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Debt Adjustment under Chapter 13 of the Bankruptcy Reform Act of 1978 Selected Articles on the Bankruptcy Reform Act of 1978.

Evelyn H. Biery

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DEBT ADJUSTMENT UNDER CHAPTER 13 OF THE BANKRUPTCY REFORM ACT OF 1978

EVELYN H. BIERY*

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I. INTRODUCTION

Under the Bankruptcy Reform Act¹ that took effect October 1, 1979, debtors will have in the new chapter 13 a useful tool for financial rehabilitation.² Debtors³ now able to use 13 will include not only those previously entitled to relief under the related chapter of the Bankruptcy Act, that is, wage earners and commissioned salespersons, but also those newly included within the provisions of the chapter, designated as "individuals with regular income."⁴ Creditors who have in the past ignored chapter XIII because they dealt only with commercial debt will now find themselves facing an unfamiliar debtor relief chapter that gives the debtor considerable control over his or her financial situation. For those unaccustomed to the powers of the bankruptcy court under the old XIII, their introduction to the new 13 will be quite a shock. For those familiar with the old XIII the new provisions will come as no surprise, because the new 13 is merely an enlarged and supercharged version of the old chapter. A debtor invoking the powers afforded by the new debt

1. The Bankruptcy Reform Act of 1978 was enacted by Congress on November 6, 1978 in the form of Public Law 95-598. See Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (to be codified in 11, 28 U.S.C., and scattered other titles). This Reform Act culminates legislative process initiated in 1970 when Congress established the Commission on the Bankruptcy Laws of the United States. See Klein, *The Bankruptcy Reform Act of 1978*, 53 AM. BANKR. L.J. 1, 3 (1979) (synopsis of legislative history, enactment, and transition). The Bankruptcy Reform Act of 1978 repeals the Bankruptcy Act of 1898, as amended by the Chandler Act of 1938, and, with few exceptions, the substantive provisions became effective October 1, 1979. See *id.* at 3. See generally Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, secs. 401-411, 92 Stat. 2682-88 (1978).

In the text of this article the Bankruptcy Reform Act of 1978 will be referred to as the Code. Similarly, the Bankruptcy Act of 1898, as amended by the Chandler Act of 1938, will be referred to as the Act. In footnotes the Bankruptcy Act of 1898, as amended by the Chandler Act of 1938, will be cited in the following form: Bankruptcy Act § ____ (repealed 1978, previously codified as 11 U.S.C. § ____).

2. Under the Bankruptcy Act (repealed 1978, previously codified in 11 U.S.C. and scattered other titles), the chapter was designated by the Roman XIII. Under the Bankruptcy Reform Act (to be codified in 11 U.S.C. and scattered other titles), the chapter will be designated by the Arabic 13. Throughout this article the Bankruptcy Act chapter will be identified by the Roman XIII and the Bankruptcy Reform Act chapter by the Arabic 13.

3. Under the Bankruptcy Act a "bankrupt" was defined as "a person against whom an involuntary petition or an application to revoke a discharge has been filed, or who has filed a voluntary petition, or who has been adjudged a bankrupt." Bankruptcy Act § 1(4) (repealed 1978, previously codified as 11 U.S.C. § 1(4)). The Code has discarded the term "bankrupt," and pursuant to section 101(12), a "debtor" is defined as "any person or municipality concerning which a case under this title has been commenced." 11 U.S.C.A. § 101(12) (West Supp. 1979).

4. See 11 U.S.C.A. § 101(24) (West Supp. 1979).

adjustment chapter⁵ will have every possible opportunity to become financially sound. This article will examine powers now available to a chapter 13 debtor.

As under old chapter XIII the debtor under chapter 13 will be able to avoid interest on unsecured debt,⁶ retain both exempt and nonexempt property, even if collateral for a debt,⁷ restrain collectors' collection efforts,⁸ and pay creditors under a schedule of composition or extension, or both,⁹ whichever satisfies the family's basic financial needs.¹⁰ Under new chapter 13 the debtor clearly will be able to force creditors holding security interests to receive no more than the value of the collateral as secured debt. The balance will be treated as unsecured,¹¹ thereby postponed without interest through an extension plan, reduced through a composition plan, or perhaps reduced and extended through a combination plan.

The debtor may prevent collection efforts directed toward comakers and guarantors of his or her consumer debts, unless the comaker or guarantor "became liable on or secured such debt in the ordinary course of . . . business"¹² The debtor may also have a plan

5. A chapter 13 case will no longer be designated as a "wage earner's case." Rather, it will very likely be designated as a "13 case" or simply a "debt adjustment." The new terminology is dictated by the expansion of chapter 13 relief to individuals other than wage earners.

6. *Compare* Bankruptcy Act § 656 (repealed 1978, previously codified as 11 U.S.C. § 1056) with 11 U.S.C.A. § 502(b)(2) (West Supp. 1979); S. REP. No. 989, 95th Cong., 2d Sess. 63, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5787, 5849. Under the Code chapters 1, 3, and 5 apply to chapter 13 cases. See 11 U.S.C.A. § 103(a) (West Supp. 1979)

7. 11 U.S.C.A. § 1322(b)(2) (West Supp. 1979).

8. *Compare* Bankruptcy Act § 614 (repealed 1978, previously codified as 11 U.S.C. § 1014) with 11 U.S.C.A. § 362 (West Supp. 1979). The provisions of section 362 are discussed at length elsewhere in this volume and are therefore not detailed in this article. See Moller, *Chapter 11 of the 1978 Bankruptcy Code, or Whatever Happened to Good Old Chapter XI?*, 11 ST. MARY'S L.J. 437, 443-46 (1979). See generally BANKR. PROC. R. 13-401.

9. A composition is a reduction of debt, while an extension is merely a postponement of payment without reduction in amount. "[T]he difference is between a proceeding wherein a debtor settles his indebtedness in an agreed amount less than the amount owed and a proceeding wherein he merely obtains an extension of time within which to pay in full." *In re Thompson*, 51 F. Supp. 12, 14 (W.D. Va. 1943). The Code does not specifically state that the plan may provide a composition or extension of claims; however, the legislative history indicates such intent. See H.R. REP. No. 595, 95th Cong., 1st Sess. 118, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6079.

10. See Akard, *Wage Earner Plans Under Chapter XIII of the Bankruptcy Act*, 39 TEX. B.J. 790, 792 (1976).

11. See 11 U.S.C.A. § 506 (West Supp. 1979); H.R. REP. No. 595, 95th Cong., 1st Sess. 124, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6085.

12. 11 U.S.C.A. § 1301(a)(1) (West Supp. 1979). The codebtor stay is not unlimited. If the plan does not provide for payment in full, the creditor may have the stay modified to allow recourse for the difference under a composition plan and possibly even interest under

confirmed without the vote of unsecured creditors that was formerly required under the Bankruptcy Act.¹³ If the chapter 13 debtor proves to the satisfaction of the court that creditors will receive more through the plan than through a chapter 7 liquidation, the plan will be confirmed,¹⁴ and the debtor will thereafter pay his or her debts under a schedule which takes into account the assets, liabilities, income, expense, and physical needs of the family.

II. DEBTOR

The new 13 is available to an individual with regular income whose debts aggregate less than \$100,000 unsecured and less than \$350,000 secured.¹⁵ It is obvious that a case involving debts totalling up to \$450,000 is not necessarily insubstantial, and a large amount of debt will be adjusted under the provisions of 13 once debtors' attorneys are made aware of the vast potential of the new debt adjustment chapter.

Under the Act XIII relief was available only to "an individual whose principal income [was] derived from wages, salary or commissions."¹⁶ Under a strict interpretation of that statute individuals whose principal income was derived from "investments, pensions, social security, or welfare," were often denied relief, as were self-employed persons.¹⁷

New chapter 13 is available to individuals whose income is derived primarily from "investments, pensions, social security, or wel-

an extension plan that provides for payment of principal only. Also, if the debtor can show irreparable harm, such as diminishing prospects for payment from the codebtor, the stay will be modified.

13. Compare Bankruptcy Act §§ 651, 652 (repealed 1978, previously codified as 11 U.S.C. §§ 1051, 1052) with 11 U.S.C.A. § 1325 (West Supp. 1979).

14. See 11 U.S.C.A. § 1325(a)(4) (West Supp. 1979).

15. *Id.* § 109(e).

16. Bankruptcy Act § 606(8) (repealed 1978, previously codified as 11 U.S.C. § 1006(8)).

17. See H.R. REP. No. 595, 95th Cong., 1st Sess. 119, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6080. It is true that some courts did allow chapter XIII plans to be filed by recipients of unemployment benefits, see *In re Wilson*, 1 BANKR. CT. DEC. 670, 672 (D. P.R. 1975), and social security benefits, see *In re Bradford*, 268 F. Supp. 896, 899 (N.D. Ala. 1967). However, the "wage earner" language of the statute led to contradictory holdings. A self-employed carpenter was allowed XIII relief, see *In re Reed*, 368 F. Supp. 615, 617 (E.D. Va. 1968), but a coffee shop proprietor was not, see *In re Fenwick*, No. EV74-394B (S.D. Ind. 1975). All individuals with regular income clearly are entitled to relief under new 13, if their debts do not exceed the limitations of section 109(e). See 11 U.S.C.A. § 101(24) (West Supp. 1979).

fare,"¹⁸ as long as the income is "sufficiently stable and regular to enable such individuals to make payments" under a 13 plan.¹⁹ Even more important is the fact that 13 relief is now available to individual proprietors of small businesses. Congress intended to enable small business proprietors to utilize 13, which is less cumbersome and less expensive than reorganization under the new chapter 11.²⁰

A partnership, regardless of size, is ineligible for chapter 13 relief.²¹ The exclusion of partnerships is especially significant when viewed in the context of joint petitions for spouses. Although an individual with regular income may file a joint petition with his or her spouse²² even though the spouse does not qualify as an individual with regular income,²³ a joint petition may be denied if a creditor proves that the husband and wife are partners in a business.²⁴ Nevertheless, it is likely that a debtor who is also a partner may file if he or she has regular income from a source other than the partnership, since the statute does not specifically exclude partners but instead requires that a person be an individual with regular income.²⁵ It is also likely that a husband and wife can file a joint petition even if they are partners, if one of them has income from another source, since the statute does not exclude "persons" but merely allows only "individuals with regular income" and their spouses to file. The wage earning debtor's eligibility will very likely make the spouse eligible so that both can file even though they are partners.²⁶

18. H.R. REP. NO. 595, 95th Cong., 1st Sess. 119, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5963, 6080.

19. 11 U.S.C.A. § 101(24) (West Supp. 1979).

20. H.R. REP. NO. 595, 95th Cong., 1st Sess. 119, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5963, 6079.

21. *Compare* 11 U.S.C.A. § 109(e) (West Supp. 1979) *and id.* § 101(24) ("individual with regular income" means individual . . .) *with id.* § 101(30) ("person" includes individual, partnership, . . .).

22. Unless the spouse is a stockbroker or commodity broker. *See* 11 U.S.C.A. § 101(24) (West Supp. 1979).

23. *See id.* § 109(e). Under the Act joint petitions were available where the husband and wife were both eligible for relief under chapter XIII, but a noneligible spouse could not file either separately or jointly. *See* Bankruptcy Act § 606(8) (repealed 1978, previously codified as 11 U.S.C. § 1006(8)); BANKR. PROC. R. 13-111(a). *See generally* Reed v. General Fin. Loan Co., 394 F.2d 509, 509 (4th Cir. 1968).

24. H.R. REP. NO. 595, 95th Cong., 1st Sess. 320, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5963, 6277.

25. *See* 11 U.S.C.A. § 109(e) (West Supp. 1979).

26. Neither the Code nor the legislative history addresses the point squarely, but the result is logical, since the Code does not exclude partners as it expressly excludes stockbrokers and commodity brokers. *See* 11 U.S.C.A. §§ 109(e), 101(24) (West Supp. 1979).

There is no limitation on the amount of income that can be earned by the chapter 13 debtor, just as there was no limitation under the Act at the time the Code was enacted.²⁷ There is, however, an occupational restriction. Stockbrokers or commodity brokers are ineligible for chapter 13 relief either as petitioning debtors or as spouses of a petitioning debtor.²⁸ The reason for denying chapter 13 relief to a stockbroker or commodity broker is that chapter 13 does not contain the same protection for customers of the stockbroker or commodity broker as is provided by chapter 7 liquidation²⁹ and presumably chapter 11 reorganization. Whereas the exclusion of partnerships is by inference,³⁰ the exclusion of stockbrokers and commodity brokers is express. A person who is a stockbroker or commodity broker is specifically prohibited from filing or joining in a 13 petition.

Therefore, the rule will probably be that a husband and wife may file a joint petition even if they are partners, or if one is a partner, so long as one of them is an "individual with regular income." Nevertheless, if either is a stockbroker or commodity broker that spouse may not file a 13 petition and they may not file a joint petition.

III. COMMENCEMENT OF THE CASE

As under the Act, a chapter 13 case is initiated by the filing of a petition.³¹ Code provisions regarding the commencement of a chapter 13 case contain no substantive changes but merely a semantic change; the filing of a voluntary petition now constitutes an order for relief.³² It is likely that the distinctions under the Rules will be retained and that the filing of the petition will commence a *case*, rather than a *proceeding*.³³

27. There was previously a limitation on the amount of income which could be earned by a chapter XIII debtor established by chapter XIII of the Chandler Act in 1938. A 1959 amendment eliminated the income limitation for persons seeking XIII relief. See S. REP. NO. 179, 86th Cong., 1st Sess. 1-2, reprinted in [1959] U.S. CODE CONG. & AD. NEWS 1446, 1447.

28. See 11 U.S.C.A. §§ 109(e), 101(24) (West Supp. 1979).

29. See H.R. REP. NO. 595, 95th Cong., 1st Sess. 312, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6269.

30. The inference arises from comparison of the definitions of "person" and "individual with regular income." Compare 11 U.S.C.A. § 101(24) (West Supp. 1979) with *id.* § 101(30).

31. Compare *id.* § 301 with Bankruptcy Act §§ 621, 622 (repealed 1978, previously codified as 11 U.S.C. §§ 1021, 1022) and BANKR. PROC. R. 13-101.

32. See 11 U.S.C.A. § 301 (West Supp. 1979).

33. Compare Bankruptcy Act § 606(6) (repealed 1978, previously codified as 11 U.S.C. § 1006(6)) with Bankruptcy Act § 1(24) (repealed 1978, previously codified as 11 U.S.C. §

As under the Act, the filing of a petition under chapter 13 is voluntary only.³⁴ Likewise, conversion to 13 is purely voluntary.³⁵ Congress recognized the prohibitions of the thirteenth amendment against involuntary servitude and agreed that it would be inadvisable to allow a creditor to force a debtor into a repayment plan.³⁶ If no case is pending under the Code, a voluntary petition may be filed pursuant to section 301. If a petition is pending under one of the other chapters, the case may be converted to chapter 13 pursuant to section 348.³⁷ Under the Act there was of course no provision for conversion from a chapter XI case to chapter XIII, since XI was limited to business arrangements and XIII to wage earner cases. There was, however, a provision for converting from straight bankruptcy to chapter XIII.³⁸ A debtor may now convert from chapter 7 liquidation or chapter 11 reorganization to chapter 13, but only prior to the discharge and only if the case was not previously converted from 7 or 11.³⁹

The Code filing fee for a chapter 13 case is \$60, as compared with \$30 filing fee plus confirmation fee under the Act.⁴⁰ Evidently, only one filing fee will be required for a joint petition. As under the Act, the filing fee may be paid in installments. The debtor will still be

1(24)). A "case" encompassed all matters of controversy and administration arising during the pendency of the case, whereas a "proceeding" was that portion of the case which was adversarial in nature and filed pursuant to the adversary proceeding provisions of the Rules. See BANKR. PROC. R. 101 and Advisory Committee's Note.

34. See 11 U.S.C.A. § 303(a) (West Supp. 1979) ("An involuntary case may be commenced only under chapter 7 or 11 of this title . . .").

35. See *id.* §§ 706(c) (conversion from chapter 7 liquidation), 1112(d)(1) (conversion from chapter 11 reorganization).

36. See S. REP. NO. 989, 95th Cong., 2d Sess. 32, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5787, 5818; H.R. REP. NO. 595, 95th Cong., 1st Sess. 120, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6080.

37. See 11 U.S.C.A. §§ 301, 348 (West Supp. 1979).

38. See BANKR. PROC. R. 13-104, derived from Bankruptcy Act § 622 (repealed 1978, previously codified as 11 U.S.C. § 1022).

39. See 11 U.S.C.A. §§ 706(a), 1112(d) (West Supp. 1979). There has been some speculation that a debtor could receive a chapter 7 discharge and thereby reduce his or her debts to the limitations of chapter 13. Some have theorized that a debtor could receive a discharge of all dischargeable debts in chapter 7 and then seek a chapter 13 extension of only those debts he or she desired to pay, primarily debts secured by household goods. It is the opinion of this writer that a new petition filed under chapter 13 while a chapter 7 case is pending will be treated as a merger of the two petitions and if a discharge has been granted in the chapter 7 case the request for relief under chapter 13 must be denied.

40. Compare 28 U.S.C.A. § 1930(a)(1) (West Supp. 1979) (\$60 per person or couple) with Bankruptcy Act §§ 624(2), 633(2) (repealed 1978, previously codified as 11 U.S.C. §§ 1024(2), 1033(2)) (filing fee plus confirmation fee equals \$30 per person).

required to file for an application for authority to pay the filing fee in installments.⁴¹ If a case is converted from one chapter to another, there is evidently no additional fee.

The conversion to chapter 13 does not effect a change in the date of the filing of the petition. Rather, as under the Act, the rights of creditors in the case are determined as of the date of the initial filing, not the date of conversion.⁴²

IV. CHAPTER 13 PLAN

The Act required that the debtor's plan be filed at the first meeting of creditors or "any adjournment thereof,"⁴³ and the superseding Rule 13-201 provided that the plan be filed with the petition or within ten days thereafter.⁴⁴ For good cause shown the court was authorized to extend the time period.⁴⁵ Under the Code, as under the Act, the plan is to be filed by the debtor.⁴⁶ There is no time limitation in the Code for filing the plan, and the time limit will very likely be established by the Rules soon to be promulgated.

A. *Mandatory Provisions*

1. *Submission of future earnings.* The debtor must include provisions for the submission of all or a portion of his or her future earnings or other future income to the supervision and control of the trustee, to the extent necessary for the execution of the plan. In contrast, under the Act the debtor's earnings were submitted to the control of the court rather than the trustee.⁴⁷ The change of control is consistent with the legislative intent to transfer administrative functions to the trustee under the Code and restrict the court to judicial functions, whenever possible.⁴⁸

41. Compare 28 U.S.C.A. § 1930(a)(1) (West Supp. 1979) with Bankruptcy Act § 624(2) (repealed 1978, previously codified as 11 U.S.C. § 1024(2)). The existing Rules require such an application. BANKR. PROC. R. 13-106(b). The Rules soon to be promulgated will very likely continue the requirement.

42. Compare 11 U.S.C.A. §§ 301, 348 (West Supp. 1979) with BANKR. PROC. R. 13-104 (incorporating Bankruptcy Act § 625 (repealed 1978, previously codified as 11 U.S.C. § 1025)).

43. Bankruptcy Act § 633(2) (repealed 1978, previously codified as 11 U.S.C. § 1033(2)).

44. BANKR. PROC. R. 13-201.

45. See *id.*

46. See 11 U.S.C.A. § 1321 (West Supp. 1979).

47. Compare *id.* § 1322(a)(1) with Bankruptcy Act § 646(4) (repealed 1978, previously codified as 11 U.S.C. § 1046(4)).

48. See H.R. REP. NO. 595, 95th Cong., 1st Sess. 105, reprinted in [1978] U.S. CODE

2. *Payment of priority claims.* The debtor must include provisions for the full payment of all claims entitled to priority under section 507 of the title, in deferred cash payments, unless the claimholder agrees to a different treatment.⁴⁹ The statutory requirement for payment of priority claims in deferred cash payments is new. The Act specifically required the payment of priority claims in advance of general claims.⁵⁰ The new priority deferment provisions of the Code will enable the debtor to make payments to unsecured creditors even before priority creditors are paid in full.

3. *Equal treatment of classified claims.* If the plan classifies claims, it must provide the same treatment for each claim within a class.⁵¹ Under the Act, unsecured creditors were dealt with "generally, upon any terms"⁵² Ordinarily, unsecured creditors were paid on a pro rata or per capita basis, with payments made at regular intervals, usually monthly. Chapter XIII did not specifically authorize a plan to deal with fewer than all unsecured creditors or to divide unsecured creditors into classes and treat the classes in different ways or upon different terms.⁵³ Consequently, some courts applying the Act held that the XIII plan could not classify claims.⁵⁴ Now the debtor may classify claims by amount, paying smaller creditors a larger amount to extinguish their debts earlier in an extension plan, paying smaller creditors a larger percentage than other creditors in a composition plan, or paying various amounts or percentages to various types of creditors based upon the nature of the claims. This type of classification has been prevalent pursuant to chapters X and XI under the Act and will be extremely useful in the business 13 when the debtor wishes to prevent a certain group from contesting the confirmation of the plan. The debtor may treat such dissenting creditors differently and retain the original proposal for the cooperating creditors, so long as the classifications are reasonable, all creditors within the class are treated equally, and the creditors of each class receive more than liquidation value.

CONG. & AD. NEWS 5963, 6066.

49. Compare Bankruptcy Act § 646 (repealed 1978, previously codified as 11 U.S.C. § 1046) with 11 U.S.C.A. § 1322(a)(2) (West Supp. 1979).

50. See Bankruptcy Act § 659(6) (repealed 1978, previously codified as 11 U.S.C. § 1059(6)). See generally *In re Belkin*, 358 F.2d 378, 380 (6th Cir. 1966).

51. See 11 U.S.C.A. § 1322(a)(3) (West Supp. 1979).

52. Bankruptcy Act § 646(1) (repealed 1978, previously codified as 11 U.S.C. § 1046(1)).

53. See 10 COLLIER ON BANKRUPTCY ¶ 28.02, at 272 (14th ed. 1976).

54. See *In re Bailey*, 188 F. Supp. 47, 49 (N.D. Ala. 1960).

B. *Permissive Provisions*

The requirement that creditors of the same class be treated equally relates to the first of the permissive provisions of the plan.⁵⁵ The other permissive provisions include the following:

1. *Modification of secured creditors' rights.* With the exception of the debt secured by the debtor's principal place of residence, the plan may modify the rights of creditors whose claims are secured.⁵⁶ Prior to the enactment of the Code, secured creditors often insisted that in order for a plan to be confirmed it had to provide for preconfirmation curing of default and postconfirmation maintenance of payments in the full installment amounts provided in the contract.⁵⁷ Some courts held that a secured creditor whose claim was modified by a plan could block confirmation simply by refusing to accept the plan.⁵⁸ Other courts allowed debtors to confirm plans over the objections of secured creditors who would receive as much under the plan as under foreclosure and sale of the collateral.⁵⁹ Such decisions generated the present requirement that each secured creditor be treated as secured only to the extent of the value of its collateral.⁶⁰

Debtors may still have difficulty with creditors whose debts are secured by real property which constitutes the debtor's principal residence, since chapter 13 plans cannot be confirmed if they modify the rights of those creditors.⁶¹ However, debtors under the Act were able to confirm plans over the objection of creditors secured by the debtors' residence, even though chapter XIII specifically excluded claims secured by real property.⁶² Some courts held that even though the plan could not provide for payment of the debtor's home loan, the creditor whose debt was secured by a lien on the debtor's

55. The first permissive provision *allows* different classes, whereas the first mandatory provision *requires* that the creditors within a class receive equal treatment. Compare 11 U.S.C.A. § 1322(a)(3) (West Supp. 1979) with *id.* § 1322(b)(1).

56. See *id.* § 1322(b)(2).

57. See, e.g., *Terry v. Colonial Stores Employee's Credit Union*, 411 F.2d 553, 554 (5th Cir. 1969); *In re Pappas*, 216 F. Supp. 819, 822 (S.D. Ohio 1962); *In re O'Dell*, 198 F. Supp. 389, 390-91 (D. Kan. 1961). See generally *Thompson v. Ford Motor Credit Co.*, 475 F.2d 1217, 1219 (5th Cir. 1973); *In re Teegarden*, 330 F. Supp. 1113, 1114 (E.D. Ky. 1971); *In re Willett*, 265 F. Supp. 999, 1004 (S.D. Cal. 1967).

58. See, e.g., *In re Terry*, 294 F. Supp. 253, 254 (S.D. Ga. 1968); *In re Rutledge*, 277 F. Supp. 933, 934 (E.D. Ark. 1967); *In re O'Dell*, 198 F. Supp. 389, 391 (D. Kan. 1961).

59. See *In re Teegarden*, 330 F. Supp. 1113, 1114 (E.D. Ky. 1971).

60. See notes 108-114 *infra* and accompanying text.

61. See 11 U.S.C.A. § 1322(b)(2) (West Supp. 1979).

62. See Bankruptcy Act §§ 606(1), (4), 646(2) (repealed 1978, previously codified as 11 U.S.C. §§ 1006(1), (4), 1046(2)).

home could be stayed from foreclosing, so long as the arrearages were made up over a reasonably short period of time and the current payments were maintained outside the plan.⁶³ Now, only the claims secured by the debtor's principal residence are excluded, and the plan may modify other claims secured by real property.⁶⁴ It is likely that the plan may now, as under previous decisions, provide for, though not modify, the schedule of the current payments and simultaneous payment of the arrearages under a debt secured by a lien on the debtor's principal residence. Thus, though the plan may not *modify* the rights of creditors whose debts are secured by liens on a debtor's principal residence,⁶⁵ it is likely that the cases allowing the debtor to prevent foreclosure while providing for payment of arrearages will continue to be followed, since those decisions held that such action did not materially and adversely affect the rights of the creditors.⁶⁶

2. *Curing or waiving default.* The debtor is allowed to provide in the plan for waiver or curing of any default. There is no language limiting this provision to secured or unsecured debt or debt secured by real or personal property.⁶⁷ The legislative history does not clarify or limit the broad provisions of the subsection 1322(b)(3).⁶⁸ Nor is there any provision limiting the section's purview to pre-filing debt. It is possible, therefore, that the debtor may make arrangements in the plan for curing a default which occurred prior to the filing of the petition, prior to confirmation, or during the performance of the plan. For example, a plan might provide that the default which occurred prior to the filing of the 13 and prior to confirmation might be cured by adding a portion of the arrearages to each of the regular payments to the creditor during the pendency of the plan. It could also provide that any default occurring later might be cured by once again adding delinquent installments to future payments to the

63. See, e.g., *In re Hawks*, 471 F.2d 305, 307 (4th Cir. 1973); *Hallenbeck v. Penn Mut. Life Ins. Co.*, 323 F.2d 566, 573 (4th Cir. 1963); *In re Willett*, 265 F. Supp. 999, 1002-03 (S.D. Cal. 1967).

64. See 11 U.S.C.A. § 1322(b)(2) (West Supp. 1979).

65. See note 64 *supra* and accompanying text.

66. See, e.g., *In re Hawks*, 471 F.2d 305, 307 (4th Cir. 1973); *Hallenbeck v. Penn Mut. Life Ins. Co.*, 323 F.2d 566, 574 (4th Cir. 1963); *In re Willett*, 265 F. Supp. 999, 1002-03 (S.D. Cal. 1967).

67. See 11 U.S.C.A. § 1322(b)(3) (West Supp. 1979).

68. See H.R. REP. NO. 595, 95th Cong., 1st Sess. 429, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6384; S. REP. NO. 989, 95th Cong., 2d Sess. 141, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5787, 5927.

creditor under the plan. If the plan satisfies the requirements for confirmation, it may be confirmed in spite of the fact that specific provision was made for subsequent default.

A provision for the curing of default would be extremely helpful to the debtor whose income was sufficiently stable and regular to have a plan confirmed but was not so stable and regular that payments are guaranteed. If during a season of low income the debtor was forced to skip or reduce a payment under the plan, a provision in the plan for the waiver or postponement of the defaulted payment could prevent the dismissal of the plan for noncompliance. However, the Code makes postconfirmation modification sufficiently easy that the failure to include such a provision in the plan will seldom cause dismissal.⁶⁹

3. *Concurrent payments to secured and unsecured creditors.* Secured creditors have at times objected to receiving payments under chapter XIII plans, claiming that XIII was available only as a vehicle for extension or composition of unsecured debt.⁷⁰ Now creditors, secured or unsecured, may receive concurrent payments under the plan.⁷¹

4. *Payment of long-term mortgage.* Regardless of the fact that the term of a mortgage extends well beyond the term of the plan, the plan may provide for payment of the mortgage installments due prior to or during the pendency of the case.⁷² Thus, even though the payout under the plan may be restricted to three or five years,⁷³ the plan may provide for the curing of default and maintenance of current payments during the payout period. Thereafter, the debtor is evidently required to maintain the future payments as if no plan had been filed.

5. *Payment of postpetition claims.* The debtor may provide that taxes which become due during the pendency of the case or consumer debts arising after the date of the order for relief for property or services necessary for the debtor's performance shall be paid under the plan.⁷⁴ In fact, it is advisable for the debtor to include such a provision. The statute does not clearly indicate whether the debtor may force the postpetition creditor to accept payments under

69. See 11 U.S.C.A. § 1329 (West Supp. 1979).

70. See note 57 *supra*.

71. 11 U.S.C.A. § 1322(b)(4) (West Supp. 1979).

72. See *id.* § 1322(b)(5).

73. See *id.* § 1322(c).

74. *Id.* §§ 1322(b)(6), 1305.

the plan. Rather, the statute speaks in terms of the creditor filing a claim.⁷⁵ It is possible that a creditor who has such a claim may choose not to participate in the plan and insist on the payments it would have received had no plan been filed. However, the claim of a creditor who supplies consumer goods or services will be disallowed if the creditor "knew or should have known that prior approval by the trustee of the debtor's incurring the obligation was practicable and was not obtained."⁷⁶ Since claims arising after an order for relief has been granted may be paid outside the plan, a creditor could conceivably circumvent congressional intent that the trustee approve all credit purchases during pendency of the case. The creditor could simply refrain from filing a proof of claim for payment pursuant to the plan, then demand payment from the debtor outside the plan. It is not clear whether Congress intended that the debtor be free from such creditor demands since neither the Code nor the legislative history specifically indicates such congressional intent.

6. *Assumption or rejection of executory contracts.* As under the Act, debtors under 13 can assume or reject executory contracts—generally, contracts under which both parties have some unperformed obligations.⁷⁷ The power to reject executory contracts has been used most frequently in XIII by debtors who purchased a series of books, encyclopedias, recipe lists, or magazines by mail.⁷⁸

7. *Payment from any property of the debtor.* The plan may provide for the payment of debtor obligations from "property of the estate or property of the debtor"⁷⁹ Although it is not clear, it is likely that property of the estate includes all nonexempt property and property of the debtor includes all exempt property. Under the Act there was a reasonably clear distinction. For example, in *Lockwood v. Exchange Bank*,⁸⁰ the Court held that the bankruptcy court did not have jurisdiction to determine whether the debtor had

75. *See id.* § 1305(a).

76. *Id.* § 1305(c).

77. *See id.* § 1322(b)(7); Countryman, *Executory Contracts in Bankruptcy: Part 1*, 57 MINN. L. REV. 439, 460 (1973).

78. Often, when the debtor rejected the contract, no claim was filed but the service simply cancelled. If the creditor did file a claim the debtor objected to the amount of the claim until the creditor proved the cost of performance and deducted it from the contract price. Since the cost of making such proof was usually prohibitive, the creditor frequently failed to respond to the objection and the claim was disallowed.

79. 11 U.S.C.A. § 1322(b)(8) (West Supp. 1979).

80. 190 U.S. 294 (1903).

waived his homestead exemption, because the homestead was not property of the estate.⁸¹ The legislative history of the Code seems to maintain that distinction when it states that the property listed in section 541 will be property of the estate and the court will determine "what property may be exempted and what *remains* as property of the estate."⁸² The drafters created some confusion when they said that *Lockwood* is now overruled. Nevertheless, the legislative history and the Code provisions are not inconsistent if *Lockwood* is overruled only to the extent it held the bankruptcy court did not have jurisdiction to determine the dispute and not overruled to the extent it held the exempted property was not part of the estate. Thus, under the Code, once property is set aside as exempt it is no longer property of the estate. The bankruptcy court can now determine disputes concerning the exempted property, and a 13 debtor may use that property to fund a plan.⁸³

8. *Vesting of property.* If the debtor chooses to have the property of the estate vest in someone else upon confirmation or at some later date, the plan may so provide.⁸⁴

C. *Modification*

Under the Act, a plan could be modified any time prior to confirmation, and the debtor could obtain advance acceptance of the modification from creditors.⁸⁵ If the court found that the modification did not materially and adversely affect any creditor who accepted the plan, either in writing or by silence, the court could approve the modification.⁸⁶ Otherwise the court could order that the plan as modified would be deemed accepted by any creditor failing to reject the modification within a reasonable period of time fixed by the court. If any creditor objected, the court would hold a hearing

81. *See id.* at 300.

82. H.R. REP. No. 595, 95th Cong., 1st Sess. 368, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5963, 6324 (emphasis added).

83. This interpretation is consistent with other parts of the Code, since the Code does not specifically exclude exempt property from the estate and contains specific provisions for delivery of exempt property to the trustee. Section 542(a) provides that "an entity . . . in possession, custody, or control . . . of property . . . that the debtor may exempt under § 522 of this title, shall deliver to the trustee, and account for, such property or the value of such property . . ." 11 U.S.C.A. § 542(a) (West Supp. 1979).

84. *See id.* § 1322(b)(9).

85. BANKR. PROC. R. 13-212, 13-202(a).

86. V. COUNTRYMAN, *BANKRUPTCY AND THE CHAPTER PROCEEDINGS* 280 (G. Holmes ed. 1976).

to determine whether the objecting creditor was materially and adversely affected by the modification.⁸⁷

The Code allows modification of a plan by the debtor at any time prior to confirmation provided the modification complies with the mandatory and permissive provisions for a plan.⁸⁸ The plan as modified becomes "the plan" upon the filing of the modification.⁸⁹ Secured claimholders who have accepted or rejected the plan are deemed to have accepted or rejected the preconfirmation modification unless the modification provides for a change in the rights of such holder. If there is a change, the holder's original acceptance or rejection will govern unless the claimholder specifically changes its acceptance or rejection.⁹⁰

The Act required that the plan itself provide for modification during the plan period to increase or reduce the amount of any of the installment payments under the plan.⁹¹ Rule 13-214 allowed the court to increase or reduce the amount of or extend or shorten the time for such payments, or otherwise modify the confirmation or payment order, but only after a hearing following notice to such persons as the court designated.⁹² The Code section is virtually identical to Rule 13-214(a), except that there is no provision for notice. The plan may be modified after confirmation to:

- (1) increase or reduce payments on claims of a particular class;⁹³
- (2) extend or reduce the time for such payments; or
- (3) alter payments to a creditor provided for under the plan to account for any payment on the claim from some source other than the plan.⁹⁴

Presumably the rules soon to be promulgated will provide for notice to the claimholder whose rights are changed by the modification, and the claimholder will thereby be given an opportunity to withdraw or alter the previous acceptance or rejection. Postconfirmation

87. *Id.* at 281.

88. *See* 11 U.S.C.A. § 1323(a) (West Supp. 1979).

89. *Id.* § 1323(b).

90. *See id.* § 1323(c).

91. *See* Bankruptcy Act § 646(5) (repealed 1978, previously codified as 11 U.S.C. § 1046(5)).

92. BANKR. PROC. R. 13-214(a).

93. The increase or reduction cannot discriminate within the class. *See* 11 U.S.C.A. § 1322(a)(3) (West Supp. 1979).

94. *Id.* § 1329(a).

modification of the plan is available until all payments provided for by the plan are completed.⁹⁵

D. *Payout Period*

The time for payment under the plan is now specifically limited. "The plan may not provide for payments over a period that is longer than three years, unless the court, for cause, approves a longer period" up to five years.⁹⁶ The time limit is a compromise between the five-year limit in the House bill and the four-year limit in the Senate bill.⁹⁷ Although the Act did not contain a three-year maximum payout period, in practice some courts would not approve a plan with a longer payout period⁹⁸ because the debtor could seek a discharge of all dischargeable debts three years after confirmation if the court found that failure to comply with the plan was not the fault of the debtor.⁹⁹ Under the Code the debtor can receive a discharge before paying all plan payments, even before three years have elapsed.¹⁰⁰

E. *Confirmation*

The Code requires the court to confirm a plan if six requirements are met:

- (a) the plan complies with chapter 13 and title 11 provisions;
- (b) any fees required to be paid have been paid;
- (c) the plan has been proposed in good faith and not by any means forbidden by law;
- (d) the value, as of the effective date of the plan, of property to be distributed to each unsecured creditor is not less than the amount that would have been paid on such claim if the estate of the debtor were liquidated under chapter 7 of title 11;
- (e) with respect to each allowed secured claim:
 - (i) the holder of such claim has accepted the plan;

95. *See id.* § 1329(a).

96. *Id.* § 1322(c).

97. Statement by Hon. Don Edwards, Chairman of the Subcommittee on Civil and Constitutional Rights of the House Committee on the Judiciary, upon introducing the House Amendment to the Senate Amendment to H.R. 8200, 124 CONG. REC. H11,089 (daily ed. Sept. 28, 1978), reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6481.

98. *See* L. HERZ, L. KING, E. BANDER, 3 COLLIER PAMPHLET EDITION 610 (1979 ed.).

99. *See* Bankruptcy Act § 661 (repealed 1978, previously codified as 11 U.S.C. § 1061).

100. *See* 11 U.S.C.A. § 1328(b) (West Supp. 1979).

- (ii) (A) the plan provides for retention of a lien by such holder; and (B) the value of property to be distributed on account of such plan is not less than the allowed amount of such claim; or
- (iii) the debtor surrenders the property to the lien holder; and
- (f) the debtor will be able to comply with the plan.¹⁰¹

The most substantial change in section 1325 is the removal of unsecured creditor acceptance of the plan. The Act required that a majority of unsecured creditors holding a majority in amount of the filed and allowed claims accept the plan.¹⁰² Creditors whose claims were to be paid in full in cash upon confirmation were considered not materially and adversely affected, and their acceptance therefore was not required. Those who voted were only those creditors materially and adversely affected by the plan.¹⁰³ The requirement for creditor acceptance seldom prevented confirmation of a XIII plan, since a sufficient number of unsecured creditors generally accepted the plan although their claims were reduced or extended.¹⁰⁴

The Code, however, has no requirement that unsecured creditors accept the plan. Instead, as to unsecured creditors, it requires only that the debtor satisfy the "best interests of creditors" rule. In other words, "the value, as of the effective date of the plan, of property to be distributed" to unsecured creditors must be not less than what they would have received had the debtor proceeded to liquidation under chapter 7.¹⁰⁵ Very often that test will be satisfied regardless of the amount of payments or length of the payout period, since unsecured creditors generally receive no distribution in liquidation cases.

Under the Act problems involving creditor consent arose more often with respect to secured creditors, and the greatest area of dispute under the Code will continue to be whether the plan can be confirmed over the objection of secured creditors. Some courts under the Act gave secured creditors absolute veto power over the plan, so that plans could be confirmed only if all secured creditors

101. *Id.* § 1325.

102. See Bankruptcy Act §§ 651, 652 (repealed 1978, previously codified as 11 U.S.C. §§ 1051, 1052).

103. See *In re Dunn*, 251 F. Supp. 637, 641 (M.D. Ga. 1966).

104. Meth, *Making Wage Earner Proceedings More Effective*, 80 COMM. L.J. 14, 15 (1975).

105. 11 U.S.C.A. § 1325(a)(4) (West Supp. 1979).

accepted the plan or received their contractual payments.¹⁰⁶ Other courts determined that a secured creditor was not materially and adversely affected if it received the value of its collateral.¹⁰⁷

Those courts relegated secured creditors to the true value of their collateral and deprived them of the emotional control they once exerted over debtors through the attachment of debtors' personal property. Many debtors faced with losing collateral of a relatively small value in comparison with the debt it secured would pay the debt, in spite of the economic disadvantage. The drafters of the Code attempted to ensure the debtors would be relieved of that pressure.¹⁰⁸ Under the Code the debtor may choose optional methods for treating secured creditors who do not accept the plan. If a secured creditor does not accept the plan the debtor must "with respect to each allowed secured claim"¹⁰⁹ (a) allow the creditor to retain its lien and distribute to that creditor under the plan property of a value not less than the allowed amount of such claim¹¹⁰ or (b) surrender the property to the creditor.¹¹¹

A secured creditor may try to interpret the "allowed amount of such claim" requirement to mean that it must be paid the entire amount of its claim, as a secured claim regardless of the value of the collateral. However, the value of the secured claim is the value of the collateral securing the claim, and the remainder of the claim

106. See, e.g., *Terry v. Colonial Stores Employee's Credit Union*, 411 F.2d 553, 554 (5th Cir. 1969); *In re Rutledge*, 277 F. Supp. 933, 934 (E.D. Ark. 1967); *In re Pappas*, 216 F. Supp. 819, 822 (S.D. Ohio 1962).

107. See *In re Teegarden*, 330 F. Supp. 1113, 1114 (E.D. Ky. 1971). See generally *Thompson v. Ford Motor Credit Co.*, 475 F.2d 1217, 1219 (5th Cir. 1973). To be treated as a secured creditor under the plan, however, it was necessary for the creditor to file its claim prior to the conclusion of the first meeting of creditors. BANKR. PROC. R. 13-302(e)(1). The creditor who failed to file the appropriate documents on time was often treated as unsecured. As a result the court refused to allow the creditor to recover the collateral or receive any more than the pro rata or per capita share the creditor would have received had it originally been an unsecured creditor.

108. See H.R. REP. NO. 595, 95th Cong., 1st Sess. 124, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6085. In 1976 the drafters of the Rules of Bankruptcy Procedure attempted to alleviate the problem through Rule 13-307(d), which provided for the valuation of the collateral and the treatment of the claim as secured to the extent of the value of the collateral, with the balance being treated as unsecured. See *Countryman, Partially Secured Creditors Under Chapter XIII*, 50 AM. BANKR. L.J. 269, 272 (1976). Still, many courts refused to recognize the Rule since they considered it inapplicable, ambiguous, or invalid because inconsistent with the Act. See *id.* at 274-80.

109. 11 U.S.C.A. § 1325(a)(5) (West Supp. 1979).

110. *Id.* § 1325(a)(5)(B) (emphasis added).

111. *Id.* § 1325(a)(5)(C).

is treated as unsecured throughout the Code.¹¹² The claim should therefore be divided into an allowed secured claim, equal to the value of the collateral, and an allowed unsecured claim equal to the balance of the total claim. The test will probably not be satisfied merely by paying the value of the collateral over a period of years without interest, since in these inflationary times the value over a period of years would not equal the value of the collateral "as of the effective date of the plan."¹¹³ The debtor's attorney may be required to become familiar with discount factors to prove that the present value of the payments to the creditor on the allowed secured claim has a present value equal to the present value of the collateral. In addition, the interest rate on the present value may exceed the contract interest rate, if the rate is below the market rate.¹¹⁴ The debtor will therefore retain his or her collateral so long as he or she pays to the creditor the actual value, though over a period of months or years. This method of payment will prevent any prejudice against the debtor resulting from the loss of property to which he or she has become emotionally attached.

Under the Act, debtors' attorneys sometimes accomplished the same result by submitting plans providing that the secured property or the value of the secured property, with interest, would be distributed under the plan to nonconsenting secured creditors. The plan was thereby subject to confirmation, in spite of secured creditors' objections, without the need to amend or delete provisions for nonconsenting secured creditors.¹¹⁵ Debtors' attorneys will now have statutory authority for the type of plan in which the creditor may choose to accept or be forced to accept the true value of the collateral, and secured creditors will no longer be able to block confirmation for failure to provide the full contract payments.

F. *Objection to Confirmation*

Under the Code any party in interest may object to confirmation

112. *Id.* § 506(a). See generally S. REP. NO. 989, 95th Cong., 2d Sess. 68, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5787, 5854. "Throughout the bill, references to secured claims are only to the claim determined to be secured under this subsection, and not to the full amount of the creditor's claim." *Id.* at 68, reprinted in [1978] U.S. CODE CONG. & AD. NEWS at 5854.

113. 11 U.S.C.A. § 1325(a)(5)(B)(ii) (West Supp. 1979).

114. See generally Klee, *All You Ever Wanted To Know About Cram Down Under the New Bankruptcy Code*, 53 AM. BANKR. L.J. 133, 140-46 (1979).

115. See *Cheetham v. Universal C.I.T. Credit Corp.*, 390 F.2d 234, 237 (1st Cir. 1968).

of the plan at the confirmation hearing.¹¹⁶ Objection to confirmation must be distinguished from rejection of the plan.¹¹⁷ Objection to confirmation is based on failure of the plan to conform to the requirements of chapter 13, such as failure of the plan to incorporate one of the mandatory provisions required by section 1322(a).¹¹⁸ Conversely, a rejection of the plan pursuant to the Act constituted a mere vote against the plan. Since there is no voting by creditors under new chapter 13, there will very likely be no rejections, only objections to confirmation. The standards governing confirmation of a modified plan are the same standards for original plan and preconfirmation modification, dictating that the modified plan comply with the mandatory and permissive provisions of section 1322.¹¹⁹

Under the Act confirmation of a plan could be revoked,¹²⁰ but revocation for fraud very likely never occurred.¹²¹ Under the Code "[o]n request of a party in interest at any time within 180 days after the date of the entry of an order of confirmation . . . , and after notice and a hearing, the court may revoke such order if such order was procured by fraud."¹²² If the court revokes the order of confirmation pursuant to section 1330(a), it must then either dispose of the case under section 1307, by converting to a chapter 7 case or dismissing with prejudice, or it must confirm a new plan proposed by the debtor.¹²³ A confirmed plan binds both consenting and nonconsenting unsecured creditors, as it did under the Act. The Code provides that "[t]he provisions of a confirmed plan bind the debtor and each creditor," regardless of whether the creditor's claim is provided for by the plan, and regardless of whether the creditor objected to, accepted, or rejected the plan.¹²⁴

Unless the plan or confirmation order states otherwise, confirmation vests all property of the estate in the debtor free of any claim

116. 11 U.S.C.A. § 1324 (West Supp. 1979).

117. S. REP. No. 989, 95th Cong., 2d Sess. 142, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5787, 5928.

118. See 11 U.S.C.A. § 1322(a) (West Supp. 1979).

119. See *id.* § 1329(b)(1). See notes 47-84 *supra* and accompanying text.

120. "Any party in interest may, at any time within six months after a plan has been confirmed, file a complaint pursuant to the Act to revoke the confirmation as procured by fraud." BANKR. PROC. R. 13-214(b).

121. V. COUNTRYMAN, BANKRUPTCY AND THE CHAPTER PROCEEDINGS 281 (G. Holmes ed. 1976).

122. 11 U.S.C.A. § 1330(a) (West Supp. 1979).

123. See *id.* § 1330(b).

124. *Id.* § 1327(a).

or interest of any creditor provided for by the plan.¹²⁵ Confirmation therefore binds secured creditors whose claims are dealt with according to one of the alternative methods set forth above, since the confirmation order entails a finding that the creditor's claim is properly handled under the plan. Confirmation also binds the secured creditor whose claim is not provided for in the plan.¹²⁶

V. DISCHARGE

Where the debtor has successfully completed all payments under the plan the court is required to grant a discharge unless the debtor waives the discharge under a written waiver approved by the court. Excepted from the discharge are: (1) debts upon which the last payment is to be made after the expiration of the due date of the final payment under the plan, generally, those more than three years after confirmation,¹²⁷ and (2) obligations for alimony, support, or maintenance payments.¹²⁸

Even if all payments under the plan have not been made the court may grant a "hardship" discharge to a debtor any time after confirmation of the plan, if the following three requirements are met:

- (1) the failure to make payments is due to circumstances beyond the control of the debtor;
- (2) the value, as of the date of the plan confirmation, of property actually distributed on account of unsecured claims is not less than the claimholders would have received under chapter 7 liquidation; and
- (3) modification of the plan is impracticable.¹²⁹

A hardship discharge under subsection (b) discharges a debtor from all unsecured debts provided for by the plan and all disallowed debts, except:

- (1) debts under 1322(b)(5): long-term debt, such as mortgage debt, upon which payments extend past the term of the plan; and
- (2) debts of the kind specified in 523(a) including nondischargeable debts;

125. *Id.* § 1327(b), (c).

126. *Id.* § 1327(a).

127. *See id.* § 1322(b)(5).

128. *Id.* §§ 523(a)(5), 1322(b)(5), 1328(a).

129. *Id.* § 1328(b).

- (i) certain taxes or customs duties;
- (ii) money, credit or refinancing obtained by false financial representations;
- (iii) debts neither listed nor scheduled;
- (iv) debts for fraud, defalcation in fiduciary capacity, embezzlement or larceny;
- (v) obligations for support, alimony or maintenance;
- (vi) debts for willful or malicious injury to an entity or property of an entity;
- (vii) fine, penalty, or forfeiture due a governmental unit;
- (viii) certain debts for educational loans;
- (ix) certain debts which were or could have been listed in a prior bankruptcy.¹³⁰

Thus a "hardship" discharge leaves the debtor liable for all debts that would have been nondischargeable in a chapter 7 liquidation, whereas a "payment completed" discharge relieves the debtor of all debts except obligations for support, alimony, or maintenance, even if the debtor has paid less than 100% of the debts otherwise nondischargeable.

A discharge under section 1328 discharges all debts provided for by the plan, but it does not discharge a postpetition debt specified in section 1305(a)(2) if prior approval of the trustee for incurring the debt was practicable and available but not obtained.¹³¹ Other debts arising after the filing of the chapter 13 proceeding will evidently be discharged if they are provided for in the plan. Therefore a debtor possibly should provide in the plan for incurring postpetition debt on approval of the trustee. That precaution will insure that the debt will be discharged if the debtor fails to maintain plan payments.

A debtor who has failed to complete the plan payments will have little difficulty deciding whether to seek a "hardship" discharge under section 1328(c), convert to chapter 7 liquidation, or dismiss the 13 case and immediately file a chapter 7 case. The debtor dismissing the chapter 13 petition and filing a new petition pursuant to chapter 7 receives a discharge under section 727(a)(9), which is only the limited "hardship" discharge of section 1328(c). Under section 727(a)(9) a debtor will not receive a discharge if he or she has previously received a discharge under section 1328(a) or (b) in a case commenced within six years before the chapter 7 case,

130. *Id.* §§ 1328(c), 523.

131. *See id.* § 1328(d).

unless the unsecured creditors received 100% of their claims¹³² or at least 70% of their claims and the plan was proposed in good faith and represented the debtor's best effort.¹³³ A discharge may be revoked for fraud within one year of the date of discharge if knowledge of the fraud is obtained by the objecting party after the discharge was granted.¹³⁴

VI. TRUSTEE

Under the Act, the bankruptcy judge could appoint, when feasible, one or more standing trustees to whom all chapter XIII cases were to be assigned without further order.¹³⁵ Where there were no standing trustees, or where the bankruptcy court for some reason found it expedient to do so, it could appoint an individual trustee at or prior to the confirmation of the plan.¹³⁶ Both types of trustees qualified by filing, within five days of their appointment, a bond set by the bankruptcy judge.¹³⁷ Subsection (e) of Rule 13-205 provided for a proceeding on the bond of a trustee by a party in interest prior to two years from date of discharge of the trustee in the case.¹³⁸ The chapter XIII trustee was eligible if he or she:

- (1) had no interest adverse to the estate;
- (2) was competent to perform the duties of the trustee; and
- (3) had an office or residence in the state where the court sat or in an adjacent state.¹³⁹

Experience with chapter XIII proved that the most successful plans were those conducted by standing trustees, because they became adept at the design and mechanics of chapter XIII plans and exercised a broad range of responsibilities under the plan.¹⁴⁰ As a result, the system was continued in the Code with little change.¹⁴¹

132. This could result from an extension under chapter 13 followed by a chapter 7 liquidation.

133. This could occur from a composition or unfulfilled extension pursuant to chapter 13 followed by a chapter 7 liquidation.

134. See 11 U.S.C.A. § 1328(e) (West Supp. 1979).

135. BANKR. PROC. R. 13-205(a)(1).

136. BANKR. PROC. R. 13-205(b)(1).

137. BANKR. PROC. R. 13-205(a)(2), (b)(1).

138. BANKR. PROC. R. 13-205(e).

139. BANKR. PROC. R. 13-205(d).

140. S. REP. NO. 989, 95th Cong., 2d Sess. 139, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5787, 5925.

141. Compare 11 U.S.C.A. § 1302(a) (West Supp. 1979) with BANKR. PROC. R. 13-205.

The bankruptcy judge may now appoint an individual from a panel of private trustees maintained by the Administrative Office of the United States Courts.¹⁴² The Director of the Administrative Office names individuals to serve on the panel. The number and qualifications of panel members are to be determined by rules and regulations established by the Director, and the Director may at any time remove an individual or corporation from the panel for cause. A corporation may be a trustee if its charter authorizes it to act as such.¹⁴³ This provision comports with the intent of Congress to facilitate administration of chapter XIII plans and impress more administrative duties on the trustee rather than the judge.¹⁴⁴ The Code requires that the individual reside in or have an office in the judicial district where the case is pending or in an adjacent judicial district.¹⁴⁵ The trustee must also within five days of selection post a bond set by the court conditioned upon faithful performance of his or her duties.¹⁴⁶ No bond is required of the United States Trustee if he or she is serving as trustee.¹⁴⁷ In the eighteen judicial districts of the pilot program of United States Trustees, the U.S. Trustee may serve as the chapter 13 trustee or appoint another as trustee.¹⁴⁸

The chapter 13 trustee has all the duties of a trustee under chapter 7 liquidation, including the duty to:

- (1) account for all the property of the estate;
- (2) investigate the financial affairs of the debtor;
- (3) object to the allowance of any improper claim;
- (4) oppose the discharge of the debtor, if advisable;
- (5) furnish information concerning the estate and its administration to interested parties, unless the court orders otherwise; and
- (6) make a final accounting and report of the administration of the estate to the court.¹⁴⁹

In addition the trustee is to appear at any hearing that concerns the value of property subject to a lien, confirmation of the plan, or

142. 11 U.S.C.A. § 1302(a) (West Supp. 1979).

143. *See id.* § 604(f).

144. H.R. REP. No. 595, 95th Cong., 1st Sess. 105, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5963, 6066.

145. 11 U.S.C.A. § 321 (West Supp. 1979).

146. *Id.* § 322.

147. *Id.* § 151302.

148. *Id.* § 151302.

149. *Id.* § 704.

postconfirmation modification of the plan. It is also the trustee's duty to advise and assist the debtor in performance under the plan concerning nonlegal matters.¹⁵⁰ Advising the debtor how to set up the plan and perform under it is not a legal matter, but the debtor's attorney will frequently perform these functions.¹⁵¹

Under the Act the trustee was not required to assist the debtor. He or she was only required to:

- (1) file a complete inventory of the property of the debtor;
- (2) keep a record of all receipts and disbursements;
- (3) file with the court notice of creditors' address;
- (4) furnish information concerning the estate and its administration when requested by an interested party, unless the court ordered otherwise; and
- (5) file a final accounting and report.¹⁵²

Nevertheless, chapter XIII trustees counselled debtors on their budgets and encouraged them to adjust expenses to meet their available funds.

Under chapter 13 trustees will have even greater responsibilities and opportunities to assist debtors. The enlargement of the class of eligible chapter 13 debtors to include business proprietors¹⁵³ has caused an expansion of the trustee's duties. If the debtor is engaged in business, the trustee must investigate the debtor's financial condition, the operation of his or her business and the desirability of the continuation of that business, and supervise the reporting of that information to the court and creditors.¹⁵⁴ The chapter 13 trustee operating a business may now use, sell, or lease any property of the estate in the ordinary course of business without notice and hearing.¹⁵⁵ Nevertheless, only the debtor may use, sell, or lease property outside the ordinary course of business and only after notice and hearing appropriate to the circumstances.¹⁵⁶

The trustee is also authorized to obtain unsecured credit and

150. *Id.* § 1302(b)(2), (3).

151. H.R. REP. NO. 595, 95th Cong., 1st Sess. 427, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6382.

152. Bankruptcy Act §§ 47(a), 49 (repealed 1978, previously codified as 11 U.S.C. §§ 75(a), 77); BANKR. PROC. R. 13-208.

153. H.R. REP. NO. 595, 95th Cong., 1st Sess. 119, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6079.

154. See 11 U.S.C.A. §§ 1106(a)(3), (4), 1302(c) (West Supp. 1979).

155. *Id.* §§ 363(c), 1304(b).

156. See *id.* §§ 102(1), 363(b), 1303.

incur unsecured debt in the ordinary course of business as an administrative expense under section 503(b)(1), unless the court orders otherwise.¹⁵⁷ The trustee may be authorized by the court, after notice and hearing, to obtain unsecured credit for administrative expenses other than in the ordinary course of business¹⁵⁸ or to obtain secured credit.¹⁵⁹ Nevertheless, it is not necessary that the trustee operate the business. The debtor may operate the business, subject to the rights, powers, and limitations of a trustee and any further limitations prescribed by the court.¹⁶⁰ Though the debtor has the powers of the trustee under sections 363(c) and 364, the Code does not transfer to the debtor power to assume or reject executory contracts or unexpired leases outside the plan, nor the power to avoid transfers and recover property for the estate.¹⁶¹ Evidently those powers remain in the trustee even while the debtor operates the business. The debtor operating his or her business must file with the court certain financial statements relating to the operation and taxation of the business.¹⁶²

VII. CONVERSION OR DISMISSAL

Under the Act the court was required to dismiss the case or convert it to straight bankruptcy upon application of the debtor at any time prior to confirmation. If the debtor failed to pay any installment of the filing fee or failed to prosecute the case, it was to be dismissed or converted to bankruptcy following notice to the debtor and a hearing.¹⁶³ Failure to prosecute included failure to file a chapter XIII statement, failure to propose a plan, the withdrawal or abandonment of a plan, or failure to make any deposit required by the plan.¹⁶⁴ The debtor could dismiss the case or convert to bankruptcy at any time after confirmation as well.¹⁶⁵

157. *Id.* § 364(a).

158. *Id.* § 364(b).

159. *Id.* § 363(c), (d).

160. *See id.* § 1304(b).

161. *See id.* §§ 363(c), 364.

162. *Id.* § 1304(c).

163. Bankruptcy Act § 666 (repealed 1978, previously codified as 11 U.S.C. § 1066); BANKR. PROC. R. 13-112.

164. A. MOLLER, L. KING, E. BANDER, 2 COLLIER PAMPHLET EDITION 751 (1979 ed.) (Advisory Committee's Note to Rule 13-112); *see* Bankruptcy Act § 666 (repealed 1978, previously codified as 11 U.S.C. § 1066).

165. BANKR. PROC. R. 13-215; Bankruptcy Act § 666 (repealed 1978, previously codified as 11 U.S.C. § 1066).

The Rules allowed the court to dismiss the case or adjudicate the debtor a bankrupt if the case was commenced by an original petition and if confirmation had been revoked for fraud on the part of the debtor. Where there was no fraud in an original petition case, the court could dismiss the case or adjudicate the debtor a bankrupt, with his or her written consent. If the petition had been filed in a pending bankruptcy case, the court was authorized to enter an order directing that the bankruptcy case proceed.¹⁶⁶

The Code gives the debtor an absolute right to convert the chapter 13 case to a liquidation case or have the chapter 13 case dismissed at any time, and purported waiver of either of these rights is unenforceable.¹⁶⁷ The Code further affords the court power to convert the case for cause to chapter 7 or dismiss the case, whichever best serves the interests of creditors and the estate.¹⁶⁸ The conditions allowing the court to exercise its power to convert or dismiss include: unreasonable delay by the debtor that is prejudicial to creditors, nonpayment of any fees or charges required, failure to propose a plan, denial of confirmation, material default under the plan, revocation of the confirmation order, denial of confirmation of a modified plan, or termination of a confirmed plan due to a specified condition in the plan.¹⁶⁹

On request of a party in interest, before confirmation and after notice and a hearing, the court may convert a chapter 13 case to a case under chapter 11.¹⁷⁰ The drafters of the Code determined that there might be some cases in which the creditors would be better protected or the debtor might receive more complete relief from financial distress under chapter 11. The court is to consider factors such as the nature of the debtor's business and exercise discretion in determining whether to force an involuntary conversion to chapter 11.¹⁷¹

166. BANKR. PROC. R. 13-215.

167. 11 U.S.C.A. § 1307(a), (b) (West Supp. 1979); *see* S. REP. No. 989, 95th Cong., 2d Sess. 141, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5787, 5927.

168. 11 U.S.C.A. § 1307(c) (West Supp. 1979).

169. *See id.*

170. Since chapter XI was unavailable to wage earners, there was no similar provision under the Act. The new provision is required by the fact that 13 has been extended to business proprietors. *See* H.R. REP. No. 595, 95th Cong., 1st Sess. 119, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5963, 6079.

171. H.R. REP. No. 595, 95th Cong., 1st Sess. 428, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5963, 6384.

VIII. CONCLUSION

Without doubt chapter 13 provides considerable relief for debtors. Subject to certain occupation and debt limitations, individuals and small business proprietors and their spouses may file under that chapter, no matter what their income, so long as their debts do not exceed certain limitations. Debtors may propose a plan extending payments to creditors over a three-year period, and even up to a five-year period with the approval of the bankruptcy judge. During that period debtors need not pay that portion of their debts not otherwise becoming due before expiration of the plan.

Debtors may pay unsecured creditors simultaneously with priority claimants. They may divide unsecured creditors into classes, providing, for example, a larger percentage for each small unsecured claim than for each large unsecured claim. Chapter 13 debtors need not pay either secured or unsecured creditors more than such creditors would have received under liquidation. Therefore, debtors may substantially reduce their total debt while retaining all of their property and paying creditors little more than the total value of that property. Since the automatic stay provisions of the Code will effectively freeze all actions against debtors as well as their codebtors or guarantors on consumer debts, debtors now can satisfy the maximum possible portion of their debts during the term of the plan. Zealous debtors may utilize chapter 13 to extinguish a substantial portion of their debts, while those debtors more concerned with retention of their property may pay a smaller, perhaps even miniscule, portion of their debts.

Debtors engaged in business will be able to pay their debts at an affordable rate, in a much less complex and less expensive proceeding than that provided by chapter 11 since chapter 13 requires merely a determination of liquidation value. Conversely, chapter 11 provides rigid creditor acceptance rules and complex cram down provisions which often require determination of going concern value. In fact, the chapter 11 requirements are so burdensome that Judge Moller has stated, "In all probability only strong businesses can survive the process."¹⁷² The chapter 13 debtor can utilize many of the favorable provisions of chapter 11 while avoiding many of the problems. The chapter 13 debtor need not be concerned that a trustee will be appointed because the debtor is operating the busi-

172. Moller, *Chapter 11 of the 1978 Bankruptcy Code or Whatever Happened to Good Old Chapter XI?*, 11 ST. MARY'S L.J. 437, 438 (1979).

ness, since a trustee is appointed in all cases. The chapter 11 debtor on the other hand fears the appointment of a trustee because the appointment effects automatic change of management and terminates the debtor's exclusive right to file a plan. Chapter 13 allows only the debtor to file a plan and thereby eliminates any possibility of the creditors filing a burdensome plan. Nor is there a creditors' committee with the attendant expense and burden of negotiations, and the debtor need not submit the disclosure statement required under chapter 11.

Since there will be fewer matters to negotiate and litigate, the period of time between filing and confirmation in a chapter 13 case should be much shorter than in a chapter 11 case. Litigation concerning the use and sale of collateral may therefore be diminished. Accordingly, the debtor should be able to pay a larger portion of the claims over a shorter period of time by filing under chapter 13 rather than chapter 11. The simple, direct, expeditious relief available pursuant to chapter 13 is, however, subject to abuse. The courts must carefully exercise close supervision and control to insure the debtor has filed the petition and plan in good faith. If courts exercise their discretion wisely, dismissing plans not filed in good faith, chapter 13 provides an excellent vehicle for debtor relief without prejudice to creditors.