, but not identical, treatment is necessary for certain classes of debtors. When Congress declines to use such signaling devices, however, lawyers and judges are left to wonder whether unspecified consequences are intended, or unanticipated.

26. See 11 U.S.C. § 1173(a)(3) (2000).

27. *Id.* § 1173(a)(4).

28. See *id.* §§ 741–752.

29. See *id.* §§ 761–766 (2000 & Supp. III 2003).

30. See *id.* §§ 781–784 (2000).

31. Holders of certain types of financial contracts in stockbroker liquidations, for example, receive preferential treatment not found in other sections of the Bankruptcy Code. See *id.* § 741.

32. The Commodity Futures Trading Commission must get notice of all actions, and may appear and be heard, for example, in commodity broker liquidations. *Id.* § 762.

33. Compare *id.* § 1222(b), with *id.* § 1322(b)(2).

34. *Id.* § 1222(b)(9).

35. *Id.* § 1204.

36. Compare *id.* § 1228(a), with *id.* § 1328(a).

## III. THE CHANGES

A separate segmentation of chapter 11 for individuals would help only if the changes made were sufficiently significant to justify the separate treatment. The claim that the new individual reorganization provisions effectively constitute such a subchapter—albeit a sub rosa one—ultimately turns on the effect of Congress’s changes. After first looking at the origins of these provisions, this article examines the amendments in some detail. This article then compares the overall treatment effected by these changes to the treatment a chapter 13 case would provide.

*A. Origins and Legislative History—How Did We Get Here?*

The Senate Judiciary Committee first discussed special provisions for individual chapter 11 debtors in 1999. At that time, in a markup to the then-current bankruptcy reform bill, section 321 was added to read as follows:

SEC. 321. TREATMENT OF CERTAIN EARNINGS OF AN INDIVIDUAL DEBTOR WHO FILES A VOLUNTARY CASE UNDER CHAPTER 11.

Section 541(a)(6) of title 11, United States Code, is amended by inserting “(other than an individual debtor who, in accordance with section 301, files a petition to commence a voluntary case under chapter 11)” after “individual debtor”.<sup>37</sup>

The section-by-section portion of the Senate Report accompanying the bill as ultimately reported simply stated that “[t]his section provides that post-petition income will become property of the bankruptcy estate in individual consumer cases under chapter 11.”<sup>38</sup>

The amendment did not go without comment. Senators Leahy, Kennedy, Feingold, and Schumer added the following in their Minority Views section of the Senate Report:

At the Judiciary Committee markup, Senator Grassley successfully introduced an amendment to include postpetition earnings for individual chapter 11 debtors as “property of the estate.” This so-called “super-rich” amendment, which would have been considered rather controversial had it been vetted among the bankruptcy community, is undoubtedly a significant change to bankruptcy law but is not the direct or most effective method of controlling higher income debtors and in any event is not responsive to our concerns regarding the disparate effects of the bill.<sup>39</sup>

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37. S. 625, 106th Cong. § 321 (as reported by S. Comm. on the Judiciary, May 11, 1999). The provision was not in the bill as introduced in the Senate. S. 625, 106th Cong. (as introduced in Senate, Mar. 16, 1999).

38. S. REP. NO. 106-49, at 33 (1999). The report indicates that the amendment was offered by Senator Grassley of Iowa, and that it passed by a vote of 12-5, with Senators Leahy, Kennedy, Biden, Kohl and Feingold voting nay. *Id.* at 17.

39. *Id.* at 114 n.43.

At the same time the Senate debated Senate Bill 625, the House considered a companion bill, House Bill 833.<sup>40</sup> House Bill 833 passed the House on May 5, 1999<sup>41</sup> and was received in the Senate soon thereafter. The bill as received did not have any provisions for individual chapter 11 debtors.<sup>42</sup> During Senate consideration, however, the Grassley amendment from Senate Bill 625 was inserted and, more importantly, expanded.<sup>43</sup> As a result, when the Senate ultimately passed House Bill 833, section 321 of the bill not only contained a new amendment to § 1115 regarding personal service income,<sup>44</sup> but also contained additional amendments that applied only to individuals.<sup>45</sup> The list is short, but significant:

Section 1123 of the Code was amended to require an individual's devotion of her postpetition service and other income as necessary to implement the plan;<sup>46</sup>

A "projected disposable income" test was added to § 1129(a) as new paragraph (14);<sup>47</sup>

An individual's discharge was delayed until the completion of plan payments;<sup>48</sup> and

A new section on plan modification was inserted.<sup>49</sup>

Congress passed the substance of House Bill 833 after the 2000 elections.<sup>50</sup> However, President Clinton refused to sign the bill, and it was thus "pocket-vetoed."<sup>51</sup> As a result, bankruptcy reform had to be reintroduced in the 107th Congress.

Reintroduction came soon: On January 31, 2001, House Bill 333 was introduced in the House.<sup>52</sup> This version contained the expanded version of Senator Grassley's amendment, which had passed both the House and the Senate during the previous session.<sup>53</sup> After some minor changes to

40. H.R. 833, 106th Cong. (as introduced in House, Feb. 24, 1999).

41. The bill passed on May 5, 1999 by a 313-108 vote. 145 CONG. REC. H2771 (daily ed. May 5, 1999).

42. H.R. 833 (as received in Senate, May 12, 1999).

43. The bill as passed by the Senate was nominally H.R. 833. Earlier, however, the Senate had struck the text of H.R. 833, and inserted the text of S. 625 in its place. 146 CONG. REC. S255 (daily ed. Feb. 2, 2000). The version inserted contained the Grassley amendment as expanded. See 146 CONG. REC. S407-08 (daily ed. Feb. 7, 2000).

44. H.R. 833 § 321(a)(1) (as passed by Senate, Feb. 2, 2000).

45. *Id.* § 321(b)-(e).

46. *Id.* § 321(b)(3).

47. *Id.* § 321(c)(1).

48. *Id.* § 321(d)(2).

49. *Id.* § 321(e).

50. H.R. 833 (as passed by Senate, Feb. 2, 2000).

51. For a detailed history, see Susan Jensen, *A Legislative History of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 79 AM. BANKR. L.J. 485, 533-39 (2005).

52. H.R. 333, 107th Cong. (as introduced in House, Jan. 31, 2001).

53. See S. REP. NO. 106-49, at 17 (1999). Compare H.R. 333, with H.R. 833 (as passed by Senate, Feb. 2, 2000).

the overall bill,<sup>54</sup> the House issued a report<sup>55</sup> and promptly passed the bill.<sup>56</sup> The report contains the first extended discussion of the expansion of Senator Grassley's amendment.<sup>57</sup>

House Bill 333 ultimately went to conference in 2001.<sup>58</sup> At conference, the House conferees agreed to the Senate's text, and issued a conference report.<sup>59</sup> The report contained a description of the expanded amendment that was almost word-for-word the text used in the earlier House Report.<sup>60</sup> This treatment, though somewhat extensive, is purely descriptive.<sup>61</sup> There is no discussion of the policy behind, or purposes of, these changes. This silence was a hallmark of all successive versions of the bill, none of which altered the text of section 321.

Thus, although not entirely free from doubt, it appears that the individual chapter 11 provisions were inserted as adjuncts to means testing to ensure no easy escape from chapter 7. As characterized by the Senate minority, who opposed the provisions when they were first offered, the provisions were intended for the "super-rich."<sup>62</sup> As enacted, however, these provisions do not just affect the "super-rich," as this article will now demonstrate through a detailed analysis.

### B. *The Changes in Detail*

Section 321 of BAPCPA carried forward several changes, discussed since 1999, that apply to individual chapter 11 debtors. The changes start with the original provision, which altered the nature of property of the estate.

#### 1. *Postpetition Earnings from Services Are Property of the Estate— § 1115*

Section 321(a) of BAPCPA added § 1115 to the Bankruptcy Code.<sup>63</sup> This section defines property of the estate for each individual chapter 11 case. Section 1115's text is based on and is almost identical to existing § 1306,<sup>64</sup> which is applicable only in chapter 13 cases. Both sections sup-

54. The bill was amended in committee to add what is now § 1115(b), which allows the debtor to remain in possession of postpetition service income. See 147 CONG. REC. H548 (daily ed. Mar. 1, 2001).

55. H.R. REP. NO. 107-3 (2001).

56. 147 CONG. REC. H600-01 (daily ed. Mar. 1, 2001).

57. H.R. REP. NO. 107-3, at 53-54.

58. See Jensen, *supra* note 51, at 548-49.

59. H.R. REP. NO. 107-617 (2002) (Conf. Rep.); see also Jensen, *supra* note 51, at 549 n.404.

60. Compare H.R. REP. NO. 107-617, at 220-21, with H.R. REP. NO. 107-3, at 53-54.

61. H.R. REP. NO. 107-617, at 220-21.

62. See S. REP. NO. 106-49, at 114 n.43 (1999).

63. BAPCPA, Pub. L. No. 109-8, § 321(a)(1), 119 Stat. 23, 94-95 (2005) (codified at 11 U.S.C. § 1115).

64. Compare 11 U.S.C. § 1306 (2000), with BAPCPA § 321(a)(1) (codified at 11 U.S.C. § 1115).

plement the estate with property that is excluded from the estate in an individual's chapter 7 case: postpetition earnings from services.<sup>65</sup>

This expansion of property of the estate includes income from services performed postpetition,<sup>66</sup> and ensures that this additional property, which usually is necessary to fund or otherwise implement a plan of reorganization,<sup>67</sup> is protected by the automatic stay.<sup>68</sup> This is even the case with respect to claimants who could pursue such property in a chapter 7 case, such as those holding postpetition claims.<sup>69</sup>

This inclusion of postpetition service income, however, did not change other provisions in title 11 that rely on § 541's definition of estate property, such as the "best-interests-of-creditors" test found in chapter 11.<sup>70</sup> There is also no requirement that property coming into the estate due only to the operation of § 1115(a) be listed in the schedules. Obviously, such a requirement would be unworkable, since the debtor's schedules would have to be amended to reflect each paycheck or acquisition of property, as well as every expenditure.

While § 1115(a) adds this additional property to the estate, § 1115(b) confirms the debtor's presumptive right to remain in possession of that property, as well as all other property of the estate.<sup>71</sup> As in pre-BAPCPA chapter 13 cases, the right to remain in possession of this property of the estate is a major advantage for individual chapter 11 debtors. In a chapter 7 case, these debtors would have to turn over non-exempt property to the trustee.<sup>72</sup>

## 2. *Use of § 1115 Property to Fund a Plan—§ 1123(a)(8)*

To ensure that a debtor devotes § 1115 income to plan implementation and creditor claims, section 321(b) of BAPCPA added § 1123(a)(8). This provision requires the individual chapter 11 debtor's plan to provide

65. 11 U.S.C. § 1306(a)(2); BAPCPA § 321(a)(1) (codified in part at 11 U.S.C. § 1115(a)(2)).

66. BAPCPA § 321(a)(1) (codified in part at 11 U.S.C. § 1115(a)(2)).

67. *Id.* § 321(b)(3), 119 Stat. at 95 (codified at 11 U.S.C. § 1123(a)(8)) (requiring an individual chapter 11 debtor to include such income from postpetition services as is necessary to implement the plan).

68. The chapter 13 cases construing cognate language in § 1306 establish this principle. *See, e.g.*, *Security Bank of Marshalltown, Iowa v. Neiman*, 1 F.3d 687 (8th Cir. 1993) (noting that chapter 13 estate continues to exist after confirmation of plan, so expenses to protect estate property were administrative expenses); *Carver v. Carver*, 954 F.2d 1573 (11th Cir. 1992) (holding that debtor's wages were property of estate and therefore action to collect alimony from those wages was not a § 362(b)(2) exception to automatic stay); *Annese v. Kolenda (In re Kolenda)*, 212 B.R. 851 (W.D. Mich. 1997) (providing that property acquired postpetition remains in estate after confirmation and is protected by automatic stay); *Clark v. United States (In re Clark)*, 207 B.R. 559 (Bankr. S.D. Ohio 1997) (holding that all property of debtor was property of estate protected by automatic stay after confirmation of plan when order confirming the plan so provided).

69. *See* 11 U.S.C. § 362(a)(3)–(4) (2000) (protecting property of the estate); *Carver*, 954 F.2d at 1577 (postpetition income protected from support enforcement).

70. *See* 11 U.S.C. § 1129(a)(7) (2000).

71. *See* BAPCPA § 321(a)(1) (codified at 11 U.S.C. § 1115); *see also* 11 U.S.C. § 1107 (2000).

72. 11 U.S.C. § 521(a)(4) (2000).

“all or such portion of earnings from personal services . . . or other future income . . . as is necessary for the execution of the plan.”<sup>73</sup> This provision apparently ensures that an individual debtor will devote an amount equal to his or her personal service income to the plan. However, for reasons explored later, the provision may not be sufficient to achieve that task.

3. *Disposable Income Requirement Imported from Chapter 13—  
§ 1129(a)(15)*

Section 1129(a)(15), added by section 321(c) of BAPCPA, requires individual chapter 11 debtors to either pay all allowed unsecured claims in full,<sup>74</sup> or devote an amount equal to five years’ worth of the debtor’s projected disposable income to property to be distributed under the plan.<sup>75</sup> As with the best interest of creditors test found in § 1129(a)(7), standing to object on this ground is not class based; it is irrelevant that the plan proponent obtained the consent of the class of unsecured creditors so long as there is one objecting unsecured creditor.

The concept of “projected disposable income” and the amounts of such disposable income that must be devoted to the implementation of the plan are central to the application of this provision. “Disposable income” is a concept borrowed from chapter 13.<sup>76</sup> Indeed, § 1129(a)(15) refers to § 1325(b)(2) for a definition of the concept.<sup>77</sup>

Under § 1129(a)(15), the plan must distribute property equal in value to the debtor’s projected disposable income over the five-year period beginning on the date that the first payment is due under the plan.<sup>78</sup> The confirmation requirement thus specifies the amount of all payments.

Although based on chapter 13 practice, this confirmation requirement differs in several respects. First, it differs as to time. Under chapter 13, a debtor’s plan must extend for three years (in some cases five years) unless the plan provides for earlier payment of all unsecured claims in full.<sup>79</sup> Section 1129(a)(15) does not specify a minimum period, but does specify that the value of the property to be distributed under the plan must not be “less than the projected disposable income of the debtor . . . to be received during the 5-year period” beginning with the start of plan payments.<sup>80</sup> Thus, if property from any other source—such as loans or gifts, or from exempt property—is used to supplement the

73. BAPCPA § 321(b)(3), 119 Stat. at 95 (codified at 11 U.S.C. § 1123(a)(8)).

74. *Id.* § 321(c)(1) (codified in part at 11 U.S.C. § 1129(a)(15)(A)).

75. *Id.* (codified in part at 11 U.S.C. § 1129(a)(15)(B)).

76. *See* 11 U.S.C. § 1325(b)(2) (2000).

77. Section 1129(a)(15)(B) specifically provides that “disposable income of the debtor” is used “as defined in section 1325(b)(2).” BAPCPA § 321(c)(1) (codified in part at 11 U.S.C. 1129(a)(15)(B)).

78. *Id.*

79. *See id.* § 318(3), 119 Stat. at 93–94 (codified at 11 U.S.C. § 1325(b)(4)).

80. *Id.* § 321(c)(1) (codified in part at 11 U.S.C. § 1129(a)(15)(B)).

payments to unsecured creditors, the plan may be shorter than five years.<sup>81</sup>

Chapter 13 also limits the maximum plan length to five years.<sup>82</sup> Section 1129(a)(15) explicitly permits longer plans by requiring that a minimum amount of property to be devoted to the plan, and by linking that amount to the debtor's projected disposable income for the five years following confirmation or "the period for which the plan provides payments, whichever is longer."<sup>83</sup>

Finally, chapter 13 requires payments to begin within thirty days of commencement of the case, regardless of whether the plan is confirmed.<sup>84</sup> Chapter 13 then measures the plan period from the first scheduled payment to unsecured creditors.<sup>85</sup> Under § 1129(a)(15)(B), however, the minimum five-year period begins on the "date that the first payment is due under the plan,"<sup>86</sup> which usually will be after confirmation.

4. *Delayed Entry of the Discharge Imported from Chapter 13—  
§ 1141(d)(5)*

Section 321(d) of BAPCPA changed the date on which an individual chapter 11 debtor receives his or her discharge.<sup>87</sup> Before BAPCPA, all debtors received their discharge when their plan was confirmed, regardless of whether all (or any) plan payments were made.<sup>88</sup> Section 321(d) added § 1141(d)(5), which changes the discharge date, to chapter 11.<sup>89</sup> For cases covered by BAPCPA, the discharge is now issued "on completion of all payments under the plan."<sup>90</sup>

5. *Changes to Modification of Plans—Incorporating § 1329(a) (sort of)  
into § 1127(e)*

The delay of discharge for individuals makes the terms of modification more important; if assumptions made at confirmation prove erroneous, modification will be necessary in order to issue a discharge. Section

81. This view is supported by 11 U.S.C.A. § 1123(a)(8) (West Supp. 2006), which requires an individual debtor's plan to include all postpetition earnings from services to the extent necessary to implement the plan, but does not specify any minimum period.

82. 11 U.S.C. § 1322(d) (2000); *see also* BAPCPA § 318(3) (codified in part at 11 U.S.C. § 1325(b)(4)(A)(i)–(ii)).

83. BAPCPA § 321(c)(1) (codified in part at 11 U.S.C. § 1129(a)(15)(B)).

84. *Id.* § 309(c)(2), 119 Stat. at 83–84 (codified in part at 11 U.S.C. § 1326(a)(1)). The plan must be filed within 15 days of the commencement of the case. FED. R. BANKR. P. 3015(b).

85. 11 U.S.C.A. § 1325(b)(1)(B) (West Supp. 2006).

86. BAPCPA § 321(c)(1) (codified in part at 11 U.S.C. § 1129(a)(15)(B)).

87. *See id.* § 321(d), 119 Stat. at 95–96 (codified at 11 U.S.C. § 1141(d)).

88. 11 U.S.C. § 1141(d) (2000), *amended by* BAPCPA, Pub. L. No. 109-8, § 321(d), 119 Stat. 23, 95–96 (2005).

89. BAPCPA § 321(d).

90. *Id.* § 321(d)(2) (codified in part at 11 U.S.C. § 1141(d)(5)(A)). This is a provision that permits an earlier discharge in certain circumstances. *See* discussion *infra* Part IV.B.2.c.

321(e) of BAPCPA addressed this issue by adding § 1127(e) to the Code.<sup>91</sup> This new section allows individual debtors (along with trustees and unsecured creditors) to modify the plan to increase or reduce payments, as well as repayment periods, under the plan, so long as other confirmation requirements are met.<sup>92</sup>

6. *Additional Confirmation Requirements—11 U.S.C. § 1129(a)(14) and BAPCPA Section 1228(b)*

In addition to the changes made by section 321 of BAPCPA, other significant changes were made to the confirmation requirements imposed on individual debtors. Chapter 11 debtors will now have to ensure that their postpetition domestic support obligations<sup>93</sup> are current as of confirmation.<sup>94</sup> In addition, in an uncodified portion of BAPCPA, Congress required individual debtors to prove that they have provided all tax information that was requested preconfirmation.<sup>95</sup>

C. *Chapter 11 and Chapter 13 Compared*

There is a tendency to look at the changes to chapter 11 and assume that the only difference for individuals between chapter 13 and chapter 11 is the debt limitations. This might lead one to conclude that the new chapter 11 provisions are really a subspecies of chapter 13. However, that would be problematic and likely wrong. There are some significant differences between chapter 11 and chapter 13, as illustrated by the following:

- If the debtor could file under either chapter 11 or chapter 13, and is engaged in business, the small business provisions of chapter 11 will likely apply if the debtor files under chapter 11, but will not if the debtor files under chapter 13.<sup>96</sup>
- Chapter 11 has a more expensive filing fee: \$1039 versus \$274.<sup>97</sup>
- There is no automatic co-debtor stay in chapter 11.<sup>98</sup>
- Chapter 11 does not contain a statutory authorization for separate classification of debts for which the debtor is co-liable.<sup>99</sup>

91. BAPCPA § 321(e), 119 Stat. at 96 (codified in part at 11 U.S.C. § 1127(e)).

92. *Id.*

93. *See id.* § 211(2), 119 Stat. at 50–51 (codified at 11 U.S.C. § 101(14A)).

94. *See id.* § 213(1), 119 Stat. at 52 (codified at 11 U.S.C. § 1129(a)(14)).

95. *Id.* § 1228(b), 119 Stat. at 200.

96. *See id.* § 432(a), 119 Stat. at 110 (codified in part at 11 U.S.C. § 101(51C)) (stating that only cases under chapter 11 are eligible to be “small business case[s]”).

97. Administrative Office of the U.S. Courts, Bankruptcy Filing Fees—Effective April 9, 2006, <http://www.uscourts.gov/bankruptcycourts/fees.html> (last visited Oct. 2, 2006); *see also* 28 U.S.C.A. § 1930(a) (West Supp. 2006).

98. *Cf.* 11 U.S.C. § 1301 (2000).

- The valuation standard contained in § 506(a)(2), requiring retail valuation, does not apply in chapter 11.
- Disposable income under chapter 11 need only be part of the “property to be distributed under the plan,”<sup>100</sup> which presumably means some of it may be devoted to secured creditors and post-petition administrative claimants; in chapter 13, disposable income must be distributed for the benefit of *unsecured* creditors.<sup>101</sup>
- The anticramdown provision<sup>102</sup> added by section 306(b) of BAPCPA to § 1325(a), which prohibits bifurcation of certain purchase money secured claims if the secured creditor is under-secured, does not apply in chapter 11.
- The chapter 11 disposable income test found in § 1129(a)(15) may not incorporate the IRS expense limits applicable to some chapter 13 debtors. Section 1129(a)(15) refers only to § 1325(b)(2), which calculates disposable income with reference to the debtor’s actual expenses, but not to § 1325(b)(3), which incorporates the IRS collection standards set out in § 707(b)(2) for debtors whose income is above the applicable median income for their state.<sup>103</sup>
- Creditors must be solicited and get to vote on a chapter 11 plan,<sup>104</sup> there is no creditor voting in chapter 13.
- The minimum plan length is calculated differently in chapter 13 and chapter 11. For some cases, chapter 13 plans can be less than five years;<sup>105</sup> chapter 11 may require that the debtor devote at least five years’ worth of disposable income to his plan.<sup>106</sup>
- The maximum plan length also differs in chapter 13 and chapter 11. In chapter 13, no plan may last longer than five years,<sup>107</sup> chapter 11 plans may extend over a longer period of time.<sup>108</sup>
- Payments under chapter 11 plans do not usually commence until after confirmation, which may be significantly later than the fil-

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99. *Cf. id.* § 1322(b)(1) (extending such classification only to consumer debts).

100. BAPCPA § 321(b)(3), 119 Stat. at 95 (codified at 11 U.S.C. § 1123(a)(8)).

101. *Id.* § 102(h)(1), 119 Stat. at 33 (codified at 11 U.S.C. § 1325(b)(1)(B)).

102. *Id.* § 306(b), 119 Stat. at 80 (codified at 11 U.S.C. § 1325(a)).

103. *See infra* Part IV.B.2.a.

104. *See* 11 U.S.C. § 1129(a)(8) (2000); 11 U.S.C.A. § 1125 (West 2004 & Supp. 2006).

105. *See* BAPCPA § 318(2), (4), 119 Stat. at 93–94 (amending 11 U.S.C. §§ 1325(b)(1)(B), 1329(c)); *id.* § 318(3) (codified at 11 U.S.C. § 1325(b)(4)).

106. *Id.* § 321(c)(1), 119 Stat. at 95 (codified in part at 11 U.S.C. § 1129(a)(15)(B)).

107. *Id.* § 318(3), 119 Stat. at 93 (codified at 11 U.S.C. § 1325(b)(4)).

108. *Id.* § 321(c)(1), 119 Stat. at 95 (codified in part at 11 U.S.C. § 1129(a)(15)(B)).

ing date;<sup>109</sup> chapter 13 plans must be filed within fifteen days of the filing date,<sup>110</sup> and chapter 13 debtors begin paying the designated plan amounts before plan confirmation.<sup>111</sup>

- A chapter 13 debtor may discharge certain marital property settlements to the extent that the settlements are covered by § 523(a)(15), and may discharge some forms of willful and malicious injury that do not involve personal injury or death.<sup>112</sup>
- A chapter 11 discharge for inability to complete a plan appears to be somewhat easier to obtain than a chapter 13 hardship discharge.<sup>113</sup>
- Chapter 13 debtors must complete a course in financial education as a condition to receiving their discharge;<sup>114</sup> no such education requirement is applicable to chapter 11 debtors.

#### IV. THE EFFECTS OF THE CHANGES: WOULD A SUBCHAPTER HAVE HELPED?

As section 321 of BAPCPA provided for only five relatively small changes to chapter 11 for individuals, the claim that individuals deserve their own subchapter may seem to be much ado about nothing.<sup>115</sup> However, as the effects of these changes ripple through chapter 11, they cause significant changes in the way cases can and should be administered. These effects may be divided into three areas: administration before confirmation, confirmation, and postconfirmation.

##### *A. Issues During Administration, but Before Confirmation*

Critics complained about what happens in the gap between filing the case and confirming a plan, the so-called administrative period.<sup>116</sup>

109. See *In re Haiflich*, 63 B.R. 314 (Bankr. N.D. Ind. 1986) (requiring a filing amendment due to interest accrued between the September 1984 filing and the November 1985 confirmation).

110. FED. R. BANKR. P. 3015(b).

111. 11 U.S.C. § 1326(a)(2) (2000).

112. See 11 U.S.C.A. § 1328(a)(2), (4) (West Supp. 2006).

113. Compare 11 U.S.C. § 1328(b)(1) (2000) (“[T]he court may grant a discharge to a debtor that has not completed payments under the plan only if the debtor’s failure to complete payments is due to circumstances for which the debtor should not justly be held accountable . . .”), with 11 U.S.C.A. § 1141(d)(5)(B)(ii) (West Supp. 2006) (allowing discharge without completion of the plan if modification of the plan is not practicable).

114. 11 U.S.C.A. § 1328(g)(1) (West Supp. 2006).

115. See, e.g., Leif M. Clark, *Chapter 11: Does One Size Fit All?*, 4 AM. BANKR. INST. L. REV. 167, 188–89 (1996) (concluding that one form of relief for all entities is appropriate if judges who administer the system are adequately trained).

116. As Judge Edith Jones stated, “Chapter 11 is more an intensive-care ward (or a mortuary) than a healing potion for sick businesses.” Edith H. Jones, *Chapter 11: A Death Penalty for Debtor and Creditor Interests*, 77 CORNELL L. REV. 1088, 1089 (1992); see also *In re Maxim Indus., Inc.*, 22 B.R. 611, 613 (Bankr. D. Mass. 1982) (“Bankruptcy is perceived as a haven for wistfulness and the

Congress addressed some of those concerns in BAPCPA by limiting the debtor's exclusivity<sup>117</sup> and by generally encouraging judges to be active in the administration and swift progress of chapter 11 cases.<sup>118</sup> But BAPCPA's changes may have exacerbated these problems and caused others.

### 1. *Personal Living Expenses*

Under chapter 13, debtors must file their plan within fifteen days of commencing the case<sup>119</sup> and begin payments under the proposed plan before confirmation.<sup>120</sup> By contrast, chapter 11 does not require a plan to be filed at all—it simply provides for conversion or dismissal if a confirmable plan is not filed within a reasonable time.<sup>121</sup> As a result, in chapter 11 cases there often will be a significant time gap between the commencement of the case and the confirmation of a plan.<sup>122</sup>

But what about paying expenses necessary to get the debtor to confirmation? In particular, what about a debtor's personal living expenses? Recall that new § 1115 brings into the estate all postpetition service income, but thereafter provides no real guidance as to how that income may be spent preconfirmation. Ideally, income could just accumulate, but few debtors could afford to work for a wage and not pay any bills. If, however, those expenses are "actual, necessary costs and expenses of preserving the estate," such as maintenance payments on a principal asset, then they should qualify as administrative expenses,<sup>123</sup> and may be paid, presumably in the ordinary course.

What about expenses that may not be necessary to preserve the estate, but which were part of the debtor's prepetition expenses? Many personal expenses of everyday folk are not "necessary" to preserve the "estate." Examples include payments on a country club membership, a

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optimist's Valhalla where the atmosphere is conducive to fantasy and miraculous dreams of the phoenix rising from the ruins. Unfortunately, this Court is not held during the full moon, and while the rays of sunshine sometimes bring the warming rays of the sun, they more often also bring the bright light that makes transparent and evaporates the elaborate financial fantasies constructed of nothing more than the gossamer wings and of sophisticated tax legerdemain.").

117. BAPCPA, Pub. L. No. 109-8, § 411(2), 119 Stat. at 23, 106-07 (codified at 11 U.S.C. § 1121(d)(2) (limiting extensions of the exclusivity periods to 18 and 20 months); *id.* § 437, 119 Stat. at 113 (codified at 11 U.S.C. § 1121(e)) (requiring small business debtors, with limited exceptions, to file a plan and disclosure statement within 300 days of the date of the order for relief).

118. *See, e.g., id.* § 440, 119 Stat. at 114 (codified at 11 U.S.C. § 105(d)(1)).

119. FED. R. BANKR. P. 3015(b).

120. BAPCPA § 309(c)(2), 119 Stat. at 83 (codified in part at 11 U.S.C. § 1326(a)(1)) (requiring plan payments to commence at the earlier of 30 days after filing the plan or after the order for relief).

121. *Id.* § 442(a), 119 Stat. at 116 (codified in part at 11 U.S.C. § 1112(b)(4)(J)) (listing failure to file a plan within the time fixed by the court or Code as a ground for conversion or dismissal).

122. The notable exception would be prepackaged chapter 11 plans, authorized in part by section 402 of BAPCPA, 119 Stat. at 104 (codified at 11 U.S.C. § 341(e)), and section 408 of BAPCPA, 119 Stat. at 106 (codified at 11 U.S.C. § 1125(g)).

123. 11 U.S.C. § 503(b)(1)(A) (2000). Taxes also will qualify as administrative expenses that may be paid in the ordinary course. *Id.* § 503(b)(1)(B).

vacation, or even something as prosaic as the daily hit at Starbucks.<sup>124</sup> There appears to be no statutory provision authorizing these types of payments.

These ordinary but not necessary expenses are handled in chapter 13 by § 1325, which allows the 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.”<sup>125</sup> Although new § 1129(a)(15) cross-references § 1325(b), § 1129(a)(15) applies only to plan confirmation. Thus § 1129 applies only to payments to be distributed under the confirmed plan, which typically will be after confirmation.<sup>126</sup> Indeed, if these expenses do not qualify as administrative expenses payable in full on confirmation, it appears there may be no authorization for them. This means that, at the extreme, the expenses could be recovered under § 549.<sup>127</sup>

## 2. Professional Expenses

Payment to the debtor’s professional agents also presents a concern with respect to the changes wrought by § 1115. It is quite likely that the debtor’s lawyer will have significant postfiling bills and will need to know (and will deserve to know) how to be paid. This is not a problem in chapter 13, as there is explicit recognition of the ability of a professional for a chapter 13 debtor to receive reasonable compensation “for representing the interests of the debtor.”<sup>128</sup>

No such provision exists for lawyers representing individual chapter 11 debtors. The chapter 11 debtor’s lawyer would thus presumably be covered by *Lamie v. United States Trustee*,<sup>129</sup> and could not receive compensation from the estate.<sup>130</sup> The zone of noncompensation would appear to cover advice as to exemptions, or advice on plan structuring if the plan allocates some of the estate for the debtor postconfirmation, as expenses in these areas would benefit the debtor, and not the bankruptcy estate. Further, efforts to obtain sufficient funds prepetition to cover an-

124. At the extreme end, expenses for others that are not legally required, such as support for an elderly parent, are not strictly necessary to preserve the estate—but few outside of bankruptcy would quibble that a debtor should make such payments, and that the debtor should keep making them after filing.

125. BAPCPA § 102(h), 119 Stat. at 33–34 (codified in part at 11 U.S.C. § 1325(b)(2)(A)(i)).

126. In addition, § 1129(a)(15) will not apply if no creditor objects. 11 U.S.C.A. § 1129(a)(15) (West Supp. 2006).

127. This might have a perverse effect on the best interests test and on preplan disclosure; some courts require the disclosure statement to outline the effect of avoidance power recoveries from insiders. See, e.g., *In re Sierra-Cal*, 210 B.R. 168, 176–77 (Bankr. E.D. Cal. 1997).

128. 11 U.S.C. § 330(a)(4)(B) (2000). This also applies to lawyers for chapter 12 debtors. *Id.*

129. *Lamie v. United States Tr.*, 540 U.S. 526 (2004).

130. *Id.* at 541–42 (denying a chapter 7 debtor’s lawyer compensation from the estate).

anticipated services may create causes of action under the avoiding actions, and thus raise questions of disinterestedness.<sup>131</sup>

### 3. *Taxes and Support Payments*

After BAPCPA, keeping current on taxes and support payments is critical. An individual's failure to pay taxes or timely file tax returns may constitute cause for dismissal,<sup>132</sup> as may the failure to pay any domestic support obligation that comes due after the filing.<sup>133</sup> In addition, failure to keep these expenses current may preclude confirmation because both taxes and support payments are priority claims,<sup>134</sup> subject to a separate confirmation provision.<sup>135</sup>

#### B. *Confirmation Issues*

If the debtor is able to stay in chapter 11, and proposes a plan, there are several impediments, or uncertainties, regarding confirmation. These problems are dealt with as part of all confirmations under the heading of "all" confirmations, and as part of nonconsensual confirmations.

#### 1. *All Confirmations*

BAPCPA added several paragraphs to § 1129(a), which deals with consensual confirmation; that is, confirmation accompanied by the assent of all classes of claims.

##### a. *Best Interests Test and Service-Related Income*

A central requirement of confirmation is the so-called best interests test; that is, the plan proponent must demonstrate that each and every nonconsenting, impaired creditor will receive more in reorganization than in liquidation.<sup>136</sup> One nonobvious fallout of the BAPCPA amendments is that the intersection of § 1115 and § 348 may render the "best interests" test immaterial in any case in which the debtor has significant postpetition income.

131. See, e.g., *In re Equip. Servs., Inc.*, 290 F.3d 739 (4th Cir. 2002); *In re CK Liquidation Corp.*, 321 B.R. 10 (Bankr. D. Mass. 2005); *In re Channel Master Holdings, Inc.*, 309 B.R. 855 (Bankr. D. Del. 2004); see also 3 COLLIER ON BANKRUPTCY ¶ 327.04[2][b] (15th rev. ed. 2006) (explaining that lawyers must "not hold or represent an interest adverse to the estate").

132. BAPCPA, Pub. L. No. 109-8, § 442(a), 119 Stat. 23, 115-16 (2005) (codified in part at 11 U.S.C. § 1112(b)(4)(I)).

133. *Id.* (codified in part at 11 U.S.C. § 1112(b)(4)(P)).

134. See 11 U.S.C.A. § 507(a) (West Supp. 2006).

135. *Id.* § 507(a)(1) (domestic support obligations); *id.* § 507(a)(8) (taxes); *id.* § 1129(a)(9)(A) (postpetition taxes); *id.* § 1129(a)(14) (postpetition domestic support obligations).

136. 11 U.S.C. § 1129(a)(7) (2000).

This odd result is dictated by the fact that, were a chapter 11 individual debtor to convert to chapter 7, § 1115 would no longer apply.<sup>137</sup> All the postpetition income from services brought into the estate from and after filing would revert back to the debtor (and the debtor might even have a claim for a rebate) via the operation of § 348, which tells courts that, in converted cases, the estate is deemed to have been created as of the filing date.<sup>138</sup> This would have the effect of recharacterizing all service income brought into the estate under § 1115 as property of the debtor under § 541(a)(6).

This was generally thought to be the result under chapter 13 as originally enacted.<sup>139</sup> Congress, however, thought clarity was of sufficient importance to amend § 348 in 1994 to add subsection (f), which essentially clarifies that there is a reversion of postpetition service income to the debtor.<sup>140</sup> BAPCPA did not modify § 348 to extend the same treatment to conversions from chapter 11 to chapter 7, so there remains some uncertainty over exactly how to calculate the value of the hypothetical chapter 7 estate. For this reason, the pre-BAPCPA cases examining the scope of § 541(a)(6) in individual chapter 11 cases will retain vitality.<sup>141</sup>

#### b. Treatment of Privileged Creditors

Individuals also have to treat certain classes of creditors differently. Postpetition domestic support obligations must be current to confirm a chapter 11 plan.<sup>142</sup> An uncodified provision of BAPCPA requires all “requested tax documents,” presumably all tax returns at a minimum, to be filed.<sup>143</sup> A minor concern exists in that BAPCPA did not modify § 1122 to accommodate these necessary changes; chapter 13, which borrows the classification standard from chapter 11, specifically allows the debtor to separately class favored classes of co-debtors.<sup>144</sup>

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137. One might quibble that the debtor would have to meet the means test of § 707(b)(2) in order to convert, but that conclusion is not certain; § 707(b)(1) would seem to extend the means test to “a case filed by an individual debtor *under this chapter*.” 11 U.S.C.A. § 707(b)(1) (West Supp. 2006) (emphasis added).

138. 11 U.S.C. § 348(a) (2000).

139. See 4 KEITH M. LUNDIN, CHAPTER 13 BANKRUPTCY § 315.1, at 315-2 to 315-10 (3d ed. 2000 & Supp. 2004).

140. *Id.* § 316.1. The main changes are found at 11 U.S.C. § 348(f)(1)(A).

141. See, e.g., *FitzSimmons v. Walsh (In re FitzSimmons)*, 725 F.2d 1208 (9th Cir. 1984); *In re Harp*, 166 B.R. 740 (Bankr. N.D. Ala. 1993); *In re Herberman*, 122 B.R. 273 (Bankr. W.D. Tex. 1990).

142. BAPCPA, Pub. L. No. 109-8, § 213(1), 119 Stat. 23, 52 (codified at 11 U.S.C. § 1129(a)(14)).

143. *Id.* § 1228(b), 119 Stat. at 200.

144. 11 U.S.C. § 1322(b)(1) (2000). I acknowledge that similar changes were made with respect to the current status of domestic support obligations for chapter 13 plan confirmations, and also without modification of § 1322.

### c. Good Faith

Good faith will change for individual chapter 11 debtors. Before BAPCPA, the focus in individual cases was the devotion of sufficient income to pay creditors.<sup>145</sup> Some courts had even adopted chapter 13's disposable income test as an index of good faith.<sup>146</sup> But the change to § 1123(a)(8), requiring the provision of an amount equal to at least five years' worth of projected disposable income to a plan, effectively requires debtors to devote all their service income to the plan. Thus, BAPCPA undercuts the notion that good faith means that the debtor should provide maximum income. Courts will therefore have to shift their focus in individual cases to other, more traditional, indices of good faith.

### d. Feasibility and Nondischargeable Debts

Every chapter 11 plan proponent must show that, under the plan, reorganization is not likely to be followed by the need to liquidate or reorganize further.<sup>147</sup> This so-called feasibility requirement ensures that reorganization has a lasting quality.

BAPCPA made this feasibility determination more difficult for the individual debtor. Even though BAPCPA changed chapter 11 to provide that an individual's discharge is delayed until completion of the plan,<sup>148</sup> the deadline for filing nondischargeability complaints has not been extended.<sup>149</sup> Given that complaints for fraud and other defalcations must be filed within sixty days of the conclusion of the first meeting of creditors under § 341(a),<sup>150</sup> creditors will be pressured to file a complaint before that time, or request an extension. Because the outcome of these adversary proceedings may make the difference between a complete and incomplete payment, no plan will be confirmed without some showing that it is more likely than not that the debtor will prevail on the dischargeability claim. Thus, BAPCPA forces a fast and rough estimation of the debtor's chances in order to confirm a plan,<sup>151</sup> or a postponement of the confirmation until such claims are known.<sup>152</sup>

145. *In re Harman*, 141 B.R. 878 (Bankr. E.D. Pa. 1992); *In re Kemp*, 134 B.R. 413 (Bankr. E.D. Cal. 1991); 7 COLLIER ON BANKRUPTCY ¶ 1129.03[3][a][iii][A] (15th ed. rev. 2006); see Neely, *supra* note 1, at 18–20.

146. *In re Weber*, 209 B.R. 793, 799 (Bankr. D. Mass. 1997). *But cf. In re Flor*, 166 B.R. 512, 515–16 (Bankr. D. Conn. 1994) (rejecting chapter 13 analysis).

147. 11 U.S.C. § 1129(a)(11) (2000).

148. See BAPCPA § 321(d), 119 Stat. at 95–96 (codified in part at 11 U.S.C. § 1141(d)(2), (5)).

149. See FED. R. BANKR. P. 4007(c) (Interim Rule 2006), available at [http://www.uscourts.gov/rules/Interim\\_Rules\\_CLEAN\\_2006\\_wo\\_Comm\\_Notes.pdf](http://www.uscourts.gov/rules/Interim_Rules_CLEAN_2006_wo_Comm_Notes.pdf).

150. FED. R. BANKR. P. 4007(c).

151. A creative lawyer might attempt to use 11 U.S.C. § 502(e) (2000) to estimate the amount of the nondischargeable claim for purposes of confirmation, but that action itself will take time.

152. If the debtor is also a small business debtor, however, the time within which to file and confirm a plan are substantially circumscribed. A small business debtor must file his plan within 300 days

## 2. *Nonconsensual Confirmations*

Chapter 11 raises the possibility of nonconsensual confirmation; that is, confirmation without the assent of all classes of claims. Because of the structure of § 1129(b), a plan proponent must meet both the non-consensual requirements, and all the consensual requirements (except, of course, for the requirement that all classes consent).<sup>153</sup> Given the structure of the BAPCPA amendments, however, this class-based system of confirmation may no longer effectively apply to individuals.

### a. Projected Disposable Income

A central feature of BAPCPA's amendments was the addition of § 1129(a)(15). Even though this provision is found in the consensual confirmation requirements, it applies only if a "holder of an allowed unsecured claim objects to the confirmation of the plan."<sup>154</sup> Thus, not only may every creditor press the "best interests" test of § 1129(a)(7), every unsecured creditor may also press § 1129(a)(15)'s disposable income test.

This test, borrowed almost verbatim from chapter 13, requires the debtor to devote an amount equal to five years' worth of projected disposable income to the plan, with the five years measured from the date the plan is confirmed or plan payments start, whichever is later.<sup>155</sup> This will provide a playground for creative lawyers. One question that arises is whether § 1129(a)(15) requires all actual service-related income to be devoted to the plan, or only an amount equal to the projected disposable income, determined as of confirmation. The issue might arise in the following case: say that a debtor owns significant real estate, and the plan calls for its sale. Assume that the net proceeds from the sale exceed the debtor's projected salary (or consulting agreement payments) for the five-year period. Has the debtor met this provision by offering up the property?

Finally, although the Advisory Committee on Bankruptcy Rules does not think so,<sup>156</sup> it is not beyond cavil that § 1129(a)(15)'s reference to § 1325(b)(2) incorporates the means test expenses from § 707(b). Section 707(b)(2)'s expenses are incorporated into chapter 13 by

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of filing, BAPCPA § 437, 119 Stat. at 113 (codified in part at 11 U.S.C. § 1121(e)), and must then confirm that plan within 45 days, *id.* § 438 (codified at 11 U.S.C. § 1129(e)). There are only limited circumstances in which these deadlines may be extended. *Id.* § 437 (codified in part at 11 U.S.C. § 1121(e)(3)).

153. 11 U.S.C. § 1129(b)(1) (2000).

154. BAPCPA § 321(c)(1), 119 Stat. at 95 (codified at 11 U.S.C. § 1129(a)(15)).

155. *Id.*

156. See Committee Note to Forms 22A, 22B & 22C, at 6, available at [http://www.uscourts.gov/rules/Revised\\_Rules\\_and\\_Forms/B22A-C-Note.pdf](http://www.uscourts.gov/rules/Revised_Rules_and_Forms/B22A-C-Note.pdf) ("The Chapter 11 form is the simplest of the three, since the means-test deductions of § 707(b)(2) are not employed in determining the extent of an individual Chapter 11 debtor's disposable income.").

§ 1325(b)(3), which is not specifically referred to in § 1129(a)(15).<sup>157</sup> But the lead in to § 1325(b)(3) states that it is to be used to calculate the “[a]mounts reasonably necessary to be expended under [§ 1325(b)](2).”<sup>158</sup>

Could this mean that § 1325(b)(3)’s reference to § 1325(b)(2) follows any use or reference in the Code to § 1325(b)(2)? In other words, does it follow, in much the same way that the rules of § 102 apply to all words in title 11 without any reference back to § 102, that any reference to § 1325(b)(2) carries with it all sections that help define it?<sup>159</sup> Although the Rules Committee’s interpretation will be entitled to deference, it is not the only way to read the statute, thus leaving more uncertainty about the section’s scope.

#### b. Absolute Priority and Cram Down

Any nonconsensual plan of reorganization must be “fair and equitable,”<sup>160</sup> which has generally been held to require compliance with, among other things, the absolute priority rule.<sup>161</sup> How that rule applies to individuals, however, is a puzzle.

The applicability of the absolute priority rule to individuals and small businesses has always presented confusion. Before 1952, for example, individual debtors under chapter XI of the Bankruptcy Act had to propose plans that were “fair and equitable.”<sup>162</sup> Congress deleted the “fair and equitable” requirement from chapter XI in 1952.<sup>163</sup> As the accompanying House Report stated, “the fair and equitable rule . . . cannot be realistically applied in a Chapter XI [action] . . . . Were it so applied, . . . no corporate debtor where the stock ownership is substantially identical with management could effectuate an arrangement except by payment of the claims of all creditors in full.”<sup>164</sup> Currently, chapter 12 and chapter 13 debt adjustment plans do not need to be “fair and equitable” with respect to dissenting creditors.<sup>165</sup> This means, among other things, that plans confirmed under those chapters do not have to satisfy the absolute priority rule.<sup>166</sup>

157. See BAPCPA § 102(h)(2), 119 Stat. at 33–34 (codified in part at 11 U.S.C. § 1325(b)(3)); *id.* § 102(a)(2)(C), 119 Stat. at 27–32 (codified in part at 11 U.S.C. § 707(b)(2)); *cf. id.* § 321(c)(1), 119 Stat. at 94 (codified at 11 U.S.C. § 1129(a)(15)).

158. *Id.* § 102(h)(2).

159. 11 U.S.C. § 102 (2000). The counter argument is that § 103 makes § 102 applicable throughout the Code, whereas there is no similar section that makes any provision in chapter 13 generally applicable to chapter 11 cases.

160. 11 U.S.C. § 1129(b)(1) (2000).

161. *Case v. L.A. Lumber Prods. Co.*, 308 U.S. 106 (1939).

162. H.R. REP. NO. 82-2320, at 21 (1952), *reprinted in* 1952 U.S.C.C.A.N. 1960, 1981–82.

163. Act of July 7, 1952, Pub. L. No. 82-456, § 35, 66 Stat. 420, 433 (1952).

164. H.R. REP. NO. 82-2320; *see also* S. REP. NO. 82-1395, at 11–12 (1952), *reprinted in* U.S.C.C.A.N. 1960, 1981–82.

165. 11 U.S.C.A. §§ 1225(b)(1), 1325(b)(1) (West 2004 & Supp. 2006).

166. *Id.*

Even before BAPCPA, courts were in disarray regarding whether an individual debtor could cram down a plan over the dissent of a class of unsecured creditors.<sup>167</sup> While § 1129(a)(15) requires the debtor to commit to the plan property that has a value of certain future income, the absolute priority rule looks to the allocation of prepetition assets.<sup>168</sup> In a corporate reorganization, if there is not enough value to reach a junior class, such as the equity holders, that class is eliminated.<sup>169</sup> Elimination of the “equity” class in an individual case, while not without historical precedent,<sup>170</sup> is something most courts would avoid.

This has caused some to believe that individual debtors cannot effect a nonconsensual confirmation.<sup>171</sup> Others, however, have noted that confirmation can comply with absolute priority through the contribution of exempt assets, or through loans from family, friends, or gullible third parties.<sup>172</sup> Yet, even that aspect is open to some doubt.<sup>173</sup>

c. What Assets May or Must Be Devoted to the Plan—of the Amendment to 11 U.S.C. § 1129(b)(2)(B)(ii)

The BAPCPA amendments address this conundrum of individual cram down in a roundabout way by changing the statutory example of compliance with absolute priority, found in § 1129(b)(2)(B)(ii). Section 321 of BAPCPA added the following text to § 1129(b)(2)(B)(ii), applicable only in the case of an individual debtor:

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167. See, e.g., *Unruh v. Rushville State Bank*, 987 F.2d 1506, 1508 (10th Cir. 1993); *In re Davis*, 262 B.R. 791, 794 (Bankr. D. Ariz. 2001); *In re East*, 57 B.R. 14, 15 n.1 (Bankr. M.D. La. 1985); see also H. Gray Burks IV, *Application of the Absolute Priority Rule to Exemptible and Abandonable Property—Is Cramdown Eliminated in Individual Chapter 11’s?*, 1 NORTON BANKR. L. ADVIS. 1, 1 (1991). As Sally Neely notes:

The debate over whether section 1129(b)(2)(B) applies to individual debtors has recently been fueled by the court of appeals decisions in *Security Farms v. General Teamsters Local 890* (*In re General Teamsters Local 890*), 265 F.3d 869 (9th Cir. 2001) (neither members nor parent labor union of not-for-profit local union held interests for purposes of section 1129(b)(2)(B)(ii)), and *In re Wabash Valley Power Ass’n*, 72 F.3d 1305 (7th Cir. 1995) (members could continue in control of rural electric cooperative without violating the absolute priority rule of § 1129(b)(2)(B)(ii)).

Neely, *supra* note 1, at 12.

168. 11 U.S.C.A. § 1129(a)(15), (b)(2)(B) (West 2004 & Supp. 2006).

169. See, e.g., 11 U.S.C.A. § 1129(b)(2)(B)(ii) (West 2004 & Supp. 2006) (coding absolute priority rule as to unsecured creditors).

170. See WILLIAM BLACKSTONE, 2 COMMENTARIES \*472 (“[Under Roman law], creditors might cut the debtor’s body into pieces, and each of them take his proportionable share.”); see also Vern Countryman, *Bankruptcy and the Individual Debtor—and a Modest Proposal to Return to the Seventeenth Century*, 32 CATH. U.L. REV. 809, 810 (1983).

171. Burks, *supra* note 167.

172. *In re Henke*, 90 B.R. 451 (Bankr. D. Mont. 1988) (allowing an individual to contribute non-exempt property—income from a patent held in the name of the debtor—for purposes of the new value exception).

173. Some cases have read the use of the term “property” in § 1129(b)(2)(B)(ii) to include exempt property, which effectively blocks use of that property as a contribution by the debtor for which he or she would receive credit. See, e.g., *In re Gosman*, 282 B.R. 45 (Bankr. S.D. Fla. 2002); *In re Ysparro*, 100 B.R. 91, 99 (Bankr. M.D. Fla. 1989). *Contra In re Henderson*, 321 B.R. 550, 558–60 (Bankr. M.D. Fla. 2005); *In re Egan*, 142 B.R. 730, 733 (Bankr. E.D. Pa. 1992).

the debtor may retain property included in the estate under section 1115, subject to the requirements of subsection (a)(14) of this section [related to the satisfaction of all postpetition domestic support obligations].<sup>174</sup>

The problem, however, is that this addition contains a somewhat ambiguous reference to “property included in the estate under section 1115.”<sup>175</sup> At first glance, this section might be read to allow a debtor, so long as he or she meets the projected income test of § 1129(a)(15), to keep all postpetition income from services. But this would be an odd result given the effect of § 1123(a)(8), also added by BAPCPA. It would be the rare case in which a debtor would have any funds left over after pledging an amount equal to five years’ worth of projected income to the plan. This might mean that income from and after the plan’s fifth year could be kept over the dissent of a class of unsecured creditors, but that also seems somewhat odd.

A further oddity is in the language of § 1115 itself. That section states that “property of the estate includes, in addition to the property specified in Section 541” all postpetition income from services.<sup>176</sup> But does this locution bring all of the property snagged by § 541 into the chapter 11 estate, such that a person could say that § 1115, by incorporation, specifies all property of the estate in chapter 11 cases? If so, then the exception in § 1129(b)(2)(B)(ii) becomes a lot more interesting. Given the paucity of legislative history on this point, the section’s intended scope is unclear. The reader is left with two widely different results: miserly post-fifth-year income on one side, and generous designation of all estate property on the other.

### C. *Postconfirmation Issues*

BAPCPA also modified the chapter 11 discharge for an individual. Discharge is now delayed until completion of the payments under the plan.<sup>177</sup> This tracks chapter 13 in the main, but leaves some questions open as how to assimilate into the plan the inevitable changes that will occur postconfirmation.

#### 1. *Who May Modify*

The first problem is who has standing to modify a confirmed plan. In chapter 13, the debtor, the trustee, or a holder of an unsecured claim may seek to modify the plan.<sup>178</sup> Under new § 1127(e), the same group

174. BAPCPA, Pub. L. No. 109-8, § 321(c)(2), 119 Stat. 23, 95 (codified at 11 U.S.C. § 1129(b)(2)(B)(ii)).

175. *Id.*

176. *Id.* § 321(a)(1), 119 Stat. at 94–95 (codified at 11 U.S.C. § 1115)).

177. *Id.* § 321(d)(2), 119 Stat. at 95 (codified at 11 U.S.C. § 1141(d)(5)).

178. 11 U.S.C.A. § 1329 (West 2004 & Supp. 2006).

would seem to be empowered to seek a change.<sup>179</sup> The difference is that the changes to chapter 11 did not pick up the changes made to § 1329, which now permits modification to enable the debtor to pay necessary health insurance premiums.<sup>180</sup> In addition, secured creditors are not given standing to seek modification,<sup>181</sup> although they often bear the brunt of the long-term changes effected by chapter 11 plans.

## 2. The “Hardship” Discharge

Of more interest is the opportunity for a chapter 11 individual debtor to obtain a discharge before completing plan payments. Under chapter 13, such a discharge is possible, but it covers only unsecured debts not subject to nondischargeability under § 523.<sup>182</sup> More importantly, the debtor must show that the “failure to complete [plan] payments is due to circumstances for which the debtor should not justly be held accountable,” and that “modification of the plan under section 1329 of this title is not practicable.”<sup>183</sup>

The chapter 11 analogue to this provision omits two parts. First, it does not grant a lesser discharge; there is no exception for debts covered by § 523(a).<sup>184</sup> Second, the provision drops the first part to the two conditions for discharge—that the debtor should not justly be held accountable for failure to complete payments—but keeps the second, making the early discharge turn on whether modification is “not practicable.”<sup>185</sup> At

179. See BAPCPA § 321(e), 119 Stat. at 96 (codified in part at 11 U.S.C. § 1127(e)).

180. BAPCPA added a fourth paragraph to § 1329(a) that allows the modification of a chapter 13 plan to:

(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.

*Id.* § 102(i)(3), 119 Stat. at 34–35.

181. *Id.* § 321(e), 119 Stat. at 96.

182. 11 U.S.C.A. § 1328(b) (West 2004 & Supp. 2006).

183. *Id.* § 1328(b)(1), (3).

184. This is likely not a drafting glitch. The scope of the discharge for individuals in chapter 11 has always been coextensive with the discharge in chapter 7, and thus the debts listed in § 523(a) have always been nondischargeable in chapter 11. Only in chapter 13, with its former “super” discharge, would the issue have arisen.

185. BAPCPA § 321(d)(2), 119 Stat. at 95 (codified in part at 11 U.S.C. § 1141(d)(5)(B)(ii)). See generally 11 U.S.C.A. §§ 1141(d)(5)(B)(i), 1328(b)(2) (West 2004 & Supp. 2006) (establishing that

this point, it is unclear what sort of logic was behind the omission—it cannot be the view that chapter 11 confirmation is administratively easier than confirmation in chapter 13. For one thing, chapter 11 still requires disclosure to each impaired creditor and the opportunity for each such creditor to vote.<sup>186</sup> Perhaps the thought was that before using this section, the debtor would have to propose a plan that was not accepted. However, given the relatively Draconian provisions for dismissal if one cannot confirm a plan, this would seem to require too much.

## V. CONCLUSION

As examined in this article, BAPCPA amended chapter 11 in five places and in ways that directly affect individuals. These few changes, however, have deep and wide-reaching ripple effects. Post-BAPCPA administration and confirmation of an individual's chapter 11 plan will significantly and substantially differ from the administration and confirmation of other chapter 11 plans. Indeed, given the interrelatedness of chapter 11's provisions, the full extent of these changes may not be known for a long time.

Form should follow function. The significant changes to chapter 11 should have been reflected in the structure of the Bankruptcy Code. Congress had a ready and simple tool to reflect these changes: the subchapter. For its own reasons, however, Congress chose not to use this device, which is difficult to understand. Congress has previously made effective use of the subchapter within the Bankruptcy Code, especially in the treatment of other subclasses of debtors such as railroads and stockbrokers.

The failure to use a common and simple drafting tool—the subchapter—to organize the new provisions will have the untoward effect of increasing the incubation period of understanding for thousands of individual chapter 11 debtors. Participants in the bankruptcy system deserved better.

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both the chapter 11 chapter and 13 discharges require that the plan have paid at least liquidation value to unsecured creditors).

186. Or it might. At first glance, § 1127(f) would appear to make §§ 1121–1128, and the requirements of § 1129 applicable to all modifications. The qualifier to this provision, however, refers to “any modification under subsection (a).” BAPCPA § 321(e). Subsection (a), however, only applies to preconfirmation modification, thus leaving open the question of whether these sections apply to postconfirmation modifications.

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Bankruptcy District	Local Rule	Description	Form Individual Ch 11 Plan	Form Individual Ch 11 DS
Bankr. N.D. Ala.	None			
Bankr. M.D. Ala.	None			
Bankr. S.D. Ala.	None			
Bankr. D. Alaska	None			
Bankr. D. Ariz.	Considering	Requiring Forms for Individual Ch. 11 Plan and DS		
Bankr. E.D. & W.D. Ark.	None			
Bankr. E.D. Cal.	None			
Bankr. N.D. Cal.	None	No LR regarding this model plan and DS. Use of the Plan is not required, but is strongly encouraged by many judges of the Northern District. Individual Ch 11 Debtors can ask court to authorize use of forms and should consult website whether a specific judge mandates the use of the form.	<a href="#">Combined Plan and DS</a> <a href="#">F2081-1PLAN.pdf</a>	<a href="#">F2081-1.DISCLSRSTMT.pdf</a>
Bankr. C.D. Cal.	<a href="#">LBR 2081-2</a>	Proposed Form Combined Plan and DS - based on N.D. Cal. LR Committeed has not considered a model plan		
Bankr. S.D. Cal.	Considering			
Bankr. D. Colo.	None			
Bankr. D. Conn.	None			
Bankr. D. Del.	None	LR Committeed has not considered a model plan		
Bankr. D. D.C.	None			
Bankr. M.D. Fla.	None	LR Committeed has not considered a model plan		
Bankr. N.D. Fla.	None			
Bankr. S.D. Fla.	None			
Bankr. M.D. Ga.	None			
Bankr. N.D. Ga.	None			
Bankr. S.D. Ga.	None			
Bankr. D. Haw.	None			
Bankr. D. Idaho	None			
Bankr. C.D. Ill.	None			
Bankr. N.D. Ill.	None	LR Committeed has not considered a model plan		
Bankr. S.D. Ill.	None			
Bankr. N.D. Ind.	None	LR Committeed has not considered a model plan		
Bankr. S.D. Ind.	None			
Bankr. N.D. Iowa	None	Local bankruptcy rules abolished in 2003		
Bankr. S.D. Iowa	None			
Bankr. D. Kan.	None			
Bankr. E.D. Ky.	None			
Bankr. W.D. Ky.	None			
Bankr. E.D. La.	None			
Bankr. M.D. La.	None			
Bankr. W.D. La.	None			
Bankr. D. Me.	None	LR Committeed has not considered a model plan		
Bankr. D. Md.	None			
Bankr. D. Mass.	None			
Bankr. E.D. Mich.	None			
Bankr. W.D. Mich.	None			
Bankr. D. Minn.	None	LR Committeed has not considered a model plan		
Bankr. N.D. Miss.	None			
Bankr. S.D. Miss.	None			
Bankr. E.D. Mo.	None	LR Committeed has not considered a model plan		
Bankr. W.D. Mo.	None			
Bankr. D. Mont.	None			
Bankr. D. Neb.	None			
Bankr. D. Nev.	None			
Bankr. D. N.H.	None			
Bankr. D. N.J.	<a href="#">LBR 3016-1 and 3016-2</a>	Links to form plan and DS but not requiring debtors to use the forms. This is a Plan and DS for Individuals and Businesses in Ch 11.	<a href="#">LocalForm18.pdf</a>	<a href="#">LocalForm19.pdf</a>
Bankr. D. N.M.	None			
Bankr. E.D.N.Y.	None			
Bankr. N.D.N.Y.	None			
Bankr. S.D.N.Y.	None			
Bankr. W.D.N.Y.	None			
Bankr. E.D.N.C.	None			
Bankr. M.D.N.C.	None			
Bankr. W.D.N.C.	None			
Bankr. D. N.D.	None			
Bankr. N.D. Ohio	None			
Bankr. S.D. Ohio	None	LR Committeed has not considered a model plan		
Bankr. E.D. Okla.	None			
Bankr. N.D. Okla.	None			
Bankr. W.D. Okla.	None			
Bankr. D. Or.	None			
Bankr. E.D. Pa.	None			
Bankr. M.D. Pa.	None			
Bankr. W.D. Pa.	None			
Bankr. D. P.R.	None			
Bankr. D. R.I.	None			
Bankr. D. S.C.	None			
Bankr. D. S.D.	None	LR Committeed has not considered a model plan		
Bankr. E.D. Tenn.	None			
Bankr. M.D. Tenn.	None			
Bankr. W.D. Tenn.	None			
Bankr. E.D. Tex.	None			
Bankr. N.D. Tex.	None			
Bankr. S.D. Tex.	<a href="#">LR 3016-1</a>	in Chapter 11 Cases in which a debtor is an individual, the form of the chapter 11 plan must either: (1) Be in the form as published on the Court's website and state in the title of the Plan that the Plan is a "Uniform Individual Chapter 11 Plan"; or (2) State in the title of the Plan that the Plan is a "Non-Uniform Individual Chapter 11 Plan."	<a href="#">Form Individual Combined Ch. 11 Plan and DS</a>	
Bankr. W.D. Tex.	None			
Bankr. D. Utah	None	LR Committeed has not considered a model plan		
Bankr. D. Vt.	None			
Bankr. E.D. Va.	None			
Bankr. W.D. Va.	None			
Bankr. E.D. Wash.	None			
Bankr. W.D. Wash.	None			
Bankr. N.D. W.V.	None			
Bankr. S.D. W.V.	None			
Bankr. E.D. Wis.	None			
Bankr. W.D. Wis.	None			
Bankr. D. Wyo.	None			

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Table F-2.

U.S. Bankruptcy Courts—Business and Nonbusiness Cases Commenced, by Chapter of the Bankruptcy Code.

Circuit and District	Predominant Nature of Debt <sup>1</sup>															
	Total Filings			Business Filings			Nonbusiness Filings			Total						
	Total Chapter 7	Total Chapter 11	Total Chapter 12	Chapter 7	Chapter 11	Chapter 12	Chapter 13	Chapter 7	Chapter 11	Chapter 13	Total	Chapter 7	Chapter 11	Chapter 13		
<b>TOTAL</b>	1,071,932	833	833	728,833	8,980	395	333,626	33,212	22,334	7,660	395	2,727	1,038,720	706,499	1,320	330,899
<b>DC</b>				685	39	0	109	73	35	35	0	3	760	650	4	106
<b>1ST</b>	33,138	21,284	383	1,988	21	53	11,418	1,316	763	308	53	192	31,822	20,521	75	11,226
ME	2,408	1,988	21	394	5	5	394	135	86	20	5	24	2,273	1,902	1	370
MA	12,562	9,864	114	2,559	25	25	2,559	435	288	78	25	44	12,127	9,576	36	2,515
NH	3,231	2,426	33	772	0	0	772	243	149	27	0	67	2,988	2,277	6	705
RI	3,528	2,967	6	555	0	0	555	120	107	5	0	8	3,408	2,860	1	547
PR	11,409	4,039	209	7,138	23	23	7,138	383	133	178	23	49	11,026	3,906	31	7,089
<b>2ND</b>	45,017	36,883	851	7,245	14	14	7,245	2,049	1,084	800	14	127	42,968	35,799	51	7,118
CT	7,154	6,078	95	980	1	1	980	306	210	83	1	12	6,848	5,868	12	968
NY, N	7,697	6,087	30	1,571	9	9	1,571	162	100	28	9	25	7,535	5,987	2	1,546
NY, E	14,371	12,657	250	1,460	0	0	1,460	586	321	238	0	23	13,785	12,336	12	1,437
NY, S	9,284	7,374	424	1,465	1	1	1,465	740	288	401	1	30	8,544	7,086	23	1,435
NY, W	5,588	3,948	48	1,590	2	2	1,590	210	128	46	2	34	5,378	3,820	2	1,556
VT	923	739	4	179	4	4	179	45	37	4	1	3	878	702	0	176
<b>3RD</b>	59,944	41,296	1,411	17,191	14	14	17,191	2,871	1,282	1,338	14	205	57,073	40,014	73	16,986
DE	3,424	1,865	807	721	0	0	721	974	130	807	0	6	2,450	1,735	0	715
NJ	29,370	22,439	323	6,606	2	2	6,606	934	589	280	2	63	28,436	21,850	43	6,543
PA, E	11,879	6,945	123	4,805	5	5	4,805	432	252	113	5	61	11,447	6,693	10	4,744
PA, M	6,763	4,534	50	2,178	1	1	2,178	219	132	45	1	41	6,544	4,402	5	2,137
PA, W	8,484	5,493	108	2,877	6	6	2,877	304	171	93	6	34	8,180	5,322	15	2,843
VI	24	20	0	4	0	0	4	8	8	0	0	0	16	12	0	4
<b>4TH</b>	79,537	47,903	646	30,968	20	20	30,968	2,256	1,517	537	20	182	77,281	46,386	109	30,786
MD	23,118	17,304	176	5,635	3	3	5,635	555	378	129	3	45	22,563	16,926	47	5,590
NC, E	8,183	2,511	130	5,541	1	1	5,541	320	166	115	1	38	7,863	2,345	15	5,503
NC, M	4,945	2,113	31	2,798	3	3	2,798	204	149	29	3	23	4,741	1,964	2	2,775
NC, W	5,675	3,305	53	2,313	4	4	2,313	222	144	50	4	24	5,453	3,161	3	2,289
SC	7,702	3,149	60	4,490	3	3	4,490	234	166	53	3	12	7,468	2,983	7	4,478
VA, E	19,852	12,131	136	7,584	1	1	7,584	477	339	109	1	28	19,375	11,792	27	7,556
VA, W	6,399	4,300	22	2,074	3	3	2,074	119	93	17	3	6	6,280	4,207	5	2,068
WV, N	1,598	1,346	10	242	0	0	242	58	47	9	0	2	1,540	1,299	1	240
WV, S	2,065	1,744	28	291	2	2	291	67	35	26	2	4	1,998	1,709	2	287
<b>5TH</b>	69,100	29,175	759	39,145	20	20	39,145	3,036	2,030	710	20	275	66,064	27,145	49	38,870
LA, E	3,745	1,934	35	1,776	0	0	1,776	200	150	34	0	16	3,545	1,784	1	1,760
LA, M	1,757	960	10	787	0	0	787	51	40	10	0	1	1,706	920	0	786
LA, W	10,388	2,334	40	8,009	5	5	8,009	120	69	31	5	15	10,268	2,265	9	7,994
MS, N	5,516	2,307	31	3,176	2	2	3,176	123	78	31	2	12	5,393	2,229	0	3,164
MS, S	7,357	3,943	27	3,385	2	2	3,385	178	141	25	2	10	7,179	3,802	2	3,375
TX, N	14,585	6,152	233	8,194	5	5	8,194	815	497	224	5	88	13,770	5,655	9	8,106

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FX, E	5,596	2,632	67	2	2,895	344	264	62	2	16	5,252	2,368	5	2,879
FX, S	10,728	4,164	195	3	6,366	622	381	185	3	53	10,106	3,783	10	6,313
FX, W	9,428	4,749	121	1	4,557	583	410	108	1	64	8,845	4,339	13	4,493
<b>6TH</b>	<b>150,779</b>	<b>103,304</b>	<b>620</b>	<b>51</b>	<b>46,801</b>	<b>2,914</b>	<b>2,042</b>	<b>539</b>	<b>51</b>	<b>279</b>	<b>147,865</b>	<b>101,262</b>	<b>81</b>	<b>46,522</b>
Y, E	9,213	6,701	42	4	2,466	187	123	41	4	19	9,026	6,578	1	2,447
Y, W	9,265	6,679	35	4	2,545	168	110	33	4	19	9,097	6,569	2	2,526
YI, E	31,768	25,965	176	15	5,611	657	409	160	15	72	31,111	25,556	16	5,539
YI, W	10,504	8,891	40	8	1,565	332	258	36	8	30	10,172	8,633	4	1,535
ZH, N	26,089	21,027	53	5	5,004	483	378	48	5	52	25,606	20,649	5	4,952
ZH, S	21,803	15,459	58	6	6,280	463	363	50	6	44	21,340	15,096	8	6,236
IN, E	13,297	7,353	62	5	5,877	244	171	54	5	14	13,053	7,182	8	5,863
IN, M	11,213	6,522	94	4	4,593	223	147	64	4	8	10,990	6,375	30	4,585
IN, W	17,627	4,707	60	0	12,860	157	83	53	0	21	17,470	4,624	7	12,839
<b>7TH</b>	<b>123,550</b>	<b>86,227</b>	<b>510</b>	<b>36</b>	<b>36,777</b>	<b>2,793</b>	<b>2,058</b>	<b>460</b>	<b>36</b>	<b>239</b>	<b>120,757</b>	<b>84,169</b>	<b>50</b>	<b>36,538</b>
L, N	55,094	36,303	302	1	18,488	1,423	1,062	271	1	89	53,671	35,241	31	18,399
L, C	6,762	5,256	25	1	1,480	138	102	23	1	12	6,624	5,154	2	1,468
L, S	4,807	2,974	11	1	1,821	82	52	11	1	18	4,725	2,922	0	1,803
N, N	13,617	10,415	34	5	3,163	206	148	32	5	21	13,411	10,267	2	3,142
N, S	20,229	13,987	83	1	6,158	375	273	77	1	24	19,854	13,714	6	6,134
MI, E	16,801	12,102	26	5	4,668	330	259	21	5	45	16,471	11,843	5	4,623
MI, W	6,240	5,190	29	22	999	239	162	25	22	30	6,001	5,028	4	969
<b>8TH</b>	<b>63,718</b>	<b>45,815</b>	<b>255</b>	<b>43</b>	<b>17,600</b>	<b>1,698</b>	<b>1,285</b>	<b>233</b>	<b>43</b>	<b>133</b>	<b>62,020</b>	<b>44,530</b>	<b>22</b>	<b>17,467</b>
AR, E	7,673	3,353	23	3	4,293	144	97	22	3	23	7,529	3,256	1	4,272
AR, W	4,579	2,585	35	9	1,950	162	106	29	3	18	4,417	2,479	6	1,932
A, N	2,189	2,061	3	3	122	86	76	3	3	4	2,103	1,985	0	118
A, S	3,558	3,179	7	1	371	144	133	7	1	3	3,414	3,046	0	368
IN, N	14,450	12,030	73	8	2,338	465	358	66	8	33	13,985	11,672	7	2,305
MO, E	13,768	9,741	26	0	4,000	218	185	23	0	9	13,550	9,556	3	3,991
MO, W	10,195	7,379	48	5	2,763	230	161	44	5	20	9,965	7,218	4	2,743
NE	5,169	3,556	29	10	1,572	153	101	28	10	12	5,016	3,455	1	1,560
ND	827	744	6	0	77	35	27	6	0	2	792	717	0	75
SD	1,310	1,187	5	4	114	61	41	5	4	11	1,249	1,146	0	103
<b>9TH</b>	<b>222,544</b>	<b>177,219</b>	<b>2,012</b>	<b>61</b>	<b>43,230</b>	<b>7,748</b>	<b>5,635</b>	<b>1,412</b>	<b>61</b>	<b>618</b>	<b>214,796</b>	<b>171,584</b>	<b>600</b>	<b>42,612</b>
AK	593	476	6	0	100	62	38	6	0	7	531	438	0	93
AZ	23,381	20,094	303	4	2,976	867	581	237	4	41	22,514	19,513	66	2,935
CA, N	19,197	11,863	203	13	7,117	798	552	126	13	106	18,399	11,311	77	7,011
CA, E	28,809	23,092	133	21	5,563	842	624	90	21	107	27,967	22,468	43	5,456
CA, C	75,581	61,127	725	2	13,726	2,685	2,051	502	2	129	72,896	59,076	223	13,597
CA, S	12,898	10,393	88	0	2,416	458	332	61	0	64	12,440	10,061	27	2,352
HI	2,093	1,549	20	1	523	104	75	14	1	14	1,989	1,474	6	509
D	5,574	5,067	24	5	478	184	149	21	5	9	5,390	4,918	3	469
VT	1,807	1,538	15	2	252	88	60	14	2	12	1,719	1,478	1	240
WV	13,927	11,316	277	2	2,332	544	347	175	2	20	13,383	10,969	102	2,312
OR	13,610	11,045	43	8	2,514	364	262	39	8	55	13,246	10,783	4	2,459
MA, E	5,182	4,115	27	1	1,039	117	87	20	1	9	5,065	4,028	7	1,030
MA, W	19,730	15,418	147	2	4,160	624	469	106	2	44	19,106	14,949	41	4,116

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GUAM	156	120	1	0	34	10	7	1	0	0	1	146	113	0	33
NMI	6	6	0	0	0	1	1	0	0	0	0	5	5	0	0
<b>10TH</b>	<b>61,940</b>	<b>47,941</b>	<b>272</b>	<b>29</b>	<b>13,692</b>	<b>1,707</b>	<b>1,309</b>	<b>247</b>	<b>29</b>	<b>116</b>	<b>116</b>	<b>60,233</b>	<b>46,632</b>	<b>25</b>	<b>13,576</b>
CO	22,629	18,971	113	3	3,537	740	585	103	3	44	44	21,889	18,386	10	3,493
KS	8,493	5,252	41	15	3,185	183	105	38	15	25	25	8,310	5,147	3	3,160
NM	4,330	3,913	34	0	383	148	113	29	0	6	6	4,182	3,800	5	377
OK, N	3,123	2,777	6	1	339	84	74	6	1	3	3	3,039	2,703	0	336
OK, E	1,610	1,459	3	1	147	43	39	3	1	0	0	1,567	1,420	0	147
OK, W	5,903	4,709	24	8	1,161	153	110	23	8	11	11	5,750	4,599	1	1,150
UT	14,606	9,764	40	1	4,801	295	235	35	1	24	24	14,311	9,529	5	4,777
WY	1,246	1,096	11	0	139	61	48	10	0	3	3	1,185	1,048	1	136
<b>11TH</b>	<b>161,832</b>	<b>91,101</b>	<b>1,222</b>	<b>54</b>	<b>69,450</b>	<b>4,751</b>	<b>3,294</b>	<b>1,041</b>	<b>54</b>	<b>358</b>	<b>358</b>	<b>157,081</b>	<b>87,807</b>	<b>181</b>	<b>69,092</b>
AL, N	14,685	7,012	56	2	7,615	278	213	49	2	14	14	14,407	6,799	7	7,601
AL, M	7,935	1,775	24	4	6,132	111	74	23	4	10	10	7,824	1,701	1	6,122
AL, S	4,670	1,425	22	0	3,223	81	50	18	0	13	13	4,589	1,375	4	3,210
FL, N	3,341	2,765	46	5	525	220	165	35	5	15	15	3,121	2,600	11	510
FL, M	41,167	29,390	440	16	11,319	1,617	1,120	354	16	126	126	39,550	28,270	86	11,193
FL, S	31,917	20,693	307	9	10,905	963	642	248	9	61	61	30,954	20,051	59	10,844
GA, N	39,333	22,565	232	11	16,525	1,044	736	222	11	75	75	38,289	21,829	10	16,450
GA, M	10,068	3,509	43	5	6,511	268	192	41	5	30	30	9,800	3,317	2	6,481
GA, S	8,716	1,967	52	2	6,695	169	102	51	2	14	14	8,547	1,865	1	6,681

<sup>1</sup> Section 101 of the U.S. Bankruptcy Code defines consumer (nonbusiness) debt as that incurred by an individual primarily for a personal, family, or household purpose. If the debtor is a corporation or partnership, or if debt related to operation of a business predominates, the nature of the debt is business.

Note: These figures include the following cases not reflected elsewhere:

Chapter 9		Chapter 15	
TX, N	1	NY, E	4
KY, W	2	NY, S	20
Mi, E	1	DE	31
AR, E	1	PA, E	1
NE	2	MI	1
OK, W	1	MO, E	1
FL, M	1	AK	11
		AZ	4
		CA, N	1
		CA, C	1
		CA, S	1
		WA, W	3
		GUAM	1
		CO	5
		FL, S	3

THE  
ABSOLUTE PRIORITY RULE  
IN  
INDIVIDUAL  
CHAPTER 11 CASES

American Bankruptcy Institute

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## **DID BAPCPA ELIMINATE THE ABSOLUTE PRIORITY RULE?**

As more and more individual Chapter 11 cases wind their way to the bankruptcy trial and appellate courts, more and more cases decide whether the absolute priority rule applies in individual Chapter 11 cases and, if so, what the exceptions to the absolute priority rule are in individual Chapter 11 cases.

Prior to BAPCPA, the absolute priority rule required, in the context of a Chapter 11 plan of reorganization, that the proposed plan be fair and equitable, it must provide “[t]he holder of any claim or interest that is junior to the claims of such [dissenting] class will not receive or retain under the plan on account of such junior claim or interest any property.” 11 U.S.C. §1129(b)(2)(B)(ii). There was little doubt that the absolute priority rule applied in individual Chapter 11 cases prior to BAPCPA. The United States Supreme Court’s decision in *Norwest Bank Worthington v. Ahiers*, 45 U.S. 197 (U.S. 1988), held that the absolute priority rule applied in that individual chapter 11 case. However, BAPCPA added to the above noted section, so that now, in order for a plan to be fair and equitable, it must provide that “[t]he holder of any claim or interest that is junior to the claims of such [dissenting] class will not receive or retain under the plan on account of such junior claim or interest any property, *except that in a case in 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)(15) of this section.*” [Amendment emphasized.]

BAPCPA also amended prior law by including, as property of the estate, the Debtor’s post-petition personal service income and other property acquired during the case up to closing, dismissal or conversion. After BAPCPA became effective, courts have differed as to whether BAPCPA eliminated the absolute priority rule in individual Chapter 11 cases. Most of the earlier cases, one

Bankruptcy Appellate Panel, one district court and a recent bankruptcy court case (which now appear to be in the minority) adopted the so-called “broad” view that since Congress included in Section 1129(b)(2)(B)(ii) a reference to the debtor’s retention of property included in the estate under Section 1115, it had intended to allow the individual Chapter 11 debtor to retain all of the Bankruptcy estate as property, post-confirmation, so that the absolute priority rule would thus be abrogated in individual Chapter 11 cases. *See, e.g., In re Friedman*, 466 B.R. 471 (9<sup>th</sup> Cir. BAP 2012); *In re O’Neal*, 2013 Bankr. LEXIS 1531, 3637 (Bankr. W.D. Ark. 2013), *SPCP Group, LLC v. Biggins*, 465 B.R. 316 (M.D. Fla. 2011); *In re Shat*, 424 B.R. 854 (Bankr. D. Nev. 2010); *In re Johnson*, 402 B.R. 851 (Bankr. N.D. Ind. 2009); *In re Tegeder*, 369 B.R. 477 (Bankr. D. Neb. 2007); *In re Rodemeier*, 374 B.R. 264 (Bankr. D. Kan. 2007); *In re Bullard*, 359 B.R. 541 (Bankr. D. Conn. 2007).

The *Friedman* BAP opinion noted: “A plain reading of Sections 1129(b)(2)(B)(ii) and 1115 together mandates that the absolute priority rule is not applicable in individual chapter 11 debtor cases.”

By contrast, it appears that most of the later cases (and perhaps the emerging trend in the trial courts) find and rule that the absolute priority rule still applies in individual chapter 11 cases. *In re Arnold*, 471 B.R. 578 (Bankr. C.D. Cal. 2012); *In re Tucker*, 2011 WL 5926757 (Bankr. D. Or. 2011); *In re Borton*, 2011 WL 5439285 (Bankr. D. Idaho 2011); *In re Lindsey*, 453 B.R. 886 (Bankr. E.D. Tenn. 2011); *In re Maharaj*, 449 B.R.484, 491-94 (Bankr. E.D. Va. 2011); *In re Kamell*, 451 B.R. 505, 507-12 (Bankr. C.D. Cal. 2011); *In re Draiman*, 450 B.R. 777, 820-22 (Bankr. N.D. Ill. 2011); *In re Walsh*, 447 B.R. 45, 47-49 (Bankr. D. Mass. 2011); *In re Stephens*, 445 B.R. 816, 820-21 (Bankr. S.D. Tex. 2011); *In re Karlovich*, 456 B.R. 677 (Bankr. S.D. Cal. 2010); *In re Steedley*, 2010 L 3528599 (Bankr. S.D. Ga. 2010); *In re Gelin*, 437 B.R. 435, 440-43

(Bankr. M.D. Fla. 2010); *In re Mullins*, 435 B.R. 352, 359-61 (Bankr. W.D. Va. 2010); and *In re Gbadebo*, 431 B.R. 222, 227-30 (Bankr. N.D. Cal. 2010).

The district court for the Eastern District of Tennessee, in affirming the bankruptcy court's decision, found that the absolute priority rule applies in an individual chapter 11 case. *In re Lindsey*, 2012 U.S. Dist. LEXIS 146802, 3-4 (E.D. Tenn. 2012).

In addition, all of the courts of appeal to address the issue have applied the so-called "narrow view" and ruled that the absolute priority rule remains viable in individual chapter 11 cases. In *Maharaj v. Stubbs & Perdue, P.A.*, 681F.3d 558 (4<sup>th</sup> Cir. 2012), the Fourth Circuit noted that the applicable statutory language was ambiguous and, as a result, the Court was required to review the legislative history of the 2005 BAPCPA amendments. The Court noted: "Furthermore, there is nothing in the BAPCPA's legislative history that suggests that Congress intended to repeal the absolute priority rule. To say the least, that would be an odd occurrence for such a significant change."

The Fourth Circuit thoroughly discussed the history of the absolute priority rule, BAPCPA changes and analyzed the issue:

Accordingly, we begin our analysis by reference to the language of the BAPCPA, which we conclude is ambiguous because it is susceptible to more than one reasonable interpretation. We then look to the specific and broader context within which Congress enacted the BAPCPA, as well as a familiar canon of statutory construction, the presumption against implied repeal, and conclude that Congress did not intend to abrogate the absolute priority rule. Thus, notwithstanding the ambiguity of the plain language of the relevant BAPCPA provisions, when the 2005 BAPCPA amendments are viewed in light of the specific context in which they were enacted and the broader context of the BAPCPA and the field of bankruptcy law, we arrive at the conclusion that Congress did not intend to alter longstanding bankruptcy practice by effecting an implied repeal of the absolute priority rule for individual debtors proceeding under Chapter 11. Finally, we consider, and reject, appellants' public policy contentions as unfounded.

\* \* \*

In light of the foregoing, we conclude that the language of § 1129(b)(2)(B)(ii) and § 1115 lends itself to more than one reasonable interpretation, and thus does not have a “plain” meaning. Perhaps the only thing that is clear and plain is that the courts that have considered this issue have arrived at plausible, competing arguments as to why their respective approaches are consistent with Congressional purpose in enacting BAPCPA. In short, the meaning of the BAPCPA amendments is anything but “plain.” It is ambiguous. *See Friedman*, 466 B.R. at 485 (Jury, J., dissenting) (“[T]he meaning of the words is not plain. There can be more than one cogent interpretation of their meaning and intent[.]”).

\* \* \*

As we discussed above, in addition to analyzing the plainness or ambiguity the statute's language, we must also look to the specific context in which that language is used, and the broader context of the statute as a whole. In doing so, we find persuasive the argument that the amendment to § 1129(b)(2)(B)(ii) preserved the absolute priority rule as it operated prior to the passage of BAPCPA.

\* \* \*

In our view, the context demonstrates that Congress intended § 1115 to add property to the estate already established by § 541. This position is supported by the Sixth Circuit's holding in *In re Seafort*, 669 F.3d 662 (6th Cir.2012), in which the court interpreted § 1306(a)—the parallel Chapter 13 provision to § 1115. 8 [Footnote omitted.] The Sixth Circuit interpreted the statute as follows: “ Section 1306(a) expressly incorporates § 541. Read together, § 541 fixes property of the estate as of the date of filing, while § 1306 adds to the ‘property of the estate’ property interests which arise post-petition.” *Seafort*, 669 F.3d at 667.

\* \* \*

Looking to the text of both §§ 1129(b)(2)(B)(ii) and 1115, we find no clear indication that Congress intended to abrogate the longstanding absolute priority rule for individual Chapter 11 debtors. As we discussed above, the language at issue is ambiguous, and we are unable to draw from it a clear Congressional intent to abrogate the rule. To the contrary, we are in agreement with those courts that have concluded that, if Congress intended to abrogate such a well-established rule of bankruptcy jurisprudence, it could have done so in a far less convoluted manner....

681 F.3d at 568-571.

The Tenth Circuit adopted the “narrow view” in *Dill Oil Company v. Stephens*, 704 F.3d 1279 (10<sup>th</sup> Cir. 2013). Like the Fourth Circuit, the Tenth Circuit found that the language of the statute was ambiguous but further determined that the congressional intent in adopting the 2005 changes to Section 1129(b)(2)(B)(ii) was also ambiguous. The Court noted: “the statutory language

and legislative history lack any clear indication that Congress intended to erode a pillar of creditor bankruptcy protection.” 704 F.3d at 1287.

The Fifth Circuit, in *In re Lively*, 717 F.3d 406 (5<sup>th</sup> Cir. 2013), in adopting the “narrow view” found: “[a] plain reading of § 1129(b)(2)(B)(ii) in light of § 1115(a) is that both provisions were adopted when BAPCPA was passed in order to coordinate individual debtor reorganization cases to some extent with Chapter 13 cases, whose debt limit may throw [certain chapter 13 debtors] into a chapter 11 reorganization.” The Fifth Circuit, following the other circuit courts of appeal, found that to the extent there was an ambiguity in the statutes, the Court declined to find that the ambiguity caused an implicit repeal: “[t]he absolute priority rule, in particular, has been a cornerstone of equitable distribution for Chapter 11 creditors for over a century.” 717 F.3d at 406. In the Ninth Circuit, a case has been certified for direct appeal on this question so it remains to be seen how the Ninth Circuit uses the *Friedman* decision. See *In re Arnold*, 471 B.R. 578 (Bankr. C.D. Cal. 2012).

A recent bankruptcy court decision in Arkansas went against the recent trend and adopted the broad view. *In re O’Neal*, 490 B.R. 837 (Bankr. Ark. 2013). In that case, Judge Mixon compared some of the BAPCPA amendments to similar requirements in chapter 13 cases.

The *Friedman* court pointed out that Chapter 13 does not contain an absolute priority rule and pointed to several BAPCPA amendments to individual Chapter 11s which are similar if not identical to Chapter 13. *In re Friedman*, 466 B.R. 471, 483 (B.A.P. 9<sup>th</sup> Cir. 2012). These provisions include section 1123(a)(8) which adds a requirement to individuals that the plan must provide payments of all or such portion of earnings from personal services or other future income of the debtor, resembling section 1322(a)(1). Section 1129(a)(15) was added which states that the plan must contribute an amount equal to the Debtors’ projected disposable income over the longer of five years or the plan payment period upon objection by any unsecured creditor, resembling section 1325(b). Section 1141(d)(5)(A) was added, whereby the discharge is not granted until completion of all payments under the plan, resembling section 1328(a). Section 1141(d)(5)(B) was also added, whereby a discharge is permitted for cause before completion of payments, resembling the hardship discharge located

in section 1328(b). Finally, section 1127(e) was added that permits modification of a plan after substantial consummation, resembling section 1329(a). *In re Friedman*, 466 B.R. 471, 483 (B.A.P. 9th Cir. 2012).

Other support has been found in the fact that section 1115 mirrors section 1306 which was part of the original 1978 code which gave the definition of property of the estate a broader definition in a Chapter 13 than the definition of property of the estate in Chapter 11 and Chapter 7. See *In re Friedman*, 466 B.R. 471 (B.A.P. 9th Cir. 2012); Bruce A. Markell, *The Sub Rosa Subchapter: Individual Debtors in Chapter 11 After BAPCPA*, 2007 U. Ill. L.Rev. 67, 75-76 (2007).

490 B.R. at 850.

Judge Mixon goes on to discuss and criticize the narrow view:

The weakness of the narrow view is illustrated if one were to ask the question: “If Congress was not attempting to write out of individual Chapter 11 cases the absolute priority rule, what was the purpose of all of the BAPCPA amendments to Chapter 11, including section 1115, which were obviously borrowed from Chapter 13?” [Footnote omitted.] Chapter 13 has no absolute priority rule and would not be of much use if it did. The means test for Chapter 7 debtors created by BAPCO was to move debtors who could pay something to their creditors to reorganization chapters. Here, these Debtors have no recourse to either Chapter 13 or Chapter 12 because of the debt limits imposed by Congress.

Section 1129(b)(2)(B)(ii) with respect to individual debtors eliminates the application of the absolute priority rule from property described in section 1115. Section 1115 provides that all property described in Section 541 and property from post petition personal services is included in an individual Chapter 11 estate. Section 1115 is written word for word like section 1306 and courts interpreting section 1306 have never bifurcated this section into two species of property as the narrow view does in individual Chapter 11. To read section 1115 and section 1129(b)(2)(B)(ii) as exempting only future income from the absolute priority rule renders ineffective any practical application of section 1115, especially in light of the additional requirements of section 1129(a)(15)(B). When considered in the context of all the applicable sections, section 1115 accomplishes nothing of substance under the narrow view. As one author paraphrased the explanation of the Ninth Circuit BAP in *Friedman*:

[I]t would be “illogical” to require individual debtors to devote five years of disposable income to their plans, but remove the debtors’ means of providing that income, which would be the result if the application of the absolute priority rule were to prevent debtors from retaining valuable prepetition business assets.

Andrew G. Balbus, *Continued Disagreements Over the Application of the Absolute Priority Rule to Individuals in Chapter 11: Friedman and Maharaj*, 21 Norton Bankr. L. & Prac. 755, 761 (2012).

490 B.R. 850, 851.

In a recent district court case, *In re Brown*, 505 B.R. 638 (D.Ct. 2014), the court held that the absolute priority rule remains viable, affirming the same decision made by the bankruptcy court at the trial level. The court noted:

Three circuit courts and seventeen bankruptcy Courts have adopted the narrow view. [Footnote omitted.] On the other side of the issue, one bankruptcy appellate panel, one district Court and seven bankruptcy Courts have adopted the broad view.

Not only is there no clear and unequivocal expression of Congressional intent to repeal the absolute priority rule from which one could conclude that Congress intended to overturn such a significant pre-existing practice, there is no mention of the absolute priority rule in the legislative history of BAPCPA. Congress is presumed to have been aware of the courts' interpretation of the rule and its significance. [Citations omitted.] That Congress did not express its intent to eliminate the **Absolute Priority Rule** in Section 1129(b)(2)(B)(ii) for **individual** debtors militates against finding that it did so by implication. Thus, given the **Rule's** history and its importance, and Congress's lack of explicit expression of its intent to repeal the **Rule**, we conclude that the BAPCPA amendments do not abrogate the **Absolute Priority Rule in individual Chapter 11 cases**.

Preservation of **Absolute Priority Rule** is also consistent with Congress's express goal of curbing abuses of the **bankruptcy** system when it enacted BAPCPA. . . . [Emphasis in the original.]

505 B.R. 643-649.

### **NEW VALUE EXCEPTION IN INDIVIDUAL CHAPTER 11 DEBTOR CASES**

One of the exceptions to the absolute priority rule is the exception for "new value," which allows the holders of the debtor's equity to retain an interest in the reorganized debtor even though classes senior to the equity holders have not accepted the plan and are not being paid in full. This issue was presented in *In re Eagan*, 2013 WL 237812 (W.D.N.C. 2013). Although the *Eagan* court

correctly observed that individual debtors have no shares of stock, memberships or the like to offer potential, hypothetical investors, nevertheless the new value exception to the absolute priority rule applies in individual chapter 11 cases where the plan provides for the debtor to retain equity interests in estate property because the debtor's family members were contributing new value. The Court observed: "[a] reasonable middle ground must therefore be found if individual chapter 11 cases are to retain any practical utility." The Court ultimately found that the new value exception applied, and held that the contributions were adequate to cause the plan to be confirmed as within the new value exception of the absolute priority rule.

*See also In re Henderson*, 341 B.R. 783, 790-91 (M.D. Fla. 2006) (a contribution of \$525,000 by spouse (who was not in bankruptcy) to fund the plan justified retention of non-exempt assets having a market value of approximately \$410,600 and a liquidation value of \$212,500).

Application of the new value exception in individual chapter 11 cases is, as the *Eagan* court noted, more difficult than in a corporate case or a case where tangible stock and membership interests exist that can be offered to investors. Moreover, the Supreme Court's requirements in *Bank of Am. Nat'l Trust & Sav. Ass'n v. 203 N. LaSalle St. Partnership*, 526 U.S. 434 (U.S. 1999) will also be more difficult to comply with due to the nature of the ownership/equity interests of an individual debtor, especially in a case where the individual debtor is not actively engaged in business pursuits or commercial activities.

## **USE OF EXEMPT PROPERTY TO AVOID THE ABSOLUTE PRIORITY RULE**

One of the interesting questions presented by the BAPCPA amendments in individual chapter 11 cases is whether the debtor's attempted retention of property that is exempt is a violation of the absolute priority rule. As was the case with whether the absolute priority rule exists in individual chapter 11 cases, this issue has also caused a conflict among some of the decisions considering it. The issue was before the Court in *In re Egan*, 142 B.R. 730 (Bankr. E.D. Pa. 1992). In *Egan*, the debtors' plan did not provide for any payments to the unsecured creditors. The debtors had claimed exemptions for property they were retaining. No objections had been timely filed to the claimed exemptions. Most of the unsecured creditors voted against the plan but they did not file separate objections. The Bankruptcy Court observed: "if debtors intend to retain only exempt property, then they are merely retaining that which is their absolute right to retain in any event, and they are not, properly speaking, receiving or retaining 'any interest that is junior to the interests' of any class of creditors, 11 U.S.C. § 1129(b)(2)(B)(ii), including the class of unsecured creditors." 142 B.R. at 733.

The case of *In re Grosman*, 282 B.R. 45 (Bankr. S.D. Fla. 2002) reached a contrary result. There, the debtor's plan proposed limited payments to the unsecured creditors and sought to exempt (and keep) the exempted assets. The Bankruptcy Court denied confirmation (through denial of approval of the disclosure statement because the plan lacked feasibility) and found: "[t]here can be no question that the Debtor in this case is a 'holder of an interest that is junior' to the claims of unsecured creditors...[because] Debtor owns an interest in the Exempt Property." 282 B.R. at 48. The *Grosman* court also ruled that the § 1129(b)(2)(B)(ii) reference to including "any property"

prevents a debtor from retaining exempt or non-exempt property without paying the value of all such property to creditors.

The trial court in the original *Maharaj* case mentioned this issue, 449 B.R. 484, 493 at n.4. (Bankr. E.D. Va. 2011), although it was not critical to the Court's ultimate holding. There, the *Maharaj* trial court indicated that allowing an individual chapter 11 debtor to retain exempt property in a plan under 1129(b) was consistent with the correct reasoning in the *Egan* decision and was also correct in light of 11 U.S.C. § 1123(c).

*See also In re Shin*, 306 B.R. 397, 404 n. 17 (Bankr. D.C. 2004) (relying on West's Bankruptcy Law Letter (October 2002) "to apply the absolute priority rule to an individual debtor's wholly exempt property stands the absolute priority rule on its head – affording to unsecured creditors an artificial 'priority' in exempt property that unsecured creditors simply do not otherwise possess"); *In re Brotby*, 303 B.R. 177, 195-96 (9<sup>th</sup> Cir. BAP 2003) (a contribution from an exempt pension would constitute new value). *And see Colliers on Bankruptcy* ¶ 1129.03[4][c].