AMERICAN BANKRUPTCY INSTITUTE

2020 Consumer Bankruptcy Forum

Chapter 13: The Problem, or the Solution?

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CHAPTER 13 BANKRUPTCY: THE PROBLEM OR THE SOLUTION?

Trustees' Perspectives on Overlooked Benefits of Chapter 13 and alternative views of measuring success

In January of this year, while campaigning for the Democratic presidential nomination, Senator Elizabeth Warren released a plan to overhaul the Bankruptcy Code titled, "Fixing our Bankruptcy System to Give People a Second Chance." Her plan to roll back key elements of the 2005 Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA") would certainly benefit consumers struggling with financial difficulties in many aspects. Specifically, Senator Warren proposed to eliminate the means test; allow a discharge of private student loans; allow debtors to pay the fair market value of vehicles without a 910-day waiting period; and eliminate the credit counseling class requirement for bankruptcy eligibility. She also suggested that her plan would add additional consumer benefits including permitting debtors to modify mortgages on their primary residences and ending the prohibition on discharging student loans. Any or all of these modifications would benefit many consumers.

However, Senator Warren also took specific aim at Chapter 13 calling it "onerous" and "burdensome." Additionally, she stated,

> The outcomes in our current system aren't equal, either. Black Americans appear to be much more likely to file for bankruptcy under Chapter 13, a costlier and more burdensome form of bankruptcy that requires people to make several years of payments before getting their debts wiped out – and leaves many in an even worse position as they struggle to make these payments. The data suggest Black filers are more likely to have their cases dismissed, too: people who live in majority Black zip code are more than twice as likely to have their cases thrown out as those living in majority white areas.

Senator Warren's implication is that Debtors' counsel tend to steer minorities into "onerous and burdensome" Chapter 13 cases for reasons that are racially motivated and that the only measure of success in Chapter 13 is through a discharge. While the statistics cannot be disputed, the

conclusions subsequently drawn are certainly up for debate. Chapter 13 trustees have an independent and first-hand view of the reasons for Chapter 13 filings, and some trustees might even say that, while there may be a statistically significant number of minorities in reorganization cases, the outcomes are not as dire as Senator Warrant might suggest. Many Chapter 13 cases really start years prior to an actual bankruptcy filing when consumers interact with predatory lenders and usurious interest rates. Consumers oftentimes spend years outside of bankruptcy protection dealing with the burdensome and onerous issues of financial lives. Many bankruptcy debtors have stated that the financial stress spilled over to marital and family lives, job performance, and even their own physical and mental health. Bankruptcy may be the first time that some consumers feel relief from those burdens, and Chapter 13 may help minorities to a larger extent. Minorities have historically been victims of lending discrimination, buy-here-pay-here auto sales, check cashing scams, pawn broker loans, and rent-to-own financing which may have hidden finances charges over 100% APR. According to the National Consumer Law Center, nearly 4 in 5 RTO customers earn less than $40,000 annually, and 3 in 5 are minorities. Debtors' attorneys may actually be consumer advocates using Chapter 13 reorganization to level the playing field against financial injustices.

Senator Warren also states, "[i]n Chapter 13, debtors remain in bankruptcy longer and must pay more to creditors." This statement is not accurate. 11 U.S.C. § 1325(a)(4) requires that debtors pay unsecured creditors no less than creditors would have received in a hypothetical Chapter 7 liquidation case. That is, if a debtor had non-exempt assets available to liquidate in a Chapter 7, a Chapter 13 filing allows that debtor to keep the assets so long as that debtor repays the same value; it is an equitable statute. While a Chapter 13 plan may last longer than a Chapter 7 in these circumstances, it does so only because a debtor does not want to liquidate significant assets.

The other situation in which a debtor is required to pay unsecured creditors at all occurs when the debtor has "projected disposable income." In short, projected disposable income looks at the debtor's current monthly income and subtracts reasonable expenses to determine whether the debtor

has any ability to repay unsecured creditor obligations. If the debtor has no available disposable income, then the debtor is not required to file under Chapter 13. However, equity requires that if the debtor has money remaining after living a comfortable life, then the debtor should repay some of those creditors back. In every instance, debtors repay based upon what they can afford to pay and not based upon what they owe. That alone provides more financial relief than they would have received without the bankruptcy system. The individuals who assist the debtors (their own legal advocates, the Chapter 13 trustees, and the Bankruptcy Judges) generally all take great care to make certain that debtors are able to live a reasonable lifestyle. Senator Warren's statement that Chapter 13 (in these instances) requires debtors to pay more to creditors is misplaced for two reasons. First, debtors who have disposable income are not eligible for Chapter 7, so by its very nature the debtors would pay more due to some ability to pay. Second, bankruptcy is equitable for both debtors and creditors; accordingly, if a debtor has income remaining after paying all reasonable and necessary monthly expenses, then the debtor should try to repay even a small dividend to unsecured creditors. However, a debtor who earns less than average median income for his or her state is presumed to be eligible to file a Chapter 7 bankruptcy.

Senator Warren is correct that Chapter 13 bankruptcy has become more "onerous" over the past fifteen years. Ironically, such difficulty was created by Congress itself modifying the Code, and not by the actions of debtors' counsel. Prior to the enactment of BAPCPA in October 2005, whether a debtor had disposable income was determined by trustees and judges who analyzed the debtor's financial records and looked to the reasonableness of the debtor's expenses. BAPCPA created the "means test" for above median income wage earners which is a specific formula averaging the debtor's income in the six full months prior to bankruptcy filing and subtracting National and Local standard expenses as determined by the Internal Revenue Service. Senator Warren argues that the means should be repealed, and trustees generally agree, but for a different reason. Specifically, high income wage earners are more able to manipulate their income during the six full months prior to

filing making it appear that those debtors have less income. For example, a business owner may defer income, or a doctor may take a sabbatical in the months prior to a bankruptcy filing. The means test takes discretion away from trustees and judges who otherwise help combat bankruptcy abuses, and it forces trustees and judges to accept the lowered current monthly income without accounting for the reasonableness or accuracy.

As another example, Congress added a "hanging paragraph" following 11 U.S.C. § 1325(a)(9) requiring debtors to wait 910 days after purchasing a personal vehicle to bifurcate the claim and repay the vehicle's fair market value. Congress's decision to create this delay would affect minorities more significantly. In a 2016 article entitled "Wages by Education," the Economic Policy Institute, State of Working America Data Library, concluded that African Americans are paid less than White peers at every education level (see Chart at the conclusion of this article). Additionally, the National Fair Housing Alliance conducting an investigation and found that 62.5% of the time, "Non-White testers who were more qualified than their White counterparts received more costly pricing options."[1] The investigation also revealed that minorities shopping for vehicles were not offered the same rebates as their White counterparts and on average had higher interest rates costing an average of $2,662.56 over the life of the loan. When read together, this information would suggest that minorities are purchasing less valuable and less reliable vehicles for the same cost of their White counterparts along with a higher debt to income ratio. As such, minorities would be more likely on an average to trade in vehicles with less or no equity and more likely to finance vehicles with rolled in negative equity. The 910-day prohibition means that many debtors in Chapter 13 are paying not only the MSRP of the current vehicle, but also financing the negative equity of previously traded in vehicles.

[1] National Fair Housing Alliance, "Discrimination when Buying a Car. How the Color of Your Skin Can Affect Your Car-Shopping Experience." https://nationalfairhousing.org/wp-content/uploads/2018/01/Discrimination-When-Buying-a-Car-FINAL-1-11-2018.pdf

Senator Warren provides statistics which demonstrate that an inordinate number of minorities are filing Chapter 13. From this data she has drawn an inference that the consumer debtors' bar is racially motivated to earn a living off of the backs of the working poor. In her article, "Fixing Our Bankruptcy System to Give People a Second Chance," Senator Warren wrote, "[t]he changes I've outlined above – like the new single entry point system that eliminates the steering of Black bankruptcy filers into Chapter 13" reflects the fact that she does not work directly with debtors' attorneys and those citizens struggling with financial burdens.

As an industry, attorneys who spend their lives helping the least sophisticated consumers against behemoth financial institutions with unlimited legal resources do not so with the sole motivation of wealth. Instead, as a Chapter 13 trustees tend to agree that the majority of consumer protection attorneys practice in this area of law to help combat perceived injustices and to simply help others without regard to race, religion, or education. For Senator Warren to suggest that debtors' attorneys across the board (Black and White) are racially motivated to "steer Black bankruptcy filers into Chapter 13" is disingenuous and may infer specific conclusions without necessary additional statistics.

Senator Warren also incorrectly suggests that because the average Chapter 13 bankruptcy costs $3,200.00 "more than twice a Chapter 7 filing," debtors' attorneys will earn more money by steering debtors into a Chapter 13. Such is not the case. An attorney may collect $1,000.00 for filing a Chapter 7, attending one meeting of creditors, maybe even reviewing a reaffirmation agreement, and closing the case within 90 days. A respectable attorney may spend approximately ten to twelve hours on a typical Chapter 7 case. A Chapter 13, on the other hand, will require between 36 and 60 months [or even eighty-four months with the CARES Act] of negotiation and legal representation to complete. The "flat fee" is set by each Judicial District and an attorney who signs up to represent a debtor in a Chapter 13 agrees to help the debtor on the case from birth to grave regardless of how much time it may require. There may be numerous creditor motions for relief from stay, trustee

motions to dismiss, and modified plans every time the debtor obtains a new job or has a lifestyle change. The fact that the debtors' bar is placing more minority debtors in Chapter 13 than Chapter 7 would appear to indicate that those consumer advocates are not racially motivated.

Senator Warren contends that an inordinate number of minorities are in Chapter 13 because they cannot afford their upfront attorney fees for a Chapter 7. She is correct. Debtors generally do not want to file under any chapter of bankruptcy, but in many instances are forced into such a position because of aggressive creditor collection (freezing bank accounts, garnishing wages, and placing judicial liens on real estate). Once a garnishment starts, debtors will not obtain an automatic stay until the case is filed. If a debtor's attorney files Chapter 7 while the debtor still owes fees, the debt owed to the attorney is an unsecured and dischargeable debt. The attorney is stayed from attempting to collect his or her own fee, and the fee is discharged upon completion of the case. In an effort to help consumers, the attorney may file a Chapter 13 and collect fees after the case is filed. However, in most regions across the country, those attorneys will charge a greatly reduced fee (even though the Chapter 13 flat fee is much higher) and may convert the case to Chapter 7 once the fees are received. Attorneys must take these steps because the bankruptcy judges are reviewing fees and services closely, and because most debtors' attorneys believe in equity. Senator Warren suggests that we do away with all the positive aspects of Chapter 13 reorganization simply because some debtors do not have money up front to file Chapter 7. There is no need to throw the proverbial baby out with the bathwater. Instead, Congress could simply amend Section 523 of the Bankruptcy Code, entitled "Exceptions to Discharge." The amended Code Section could read: (a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt - … (20) incurred to pay legal fees for the filing of a voluntary bankruptcy under chapter 7 of this title." Adding eighteen words to Section 523(a) would allow debtor's attorneys to charge no money down Chapter 7 filings, obtain the debtor discharge, and then collect payments over a more reasonable time frame. Fees and timing of payments could be set by each court's Local Rules.

Senator Warren is correct that, in most instances a financial reorganization takes longer than asset liquidation. But just because more time is involved does not in any sense correlate to an "onerous" reorganization. In fact, if financial life within a reorganization is more onerous than life outside of bankruptcy, then there is likely no reason for the debtor to have filed under a Chapter 13 bankruptcy. There are many reasons that Chapter 13 bankruptcy make life less onerous, allows debtors to dictate the financial terms of their debts, allows debtors to retain assets, build equity in real estate, and allows debtors an additional safety net to convert to Chapter 7 if the debtors acquire additional debt or a vehicle becomes unrepairable. Specifically:

1) **Delaying Discharge and Holding Creditors at Bay**: As noted above, the success of Chapter 13 cannot necessarily be measured by the percentage of cases which complete and obtain a discharge. Indeed, a discharge may not be the goal. While mere statistics provide a convenient measure of Chapter 13 success, behind the numbers many factors leading to a debtor's decision to opt for Chapter 13 can make that case a success for the debtor, even if the case is not completed and a discharge is not obtained. Debtors in Chapter 13, for instance, may be waiting for future events before converting to Chapter 7. That "breathing spell" afforded the debtor, although not leading to a discharge, nevertheless makes the case successful for the debtor. The automatic stay is certainly one of the most obvious advantages of a bankruptcy filing. While the automatic stay in a Chapter 7 case terminates upon the granting of the debtor's discharge (which may occur within 3-4 months) - - and keeping in mind that many debts may be non-dischargeable by virtue of 11 U.S.C. §523 - - a debtor's discharge in Chapter 13 may be delayed for 3–5 years, thus maintaining the automatic stay in place for the entire 3–5 year period. Even absent a discharge, the extended period of protection afforded by the automatic stay can provide a significant benefit to many debtors, not only in terms of dealing with their financial situation, but also in terms of the peace of mind enjoyed by a debtor knowing that aggressive creditor actions will be held at bay. Enhanced quality of life should not be underestimated.

Mortgage Debt. Specifically, with respect to non-dischargeable debts, Chapter 13, unlike Chapter 7, provides a struggling debtor a meaningful opportunity to address non-dischargeable home mortgage debt. A debtor who is behind on secured mortgage payments can save his/her residence by curing pre-petition arrearages over up to a 5-year period while maintaining ongoing post-petition mortgage payments. Chapter 7 debtors will be unable to save their homes and retain their home equity; Chapter 13 debtors have that opportunity. Particularly with home values escalating and more debtors enjoying equity in their homes, Chapter 13 provides a meaningful benefit. Further, a debtor may use the breathing spell afforded by Chapter 13 to negotiate a mortgage loan modification with a lender. Such negotiations may take several months or longer, but the debtor will have comfort that his/her residence will not be foreclosed during negotiations and may not need to make mortgage payments during the period negotiations are ongoing. Additional protections are in place for both the debtor and the lender because the loan modification ultimately must be approved by the bankruptcy court.

Student Loan Debt. Similarly, debtors burdened with non-dischargeable student loan debt may find advantages in Chapter 13. Under certain circumstances, a debtor may be able to continue to service student loan debt while in Chapter 13 - - certainly, if a debtor is paying over a 3 – 5 year period 100% of unsecured debt, student loan debts may continue. Even absent a 100% plan, however, a debtor may utilize a Chapter 13 plan to separately classify unsecured student loan debt if such classification does not "discriminate unfairly" against other classes of unsecured debt. 11 U.S.C. §1322(b)(1). See *In re Kindle*, 580 B.R. 443 (Bankr. D. So. Car. 2016); *In re Engen*, 561 B.R. 523 (Bankr. D. Kan. 2016); *In re Williams*, 253 B.R. 220 (Bankr. W.D. Tenn. 2000); *In re Sullivan*, 195 B.R. 649 (Bankr. W.D. Tex. 1996). In addition, "consumer debts" of the debtor may be separately classified when another person is liable on such debt with the debtor. Moreover, in 2019 the ABI Commission on Consumer Bankruptcy proposed changes to existing law concerning, among other things, student loans in Chapter 13. Among other recommendations, the Commission urged that (1)

student loan debt be reclassified as priority debt, (2) student loan debt be allowed to be separately classified, (3) student loan debt be afforded "cure and maintain" treatment under 11 U.S.C. §1322(b)(5), (4) in conjunction with debtors' income-driven repayment plans (IDR), payments under a confirmed Chapter 13 plan be considered an "exceptional circumstance" sufficient for DOE to accept any such payments as alternative repayments under such IDRs.

A Chapter 13 debtor's discharge of other unsecured debt may allow the debtor emerging from Chapter 13 to better able to service student loan debt post-bankruptcy. Or a Chapter 13 debtor may, after a significant period of time in Chapter 13, use his/her income and expense history – which has been monitored by the Court and the Chapter 13 trustee – to litigate a hardship discharge of student loan debt under the widely-recognized *Brunner*[2] standard. Specifically, a debtor may, for instance in month 30, seek a hardship discharge of student loan debt under Brunner using the debtor's Chapter 13 income and expense history to establish the "certainty of hopelessness" prong of the Brunner test. It also should be noted that courts recently are demonstrating a greater willingness to find ways to discharge all or a portion of non-dischargeable student loan debt. Such determinations, of course, are intensely fact specific. See *Education Credit Mgmt. Corp. v. Metz*, 2019 WL 1953119 (D. Kan. May 2, 2019) (partial discharge); *In re Swafford*, 604 B.R. 46 (Bakr. N.D. Iowa 2019) (partial discharge); *In re Rosenberg*, 610 B.R. 454 (Bankr. S.D.N.Y. 2020) (complete discharge of $220,000 student loan debt); *In re Nitcher*, 606 B.R. 67 (Bankr. D. Ore. 2019) (partial discharge); *In re Bukovics*, 612 B.R. 174 (Bankr. N.D. Ill. 2020) (partial discharge); *In re McDaniel*, (10th Cir. 2020) (funds received as educational benefit were not "loans" and therefore dischargeable).

Non-Dischargeable Tax Debt and Domestic Support Obligations. Addressing non-dischargeable domestic support obligations (DSOs) and non-dischargeable tax debt in Chapter 13

[2] *In re Brunner, 46 B.R. 752 (S.D.N.Y. 1985)*

provides an additional benefit to financially stressed debtors. Chapter 13 permits debtors to manage their tax debts. Although taxes incurred within 3 year before bankruptcy cannot be discharged, penalties and interest will stop, and debtors can pay tax debt over the applicable commitment period of the confirmed Chapter 13 plan. Penalties and fines related to priority tax debts may be discharged in Chapter 13. Moreover, DSOs which were in arrears at the time of bankruptcy filing can be paid in installments over the period of the Chapter 13 plan. In addition, a Chapter 13 debtor's discharge requires debtor's certification that both pre- and post-petition DSO obligations have been paid. Thus, a Chapter 13 discharge ensures that a debtor emerges from Chapter 13 with no overhanging DSO obligations and a fresh start.

Chapter 13 provides other salutary effects for debtors besides dealing with non-dischargeable debts. Chapter 13 grants a "super discharge;" numerous debts which would not be dischargeable in Chapter 7 can be discharged in Chapter 13. Section 1328(a)(2) lists only a limited number of the section 523(a) exceptions to discharge which are not dischargeable in Chapter 13. Those include debts incurred to pay non-dischargeable tax debts to a governmental unit; certain debts from a prior bankruptcy case for which discharge was denied; divorce decree or separation agreement property settlements which are not domestic support obligations (as defined in section 101(14A); and post-petition homeowners' association fees.

Under the CARES Act[3], debtors who have suffered a material financial hardship directly or indirectly as a result of the COVID-19 pandemic and whose plans were confirmed on or before March 27, 2020, can extend their plan payments and the automatic stay up to 84 months.

Chapter 13 debtors have the ability to recover property which had been levied or repossessed pre-petition. This issue has been most recently and most famously raised in *City of Chicago v. Fulton*, 19-357 (S.Ct.), in which the Supreme Court heard oral argument on October 13, 2020 to

[3] The Coronavirus Aid, Relief, and Economic Security Act, Pub.L. 116–136, enacted March 27, 2020

resolve a circuit split whether a creditor must turn over repossessed property immediately after a debtor files a Chapter 13 petition. It is well-known that the City of Chicago, as an integral component of its annual revenues, writes a substantial number of parking tickets each year and impounds vehicles when those tickets remain unpaid. Chapter 13 debtors' demands for the return of their impounded vehicles upon filing were met with the City's refusal to turn over impounded vehicles. The bankruptcy court, affirmed by the Seventh Circuit, required the City to turn over the vehicles, reasoning that the passive retention of impounded vehicles was an act to control estate property in violation of the automatic stay. The Seventh Circuit thereby joined the Second, Eighth, Ninth and Eleventh Circuits in the majority on the issue. The Third, Tenth and D.C. Circuits conversely have held that a creditor's passive retention of estate property was not an "act" and therefore did not violate the stay. For now, at least, in the majority of districts, Chapter 13 debtors can recover property which was repossessed pre-petition.

2) **Paying Attorney Fees Over Time:** As stated above, unlike a debtor's attorney in Chapter 7[4], a debtor's attorney in Chapter 13 may be paid through estate funds, allowing the fees to be paid over the life of the plan.[5] In most districts, a certain "no-look" fee is awarded to counsel for assisting debtors navigate the Chapter 13 process. These "no-look" amounts are presumptively reasonable but may be challenged by parties in interest.

The ability for debtors to pay attorney's fees over time may result in debtors who would have otherwise chosen to file for relief under Chapter 7 opting instead to file for Chapter 13. It is important to note, however, that not all debtors who appear to be prime Chapter 7 candidates are so; for example, a debtor, who anticipates incurring substantial medical bills in the future, may be

[4] See *Lamie v. United States Tr.*, 540 U.S. 526, 534 (2004) ("A debtor's attorney not engaged as provided by § 327 is simply not included within the class of persons eligible for compensation.").

[5] 11 U.S.C. § 330(a)(4) provides, "[i]n . . . chapter 13 case in which the debtor is an individual, the court may allow reasonable compensation to the debtor's attorney for representing the interests of the debtor in connection with the bankruptcy case."

concerned about the time restrictions on filing consecutive bankruptcies.[6] While it would appear that such debtors are done a great disservice by being steered into Chapter 13, courts and trustees work to ensure equitable results. Principally, trustees will oppose plans that appear to be "fee-only" or even "fee-centric."[7]

Bankruptcy courts are divided on the issue of confirming "fee-only" or "fee-centric" cases.[8] However, the First, Fifth, and Eleventh Circuit Courts seem to be in general agreement that "fee-centric" or "fee-only" cases are not per se unconfirmable and no rule exists to disallow them.[9] The Circuit Courts instead recognize that a "totality of circumstances" must considered.[10] Nevertheless, the First Circuit cautioned that "[w]hile fee-only plans should not be used as a matter of course, there may be special circumstances, albeit relatively rare, in which this type of odd arrangement is justified."[11]

In response to the apprehensive approach that many courts have taken to "fee-only" and "fee-centric" cases, attorneys who regularly practice in the Chapter 13 arena will tailor plans to meet the requirements of confirmation, including but not limited to, reducing their attorney's fees and increasing the proposed dividend to unsecured creditors.

3) **Reorganizing Debts and Predatory Lending Contracts:**

A) Rent to Own – At a local RTO store, a consumer can rent an Amana 3.5 cubic foot top load washer and 6.5 cubic foot electric dryer for 107 weekly payments of $19.99 each (a

[6] See *Sikes v. Crager (In re Crager),* 691 F.3d 671, 675 (5th Cir. 2012).
[7] To be confirmed, plans must be proposed in good faith. 11 U.S.C. § 1325(a)(3). Trustees have often taken the position that "fee-only" or "fee-centric" cases are per se not proposed in good faith.
[8] See *In re Doucet*, No. 15-21531, 2016 WL 2603072 (Bankr. D. Kan. May 3, 2016) (discussing the split among bankruptcy courts).
[9] *Berliner v. Pappalardo (In re Puffer)*, 674 F.3d 78 (1st Cir. 2012*); Sikes v. Crager (In re Crager)*, 691 F.3d 671 (5th Cir. 2012); *Brown v. Gore (In re Brown)*, 742 F.3d 1309 (11th Cir. 2014).
[10] *Brown v. Gore (In re Brown)*, 742 F.3d 1309, 1317 (11th Cir. 2014) ("[T]he facts of each bankruptcy case must be individually examined in light of various criteria to determine whether the chapter 13 plan at issue was proposed in good faith . . . [this circuit] basically adopts a 'totality of the circumstances' approach for determining good faith or lack thereof, which is what other circuits do, too.") (internal quotation marks and citations omitted).
[11] *Berliner v. Pappalardo (In re Puffer)*, 674 F.3d 78, 83 (1st Cir. 2012).

$2,138.93 total cost). At box retailer in the same area, that same washing machine and dryer sells for $896.00. A consumer with poor credit or no cash available would "finance" the RTO for almost exactly 100% APR over 25 months.

Although most courts have held that rental-purchase agreements are neither true leases nor security instruments, nonetheless these agreements are sufficiently executory to fall within § 365, and debtors must therefore either assume or reject the leases in question. With that being said, RTO companies do not lease used consumer goods, consumer goods depreciate quickly, and RTO companies generally want to make a profit. A wise debtor who understands that a two-thousand-dollar washer and dryer is a bad idea and a good poker face, can generally negotiate a deal with the RTO company. A plan which offers $1,000.00 plus 6% on a used washer and dryer may be confirmable without an objection from the creditor. Additionally, corporate entities must appear in Federal Court through counsel, and oftentimes hiring counsel to object to a payment of collateral will cost more than it is worth.

B) Pawnshop Transactions – With 2005 enactment of BAPCPA certain pawn transactions will never become property of the bankruptcy estate, and debtors will not have the power to modify the secured creditor's rights under section 1322(b)(2). The amendment to the definition of property of the estate can be found in § 541(b)(8) which states that property of the estate in a Chapter 13 case does not include: *inter alia* any interest of the debtor in property where the debtor pledged … personal property … as collateral for a loan or advance of money given by a person licensed under law to make such loans or advances, where— (A) the tangible personal property is in the possession of the pledgee or transferee; (B) the debtor has no obligation to repay the money, redeem the collateral, or buy back the property at a stipulated price; and (C) neither the debtor nor the trustee have exercised any right to redeem

provided under the contract or State law, in a timely manner as provided under State law and section 108(b).

Section 108(b) reads, "… if applicable nonbankruptcy law … or an agreement fixes a period within which the debtor … may … cure a default, or perform any other similar act, and such period has not expired before the date of the filing of the petition, the trustee may only file, cure, or perform, as the case may be, before the later of— (1) the end of such period, including any suspension of such period occurring on or after the commencement of the case; or (2) 60 days after the order for relief.

This exclusion from property of the bankruptcy estate reaches pawn transactions when the pawned property is in possession of the pawnbroker, the debtor the debtor has entered into a nonrecourse loan, and the right to redeem under contract or state law has expired or will expire within 60 days. A Chapter 13 debtor who desires to recover pawned property would improve her chances of success by filing the case before the redemption period expires, getting a plan confirmed as quickly as possible, and even filing a secured claim for the creditor. In this manner, the debtor is better positioned to argue that the creditor has claim, that the pledged collateral is property of the estate, and that the confirmation is binding on both the debtor and the creditor. Many trustees, if pressed, would likely be willing to pay a pawn broker as an administrative claim if the asset is necessary for the debtor's reorganization.

C) Title Loans – In most title loan cases the bankruptcy estate exclusion enumerated in § 541(b)(8) do not apply as the debtor generally retains possession of the collateral (it has not been pledged). Therefore, upon filing the collateral is property of the bankruptcy estate and the creditor is stayed from taking any steps to take possession of estate property. Additionally, many title loan companies (especially local operations) incorrectly believe that possession of the title constitutes lien

perfection. While state law applies, many states require the state DMV to notate the lien on the title through recordation. If the title loan company has failed to perfect its lien, the trustee may use its strong-arm powers to avoid the transaction and recover the title. Even if the lender did properly perfect its lien, the provisions of the 910-hanging paragraph do not apply. Specifically, for the 910-day requirement to be in effect, the transaction must be a purchase money security interest. Savvy debtors' attorneys will use the provisions in the Code to allow their clients to retain necessary vehicles with amended repayment terms which make reorganization feasible.

D) Stripping off a Second Mortgage – If a debtor owns a home encumbered by second mortgage and the home's fair market value is less than a payoff on the first mortgage (due to a housing market collapse or declining neighborhood, for example) the debtor can strip off a second mortgage in a Chapter 13. Many minorities are first-generation homeowners with a desperate desire to save their homes. Especially prior to the 2008 housing collapse, predatory lenders were willing to place 125% loan-to-value second mortgages on a home presuming that the housing values would continue to increase. Chapter 13 would allow a debtor's budget to decrease by removing a second mortgage payment and stripping off that loan altogether.

E) Renegotiating a First Mortgage(?) - Many trustees agree with Senator Warren and would support an amendment to Chapter 13 which allows debtors to modify the terms on first mortgages. After the housing market collapse in 2008, many homeowners lost equity in their homes. Allowing debtors' plans to modify the first mortgage to an agreed upon fair market value would allow debtors to build equity and would provide mortgage lenders the same amount they would receive at a foreclosure sale.

4) **The 910 Day Hanging Paragraph**: If a debtor owns a vehicle which was purchased more than 910 days before the date of filing bankruptcy, the debtor can apply 11 U.S.C. §506 to bifurcate the creditor's claim into secured and unsecured claims (i.e., debtor can cramdown the value of that vehicle). In conjunction with bifurcation, debtor can also reduce the interest rate and payment

amount on the vehicle to further assist in financing the debtor's Chapter 13 plan. The 11 U.S.C. §1325(a)(9) so-called "hanging paragraph" prohibits such treatment of vehicles purchased within 910 days of debtor's bankruptcy filing. But it is important to pay particular attention to the language of section 1325(a)(9) to determine if it applies to debtor's circumstance. With respect to motor vehicles, section 1325(a)(9) states that section 506 bifurcation will not be permitted if (1) the creditor has a purchase money security interest securing the debt, (2) the debt was incurred 910 days before the filing of the bankruptcy petition, (3) the collateral for the debt consists of a motor vehicle, and (4) the motor vehicle was acquired for the personal use of the debtor. So, for instance, if the debt is a refinance or a title loan, the claim can still be bifurcated under section 506. Similarly, if the vehicle is not acquired for the personal use of the debtor, section can still be applied to bifurcate the claim. Section 1325(a)(9) also provides that a claim secured by a purchase money security interest in "any other thing of value" (i.e., furniture, electronics, tires) which was purchased more than one year before the filing of the bankruptcy petition also may be bifurcated under section 506.

Even if a secured claim falls within the parameters of section 1325(a)(9), the interest rate may still be lowered to the Till rate, making available some additional funds to finance the debtor's Chapter 13 plan.

5) **Co-debtor Stay**: Hoping to avoid filing bankruptcy, soon-to-be debtors sometimes reach out to friends and family for financial assistance. While friends and family may be unable to provide outright monetary assistance, they will often co-sign debts with the soon-to-be debtor. At some point thereafter, the soon-to-be debtor may become unable to fulfill his/her obligation and may then cease making payments, deciding to now seek relief under the bankruptcy code. If the debtor chooses to file Chapter 7, the co-obligor is left holding the proverbial bag as the creditor pursues its various remedies under state law. If, however, the debtor chooses to file Chapter 13, the bankruptcy code will extend its protection to cover the co-signer. This protection, the co-debtor stay, is unique and integral to Chapter 13 (and its close relation, Chapter 12).

11 U.S.C. § 1301(a) provides, in relevant part, "after the order for relief under this chapter, a creditor may not act, or commence or continue any civil action, to collect all or any part of a consumer debt of the debtor from any individual that is liable on such debt with the debtor, or that secured such debt". In other words, the friends and family who co-signed debts are shielded from collection actions during the pendency of the bankruptcy case.

Although it may appear that the co-debtor stay serves only to benefit the co-obligors, it is, in fact, another form of protection for the debtor. As the legislative history notes, "[a] creditor with a co-signer on a note is often able to use the threat of collection from the co-signer as leverage to obtain preferential treatment from the debtor. Most often, co-signers are relatives, friends, or co-workers of the debtor, who have signed as a favor to the debtor, without a full understanding of their ultimate liability on the debt. The moral pressure brought to bear on the debtor to protect his family or friends gives the creditor a significant advantage over other creditors in a way that is not related to legitimate financial considerations."[12] The legislative history goes on to highlight that the co-debtor stay was "designed only to protect the principal debtor, not the co-debtor. Any protection of the co-debtor is incidental."[13]

To that end, creditors may seek relief from the co-debtor stay. Section 1301(c) provides two important bases for granting relief. A court shall grant relief to the extent that "as between the debtor and the individual protected under subsection (a) of this section, such individual received the consideration for the claim held by such creditor" or to the extent that "the plan filed by the debtor proposes not to pay such claim."[14]

Thus, "[w]hen the chapter 13 debtor is in reality the cosigner on the obligation, a creditor should be granted leave to seek recovery from the party who received the benefit of the

[12] H.R. Rep. No. 95-595, at 121 (1977).
[13] H.R. Rep. No. 95-595, at 123 (1977).
[14] 11 U.S.C. § 1301(c)(1)-(2).

transaction."[15] For example, a creditor is entitled to co-debtor stay relief when the co-debtor, not the debtor, receives proceeds from a jointly signed loan.[16] Additionally, in cases where the debtor does not pay the full amount due to the creditor, the creditor may be awarded stay relief to pursue the co-debtor for the remaining balance of the debt.[17] To protect the co-debtor, the Chapter 13 plan can propose "full payment of the joint obligation and, in appropriate circumstances, by separate classification of co-signed claims for full payment even when the debtor is unable to pay all debts in full."[18] In sum, the co-debtor stay provides additional breathing room for the debtor while he/she endeavors to reorganize and reach a fresh start.

6) **Trustee Oversight of Secured Creditors:** The trustee is in a unique position when it comes to oversight of secured creditors. Such oversight can be in the form of an objection to claim; an objection to a motion for relief from the automatic stay; conduit mortgages, not only maintaining a concise record of post-petition payments made but also the review of post-petition notice of fees and expenses (filing a motion for determination if necessary), review of notice of payment changes (filing a motion to determine if necessary), notice of final cure payment and a determination if necessary; assisting the debtor and creditor(s) in settlement discussions; review of HOA claims and related issues, etc.

- Relief from stay issues: a trustee may file an objection to a secured creditor's motion for relief from stay to raise because: (a) the lien may not be properly perfected; (b) there may be a dispute as to how plan payments made by the trustee have been applied by the creditors; and (c) there may be equity in the property to provide adequate protection of the creditor's interest even if a brief interruption in payments to the creditor.

[15] *In re Ragin*, 249 B.R. 118, 120 (Bankr. D.S.C. 2000) (internal quotation and citation omitted).
[16] *Id.* at 118.
[17] *Southeastern Bank v. Brown*, 266 B.R. 900, 907-08 (S.D. Ga. 2001).
[18] Keith M. Lundin, LUNDIN ON CHAPTER 13, § 65.1, at ¶ 2, LundinOnChapter13.com (last visited Oct. 23, 2020).

- Conduit mortgage issues: if a debtor has incurred pre-petition mortgage arrears it may be in the best interest of the debtor and creditor that not only does the trustee pay the pre-petition arrears but also pays the post-petition mortgage payment for a number of reasons: (a) the trustee will review the proof of claim to ensure that the pre-petition arrears have been properly calculate, including related escrow issues, and that all documentation required by BR 3001 has been provided. (b) The trustee will review all notices of mortgage payment changes filed pursuant to BR 3002.1(b)(1). The two areas that affect changes in the monthly mortgage payment are adjustable rate mortgages and the escrow. Paying particular attention to the post-petition escrow analysis as this is where many problems arise. The creditor must file the notice at least 21 days prior to the effective date. If necessary, the trustee will file a motion to determine whether the change is required pursuant to BR 3002.1(b)(2). If this is a direct pay situation than as trustee, it is my position it is the responsibility of the debtor and debtor's counsel to review the notice and to file any applicable pleading. (c) The trustee will review all notices of post-petition fees, expenses or charges filed pursuant to BR 3002.1(c). Paying particular attention to post-petition attorney fees, late fees, charges such as BPOs (broker's price opinion or sometimes referred to as drive buy valuations), etc. With these notices it is important to remember that all fees, charges and expenses must be incurred post-petition, must be itemized and must be recoverable per the underlying note or nonbankruptcy law. In addition, the fees, charges and expenses sought to be recovered must have been incurred within 180 days prior to the notice. If the fees, expenses or charges where incurred more than 180 days prior to the notice an objection / motion should be filed. It is important to look not just when the creditor paid the fees or expenses requested but when were the fees and expenses billed. For example, attorney fees were incurred more than 180 days prior to the notice but the creditor delayed payment of the invoices – should the debtor be responsible

for paying these fees or should it be an expense borne by the creditor? Are the fees, expenses and charges reasonable? If this is a direct pay situation than as trustee it is my position it is the responsibility of the debtor to pay such fees, expenses and charges and for debtor's counsel to review and file any applicable pleading. (d) The trustee will file a notice of final cure payment pursuant to BR 3002.1(f) within 30 days after a debtor completes all payment under the plan. The purpose of this notice is to put all parties on notice that per the trustee's records all the pre-petition mortgage arrears have been paid, and if a conduit mortgage that all post-petition mortgage payments have been paid and all post-petition fees, expenses and charges have been paid. The creditor shall, pursuant to BR 3002.1(g), file a response to the notice within 21 days after service of the trustee's notice of final cure payment and the creditor must state: (i) the amount to cure any default has been paid; (ii) whether the debtor is current; (iii) if the creditor asserts the debtor is not current must itemize the unpaid amounts due pre-petition and / or post-petition. If it is a conduit mortgage payment the trustee will file a motion to determine the amount due (and perhaps request an accounting) pursuant to BR 3002.1(h). In addition, many trustees who pay conduit mortgages will also file a motion to deem mortgage current just to have an additional order for a debtor to rely on in the event there is post discharge dispute with a creditor. Even in a direct pay situation the trustee can be of assistance to the debtor if the response shows a post-petition default. One, it may be the only way debtor's counsel finds out about the default and can take steps to assist the debtor in a loan modification, an agreement with the creditor to cure the default, or to even discuss filing a new case post discharge to deal with the new mortgage default. Two, the trustee may be able to assist the debtor with reaching a settlement with the creditor to cure the default or if an accounting dispute to obtain records from the creditor. Remember that trustees often have established relationships with servicers and their counsel that debtors and their counsel do not.

- HOA Issues: we have all seen attorney fees and charges that an HOA can incur at the expense of a debtor and often these fees and charges far exceed the default. A trustee may be willing to question the reasonableness of such fees and charges in relation to the actual default and may be able to obtain a reduction in such fees and expenses. Additionally, state law determines when an HOA lien is properly perfected. Almost universally, HOA's believe that any lien automatically attaches through the covenants which run with the land. In several states, a HOA lien does not attach until the recording of a notice of lien with a county recorder and is perfected upon a filed notice or a recorded judgment lien. Several trustees fight improperly perfected HOA liens.

7) **Unperfected Liens (not just a benefit for unsecured creditors):** Why are the trustee's lien avoidance powers under §§544, 545, 547; and the other trustee powers under §§548 and 549 important in chapter 13? Many debtors, creditors, and even judges might believe such action is a waste of time if a reorganizational plan allows debtors to repay the value of that collateral. However, I have seen that the use of these powers can be a benefit not only to unsecured creditors but also the debtor. For example, title loans, which are normally a financial disaster for a debtor, if not properly perfected will allow the debtor to pay the trustee the value of this claim without any interest or fear of an unscrupulous lender taking action against the collateral. As a second example, a debtor purchased a vehicle within 910 days from a secondary or "subprime" dealership paying an inflated price and interest rate The retail installment contract was with recourse, and when the debtor defaulted the dealership had to buy the note back. The original lender filed a proof of claim even though the dealership repurchased the loan pre-petition. The trustee was able to object to the claim on the basis it was tardy and unperfected. Had this case been filed as a Chapter 7, there is little likelihood that the creditor would have even filed a claim and a high likelihood that the debtor would have been required to reaffirm the debt. As long as debtor completes the plan and receives a

discharge, he or she will receive the title with a release of lien and will have paid no interest for the car.

8) **Voluntary Dismissal and Refiling:** absent those extraordinary circumstances involving bad faith I believe trustees understand, support and sometimes encourage the dismissal of a case and a refiling. For most debtors a single event can derail a chapter 13 – loss of a job, illness in the family, a death in the family, a divorce, home or auto repairs, etc. When this occurs sometimes the best option is to dismiss and refile. Of importance is to know when it is the best interest of the debtor to voluntarily dismiss or for a dismissal to be another order of the court, such a trustee's motion to dismiss. When I see a creditor file a motion for relief from stay usually because of a default in plan payments, including direct payments, I will file a motion to dismiss. This step is not taken to punish the debtor but to allow an involuntary dismissal so as to not impede a debtor's ability to refile. §109(g)(2) imposes a 180 day bar to refiling "if the debtor requested and obtained the voluntary dismissal of the case following the filing of a request for relief from the automatic stay …."

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African Americans are paid less than whites at every education level

Average hourly wages, by race and education, 2015

	White	Black
Less than HS	$13.57	$11.25
High school	$18.00	$14.24
Some College	$19.80	$15.85
College	$31.83	$25.77
Advance Degree	$39.82	$33.51

Source: Economic Policy Institute, *State of Working America Data Library*, "Wages by education," 2016