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BANKRUPTCY REFORM: RELIEF FOR INDIVIDUALS WITH REGULAR INCOME

*Pete Connors**

I. INTRODUCTION

The consumer debtor faced with insolvency is given two options under the present Bankruptcy Act:¹ (1) straight bankruptcy, and (2) wage earner proceedings. In contrast to straight bankruptcy, which is a liquidation oriented remedy, the debtor in a wage earner proceeding is not required to surrender any assets to the bankruptcy trustee, nor is he actually adjudicated a bankrupt. On the contrary, under Chapter XIII of the Bankruptcy Act (the wage earner section), the debtor is given a means of repaying his debts from future earnings under the protection of the court.²

The basic format of Chapter XIII is simple.³ After making a decision to use the relief provided by this chapter,⁴ the debtor and his attorney formulate a plan through which the debtor proposes to pay off all or a portion of his debts from earnings. The plan is submitted to both secured and unsecured creditors, who within the limitations of the Act, are given the opportunity to accept or reject the suggested plan. Upon acceptance by the requisite number of creditors,

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1. Bankruptcy Act of 1898, 11 U.S.C. *et seq.* (1970). Citations to Title 11 shall be omitted. References to the Bankruptcy Act shall be made by citation of the applicable section of the Act rather than to the section of the United States Code.

2. *Id.*

3. The sections of the Bankruptcy Act dealing with wage earner proceedings are contained in §§ 601-86. In addition, §§ 1-72 which deal with bankruptcy proceedings generally are made applicable to wage earner proceedings through § 602 where such provisions are not inconsistent. Many provisions of Chapters I-VII (§§ 1-72) and of Chapter XIII are made surplusage in view of the Bankruptcy Rules promulgated by the Supreme Court which relate to procedure under Chapter XIII. Statutory authority for the promulgation of the Bankruptcy Rules is found in 28 U.S.C. § 2075 *et seq.* (1970).

4. Consumer debtors are responsible for the vast majority of all bankruptcy case filing. Between fiscal years 1961 and 1972, they represented at least 90 percent of all bankruptcy debtors. While the overall percentage of consumer debtors has decreased in subsequent years, Chapter XIII cases continue to encompass approximately 17 percent of all non-business filings. During fiscal year 1975, the year in which bankruptcy filings reached their highest level, over 41,000 Chapter XIII petitions were filed. TABLES OF BANKRUPTCY STATISTICS, administrative office of the United States Courts, (unpublished report for fiscal year ending June 30, 1977).

and compliance with certain other statutory requirements, the bankruptcy court may confirm the plan, if convinced of its feasibility. Thereafter, all or a portion of the debtor's income is given to the bankruptcy trustee who disburses it to creditors in accordance with the plan. Upon completion of payments, a debtor will receive a discharge from all debts affected by the plan whether the creditors receive full or partial payment on their claims. If the debtor is unable to meet his obligations under the plan within three years after confirmation, a discharge will be granted only if he can show that his failure to complete payments was due to exigent circumstances such as loss of job or illness. Although confirmation can be attacked where fraud is involved, all creditors, whether or not they have consented, are bound by the plan and any discharge granted thereunder.⁵

The possibility of a massive restructuring of the present bankruptcy system has been the subject of serious congressional inquiry since 1968.⁶ While the major thrust of congressional proposals revising the current system has been directed toward other portions of the law, there will be substantive changes which affect the present wage earner section. This note will contrast the present bankruptcy system with H.R. 8200,⁷ the final version of the Bankruptcy Reform

5. Bankruptcy Act of 1898, *supra* note 1, § 1 *et seq.*

6. S.J. Res. 100, 90th Cong., 2d Sess. (1968).

7. BANKRUPTCY REFORM ACT, H.R. 8200, as amended, 95th Cong., 2d Sess. (1978) [Hereinafter cited as H.R. 8200]. H.R. 8200 reflects the conclusion of a legislative process which began with the establishment in 1970 of the Commission on Bankruptcy Laws of the United States. S.J. Res. 82 (Pub. L. No. 91-354, July 24, 1970, as amended). The final report of the Commission prompted the introduction of its recommendation to reform existing bankruptcy laws. A bill implementing its recommendations was first introduced in 1973 as H.R. 10729, and S. 2563, 93rd Cong., 1st Session. Dissatisfaction with the Commission proposal resulted in the introduction of a proposal offered by the National Conference of Bankruptcy Judges. The latter was introduced as H.R. 16643, 93rd Cong., 2d Sess. (1974).

Both bills were reintroduced in the 94th Congress where extensive hearings on bankruptcy reform took place. H.R. 10729 was reintroduced as H.R. 31, and S. 236, 94th Cong., 1st Sess. (1975). [Hereinafter cited as H.R. 31]. H.R. 16643 was reintroduced as H.R. 32 and S. 235, 94th Cong., 1st Sess. (1975). [Hereinafter cited as H.R. 32].

Extensive hearings continued in the House of Representatives and a synthesis bill H.R. 6 was introduced on January 4, 1977, to replace all prior proposals. H.R. 6, 95th Cong., 1st Session. This bill was marked up in Committee and later introduced as H.R. 7330, 95th Cong., 1st Sess. It was introduced on May 23, 1977, only to be modified again and introduced as H.R. 8200 on July 11, 1977. Before its initial adoption by the House on February 1, 1978, H.R. 8200 was amended and reintroduced.

Concomitantly, Senate discussion on bankruptcy reform focused on its own synthesis bill S. 2266, 95th Cong., 1st Sess. (1977), with passage being accomplished on September 7, 1978.

Act which was recently adopted by Congress and signed into law by President Carter on November 6, 1978.⁸ Emphasis also shall be placed on giving the practitioner some direction in choosing between straight bankruptcy and wage earner proceedings under both bankruptcy acts (i.e., the present Act, and the Bankruptcy Reform Act of 1978). Finally, Chapter 13 of H.R. 8200, which replaces Chapter XIII of the present Act, will be reviewed in an attempt to summarize the operation of this revised form of debt relief.

II. THE BANKRUPTCY REFORM ACT OF 1978: H.R. 8200

The enactment of the Bankruptcy Reform Act of 1978, H.R. 8200,⁹ marks the completion of the first major overhaul of the bankruptcy system in nearly 40 years.¹⁰ Under the Reform Act, which becomes effective on October 1, 1979,¹¹ three structural changes to the present bankruptcy system are envisioned. The first change enhances the status of the bankruptcy court by both expanding its jurisdiction,¹² and providing for the appointment of bankruptcy judges by the President with the consent of the Senate (rather than by judges of the districts courts, as is the present practice). The second change pertains to the adoption of a single consolidated reorganization chapter unlike the present system which allows a debtor to file

Having two conflicting, although not wholly dissimilar proposals before Congress, Senate leaders agreed to postpone indefinitely discussion on S. 2266 in favor of making all modifications necessary to resolve disputes over unsettled issues in the form of amendments to H.R. 8200. As finally adopted, H.R. 8200 was passed by the House on October 5, 1978, and by the Senate on October 6, 1978.

8. Pub. L. No. 95-598.

9. The Bankruptcy Reform Act is divided into four titles. Title I, which consists of only Section 101, revises Title 11 U.S.C., thereby replacing that section of the Code dealing with bankruptcy. Title II contains amendments to Title 28 U.S.C. These amendments set the framework for the establishment of a new Bankruptcy Court (Section 201) and United States Trustee System (Section 224). Title III contains conforming amendments to many other areas of the Code affected by the Act. Finally, Title IV contains the transitional sections, with Section 401 repealing the present Bankruptcy Act.

All textual references to H.R. 8200 shall be § 101 unless otherwise indicated.

10. The Chandler Act of 1938 is the basis for most of the law contained in the present Act of June 22, 1938, c. 575, 52 Stat. 840.

11. H.R. 8200, *supra* note 7, § 402(a).

12. H.R. 8200, *supra* note 7, § 201, *et seq.* The bankruptcy court would be given jurisdiction over all property of the estate without regard to who has possession of the property. *Id.* § 241. (28 U.S.C. § 1471). Under the present Bankruptcy Act, the comprehensive grant of jurisdiction imposed by § 2(a)(7) is qualified by § 23 which gives the courts of bankruptcy summary but not plenary jurisdiction.

under two or more chapters of the Bankruptcy Act, each of which dictates differing substantive rights.¹³ The third major change pertains to the enlargement of the role of the bankruptcy trustee and the establishment, on a pilot basis, of a system of United States Trustees under the control of the Department of Justice.¹⁴ The basis for this change was the congressional attitude that bankruptcy trustees, rather than bankruptcy judges, are better suited to administer bankruptcy cases.¹⁵ The major impact of this provision is that for the first time responsibility for the management of a centralized bankruptcy system will be divided between two branches of government: the Executive Branch, through its central control over the United States Trustee System, and the judicial branch, which will retain the responsibility of settling disputes. As noted, the implementation of the U.S. Trustee System will be made on a pilot basis.¹⁶ At the end of a 5 year transition period, Congress will decide whether to implement the system of U.S. Trustees or to terminate the pilot program.¹⁷

Chapter 13 of H.R. 8200 is entitled "Adjustment of Debts of an Individual with Regular Income" and covers what is known as the wage earner plan under Chapter XIII of the present Act.¹⁸ As many of the provisions dealing with ordinary liquidation proceedings apply to Chapter 13 proceedings as well, one must also look to Chapters 1, 3, 5 & 7 of H.R. 8200 for additional guidance concerning Chapter 13 cases.¹⁹ Also, the provisions dealing with United States Trustees for all cases have been aggregated in Chapter 15.²⁰

13. See REPORT OF THE COMMISSION OF THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. Doc. No. 137, 93rd Cong., 1st Sess., Part I at 237-48 (1973) [Hereinafter cited as COMMISSION REPORT].

14. H.R. 8200, *supra* note 7, § 224 (28 U.S.C. § 586).

15. One of the difficulties with the present system revolves around the fact that bankruptcy judges, without the aid of their clerks, presently spend as much as 22 percent of their time in administrative matters. COMMISSION REPORT, *supra* note 13, at 5.

16. The ten pilot districts will be as follows: (1) Districts of Maine, New Hampshire, Massachusetts and Rhode Island; (2) Southern District of New York; (3) Districts of Delaware and New Jersey; (4) Eastern District of Virginia and District of Columbia; (5) Northern District of Alabama; (6) Northern District of Texas; (7) Northern District of Illinois; (8) Districts of Minnesota, and North and South Dakota; (9) Central District of California; and (10) Districts of Colorado and Kansas. H.R. 8200, *supra* note 7, § 224.

17. H.R. 8200, *supra* note 7, § 408(b).

18. *Id.* § 101, 11 U.S.C. §§ 1301-1330.

19. *Id.* § 101, 11 U.S.C. §§ 101 to 728.

20. *Id.* § 101, 11 U.S.C. §§ 1501 to 151326.

With the exception of those changes regarding the confirmation of proposed Chapter 13 plans, most of the changes relating to wage earner proceedings are of a substantive rather than a procedural nature. This stems from the assumption by the drafters of the Reform Act that Rules similar to the Chapter XIII rules adopted in April 1973 by the Supreme Court will be promulgated. To be sure, many of the matters covered by the 1973 Rules will have to be modified with the enactment of H.R. 8200 since several procedural changes have been made. Thus, complete reliance upon the existing Bankruptcy Rules of Procedure would be unwarranted.²¹

III. THE WAGE EARNER PLAN AS AN ALTERNATIVE

For the attorney advising the non-business debtor, the decision to initiate either straight bankruptcy or wage earner proceedings is an important though not complex matter.²² The choice usually involves balancing the advantages and disadvantages provided to the debtor along with a consideration of his attitude toward the choice of relief available. Factors in this decision should include the following: (a) the degree of protection afforded the debtor's assets under state exemption and homestead laws in straight bankruptcy proceedings; (b) whether the petitioner had previously had a plan confirmed or had received a straight bankruptcy discharge within the past six years; (c) the extent to which certain debts will be exempt from

21. Section 247 of H.R. 8200, *supra* note 7, authorizes the Supreme Court to prescribe rules of practice and procedure for the bankruptcy courts. Rules promulgated will not be permitted to be inconsistent with the statute, in contrast to the Rules promulgated under the present Bankruptcy Act. See BANKRUPTCY LAW REVISION — REPORT OF THE COMMITTEE ON THE JUDICIARY, H. R. Rep. No. 595, 95th Cong., 1st Sess. 449 (1977). [Hereinafter cited as COMMITTEE REPORT]. Until new rules have been promulgated the transitional section provides that the present Rules will govern to the extent they are not inconsistent with the bill. H. R. 8200, *supra* note 7, § 405(d).

22. Numerous attempts to force a wage earner into Chapter XIII proceedings have failed. H.R. 127, H.R. 818, 88th Cong. 2d Sess. (1964); S. Rep. No. 613, H.R. 613, H.R. 292, 89th Cong., 1st Sess. (1965). See Adam, *Should Chapter XIII Bankruptcy Be Involuntary?* 44 TEXAS L. REV. 533 (1966).

Clearly, these proposals would amount to little more than forced long term garnishments with their attendant disadvantages. Where the debtor's motivation plays a significant role in the success of such an arrangement, it is submitted that a mandatory wage earner provision would be subject to inordinate difficulties. Nonetheless, under the proposed Act, individuals would no longer be exempt from involuntary liquidation proceedings as they are now under § 4(b) of the Bankruptcy Act. On the other hand, individuals earning more than eighty per cent of their gross income from farming would remain exempt. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 303.

discharge in straight bankruptcy; (d) the likelihood that secured creditors will object to a plan which alters their rights; (e) the debtor's ability to support a wage earner plan successfully; (f) the stigma imposed by straight bankruptcy proceedings; and (g) the extent to which the debtor feels a moral obligation to repay his debts.

These are the principal considerations involved in advising a client under the present bankruptcy system. Under the Bankruptcy Reform Act, a number of these factors will be modified so as to affect the ultimate decision involved in electing between straight bankruptcy and Chapter 13 proceedings.

A. *Exemptions*

The decision to proceed under the wage earner section will often be based on the amount of assets which are protected from liquidation by state homestead and exemption laws. If a debtor has a substantial amount of assets which would ultimately be turned over to the trustee for liquidation in a straight bankruptcy case, a wage earner plan should be seriously considered.²³ Under present exemption statutes, approximately 80 percent of all consumer bankruptcies are, however, no-asset cases (i.e., cases where all assets are either protected or are non-existent).²⁴ This figure should increase under the Reform Act as the debtor is allowed to choose between the exemptions provided by either federal and state laws,²⁵ or those

23. On the other hand, if a large portion of one's assets can be protected by either exemption or homestead statutes, a debtor might be wise to consider straight bankruptcy (liquidation) proceedings. There is no provision for this type protection under either Chapter XIII of the present Act, or Chapter 13 of the Reform Act since neither Chapter contemplates the surrender of assets.

Apart from this question, one should also be cognizant of the influence garnishment and exemption statutes have on the overall rate of consumer insolvency. For example, states which have totally exempted wages from garnishment such as Texas and South Carolina, have enjoyed the lowest rates of non-business bankruptcy. COMMISSION REPORT, *supra* note 13, at 49.

24. Statement of Hon. Conrad K. Cyr., *Hearings on S. 235 and S. 236 Before the Subcommittee on Improvements in Judicial Machinery of the Senate Committee on the Judiciary* 104 (1975) [Hereinafter cited as *Senate Hearings on S.235 and S.236*].

25. State laws vary substantially as to the amount and type of property which they protect. For a survey of state exemption and homestead laws, see J. MEYERS, *WIPE OUT YOUR DEBTS AND MAKE A FRESH START* 205-228 (1973).

The Virginia statutes provide the debtor with two exemptions: the homestead exemption of \$3500 available to heads of households, VA. CODE ANN. § 34-4 (Repl. Vol. 1970) *as amended*

provided by the new national exemption—a minimum federal homestead exemption of \$7500 and a personal property exemption of up to \$2,550.²⁶

The debtor's ability to select between the national exemptions, and the exemption afforded by local law may be limited, however, to the extent that the applicable state has elected to forbid use of the former.²⁷ Irrespective of the applicable exemption,²⁸ the debtor is given the right to void any judgment lien to the extent of any applicable exemption, as well as any non-purchase money lien on certain types of personal property.²⁹ Each debtor in a joint petition will be permitted to take the maximum personal exemption.³⁰ No restriction exists, however, to require a spouse in a joint petition to

§ 34-4 (Cum. Supp. 1975); and the "poor debtor's exemption," which is available to virtually all debtors against selected household articles. *Id.* § 34-26.

26. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 522. Under this section, provision is made for a minimum exemption of \$400 in any form of property. In addition, other property including livestock, wearing apparel, jewelry, household furnishings, tools of the trade or profession, and motor vehicles up to an aggregate amount of \$2150 also are exempted. Any unused portion of the homestead exemption may be added to the minimum exemption referred to above.

The Reform Act also contemplates the exemption of many payments including social security, pension, alimony and public assistance benefits which are akin to future earnings. *Id.* § 101, 11 U.S.C. § 522(d)10. Many of these exemptions are already allowed under federal laws. *See, e.g.*, 42 U.S.C. § 407 (social security payments); 45 U.S.C. § 352 (veterans benefits). In the event the debtor does not opt for national exemption, these sources would be exempt as being included under the category of other "federal laws." H.R. 8200, *supra* note 7, 11 U.S.C. § 522(b)(2)(A).

Cf. Uniform Exemption Act, 13 U.L.A., Civil Proc. and Rem. Laws, 1977 Pamphlet, which generally restricts the debtors right to exemptions to specific items, with only a \$1,500 allowance in cases where the debtor did not qualify for a residential exemption.

27. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 522(b)(1). The Rules of Procedure specify the manner in which the debtor may change his exemption from that of local law or to the national exemption after he has filed his petition. COMMITTEE REPORT, *supra* note 21, at 360.

28. This section also specifies that the debtor or his dependent must list the property claimed to be exempt. *Cf.* H.R. 32, *supra* note 7, § 4-503(1) in which failure to claim the exemption in a petition would not cause the debtor to lose the exemption. The Act also codifies the rule that the conversion by the debtor of non-exempt property into exempt property, in the absence of actual fraud, shall not be grounds for denying a claimed exemption. COMMITTEE REPORT, *supra* note 21, at 361. It seems questionable to contend that one can attempt to take advantage of a property right afforded by law and still be said to have acted fraudulently. *See Forsberg v. Security State Bank of Canova*, 15 F.2d 499 (8th Cir. 1926)(the debtor's trading of non-exempt property for exempt property for the purpose of securing an exemption was held not to have involved an intent to defraud creditors).

29. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 522(f).

30. *Id.* § 522(m).

select the same exemption (i.e., local or national) which the other spouse chose.

In some states, a previously filed bankruptcy petition will affect a debtor's right to claim a property exemption. For example, in Virginia, the homestead exemption³¹ is allowed only once during a person's lifetime whereas the "poor debtor's exemption"³² is allowed each time a petition is filed. Like the "poor debtor's exemption" in Virginia, the national exemption³³ would not be limited in use.

B. *Availability of a Straight Bankruptcy Discharge*

As under the current law, a debtor will not be eligible to seek a discharge in straight bankruptcy until six years³⁴ have passed from any previous discharge.³⁵ In contrast to the present Act, however, a debtor seeking relief under the H.R. 8200 would be permitted to obtain a straight bankruptcy discharge despite having obtained a Chapter 13 confirmation during the period in which he would otherwise be required to wait between straight bankruptcy discharges. This would occur where either payments under the plan total at least 100 percent of the allowed unsecured claims, or in the alternative, where payments total at least 70 percent of the allowed unsecured claims in the case and the plan is proposed by the debtor in good faith and is his best effort.³⁶ Where the plan does not meet

31. VA CODE ANN. § 34-4 (Repl. Vol. 1970), as amended § 34-4 (Cum. Supp. 1975).

32. *Id.* § 34-36.

33. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 522(b).

34. Bankruptcy Act of 1898, *supra* note 1, § 14(c)(5), H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 727(a)(8).

35. Other bankruptcy proposals, most notably, H. R. 32, *supra* note 7, § 4-505(A)(7), called for a five year waiting period, with a waiver provision where unforeseen circumstances such as a major illness resulted in the debtors inability to pay his debts. Compare H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1328(b) (providing a discharge in special hardship cases under Chapter 13 where the debtor has been unable to complete payments prescribed by the plan).

Cf. *Perry v. Commerce Loan Co.*, 383 U.S. 392 (1966). In *Perry*, the Court allowed a debtor to have an extension plan confirmed where he had obtained a discharge in straight bankruptcy within six years prior to the date of his Chapter XIII petition. Language in the case indicated, however, that *had* the situation involved a debtor who had failed to complete a Chapter XII composition plan (a plan where less than full payment is made on all claims) in a subsequent straight bankruptcy proceeding, a discharge would not have been available. *Id.* at 398-99.

36. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 727(a)(9). Since the question as to whether a plan was the best effort may serve as a litigation issue in the event the debtor must later use a Chapter 7 proceeding, it would be advantageous to include a clause in the Confirmation Order indicating the court's review of this matter.

these standards, if the debtor seeks a straight bankruptcy discharge at a later date, the right to obtain a discharge will be restricted in the same manner as if he had previously obtained a straight bankruptcy discharge.

C. *Dischargeability of Particular Debts In Straight Bankruptcy*

Whether or not a particular debt is dischargeable in straight bankruptcy can have considerable influence on one's decision to choose between straight bankruptcy and a wage earner proceeding. If a major debt is not dischargeable, the debtor will generally be wise to use the wage earner proceeding to allow him to pay the debt over the period of the plan.

Income taxes, as under the present Act, will be non-dischargeable if returnable during the three years prior to the date of the filing of the debtor's petition.³⁷ Similarly, income taxes for which (1) the debtor has made a fraudulent return, or (2) for which the debtor has failed to file a return, or (3) for which he filed a return but the return was not timely, such return being filed within two years of bankruptcy,³⁸ also will be non-dischargeable.

Likewise, the Reform Act continues present statutory law and codifies existing case law with respect to the non-dischargeability of debts obtained by false representation including those obtained by false financial statements. It adds to the latter, however, the requirement that any reliance upon the debtor's false financial statement must have been reasonable.³⁹ To avoid abuse of these provisions by recalcitrant creditors, the court has discretion to award a judgment for fees and other costs where this exception is alleged and judgment is rendered in favor of the debtor.⁴⁰

37. *Id.* § 101, 11 U.S.C. § 523(a)(1)(A), Bankruptcy Act of 1898, *supra* note 1, § 64(a).

38. *Id.* § 523(a)(1)(B). Likewise, debtors, with obligations in the form of educational loans will be unable to seek their discharge if the first installment was due less than five years prior to the date of the petition, or after the date of filing, unless the court finds that repayment of the debt from the debtor's income would impose an undue hardship on the debtor or his dependents. *Id.* § 523(a)(8). See *State v. Wilkes*, 394 N.Y.S. 849, 41 N.Y.2d 943 (1977), where, in a curious decision, the New York State Court of Appeals held that an educational debt which was forgivable on death or disability had not been discharged in a prior bankruptcy proceeding as the debt was a contingent debt, not capable of being liquidated, and thus not provable.

39. Bankruptcy Act of 1898, *supra* note 1, § 17(a)(2). H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 523(a)(2).

40. *Id.* § 523(d).

In order for a debt to be discharged under the present Act, it must be provable.⁴¹ This generally means that the debtor must show that the debt can fall within one of nine categories of provable debts. While a debt may initially fall within one of those categories, the bankruptcy court may find that neither liquidation or estimation is possible, or that the delay in obtaining such status would unduly hinder the administration of the case. Should this occur, a debt which is otherwise provable would be deemed to be non-provable and, hence, no longer capable of being discharged in the proceeding. Under the Reform Act, however, the concept of approvability has been eliminated and all debts which are contingent or unliquidated must be estimated if liquidation would unduly delay the closing of the case. Accordingly, a discharge from both unliquidated and contingent debts is now available.⁴² Where such unliquidated debts are a factor, it would seem that the debtor might select straight bankruptcy as a remedy where he formerly would have been unwise to do so.

D. *Creditor's Approval*

Under the present Act each creditor whose interest is secured by personal property must accept any plan which affects his security interest before the court may confirm a proposed wage earner plan.⁴³

41. Bankruptcy Act of 1898, §§ 17(a), 63(a). *Elmore v. Hill*, 345 F. Supp. 1098 (W.D. Va. 1972).

42. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. §§ 101(4)(A), 502(c). The requirement of §§ 57(d) and 63(a) of the present Bankruptcy Act, *supra* note 1, that, where otherwise provable, contingent or unliquidated claims be estimated has been retained. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 502(c).

43. Under sections 651 and 652 of the Bankruptcy Act, *supra* note 1, the debtor is authorized to obtain acceptances filed by creditors before or after the filing of his petition. If the acceptances filed by creditors and those filed on creditors' behalf by the debtor are filed before the conclusion of the first meeting of creditors, together with those creditors who are deemed to have accepted the plan, and such constitute all the creditors affected by the plan, then the court may confirm the plan if otherwise acceptable under section 656. If not, only those acceptances filed by the debtor on behalf of creditors filing claims before the conclusion of the first meeting together with those acceptances filed by creditors who have filed claims, and those creditors who are deemed to have accepted, will be counted in determining whether the necessary number and amount of unsecured creditors required by § 652(1) have accepted the plan. 15 COLLIER ON BANKRUPTCY ¶ 13-202.04 (14th ed. J. Moore, 1978) [hereinafter cited as COLLIER]. Section 652 requires acceptances by a majority in number of unsecured creditors affected by the plan (which actually represents a majority in amount of such claims) and by the secured creditors whose claims are dealt with by the plan.

Courts have interpreted the meaning of "affected" rather progressively. A plan that does

While an adjustment to the value of the secured claim will be made in the event of depreciation, acceptance by the secured creditor is still required unless the plan does not include a provision for the secured claim.⁴⁴ In considering a proposed plan, however, it is unlikely that a secured creditor will accept any plan which lessens the priority he would receive in a liquidation proceeding.⁴⁵ This is particularly true where the debt is one which a creditor can expect the debtor to reaffirm if faced with the possibility of repossession.

Under such circumstances, the debtor is often forced to elect straight bankruptcy or to propose a plan which avoids any reference to a secured creditor who will not accept the debtor's plan. If the bankruptcy court is willing to use its injunctive powers to discourage creditors from repossessing the collateral,⁴⁶ the debtor faced with a substantial number of secured debts should still be advised to proceed under Chapter XIII. This advice is warranted even where the debtor's plan avoids any reference to the creditor's claim in order to receive the requisite approval of creditors. In this manner he may be allowed to retain the collateral where it would otherwise be subject to repossession after a straight bankruptcy proceeding.

Under the Reform Act, both the secured and unsecured creditor's situation is substantially modified. An agreement to affirm a debt is enforceable only if made prior to the granting of the discharge and if the debtor has not rescinded the agreement within 30 days after

not provide for the payment of any installments on a secured debt does not affect the debt in such a way as to require the secured creditor to accept the plan even though the court enjoins the enforcement of the secured creditor's right to possess the collateral. *In Re Duncan*, 33 F.Supp. 997 (E.D. Va. 1940). See also *In Re Teegarden*, 330 F.Supp. 1113 (E.D. Ky. 1971) (a secured creditor was held not to be adversely affected by a plan if paid the present value of his security in monthly payments).

44. A debtor can exclude a secured creditor from a plan by omission as specifically permitted in § 646(a) and (6), or a secured creditor can exclude himself from the plan simply by not accepting the plan under § 652(1). Thus, the notion, it is argued, that a secured creditor's consent must be obtained is eliminated and any rejection by him will not bar confirmation of a plan. This is the position espoused in Poulous, *In Re Teegarden — Secured Creditors — Standard for Determining When Affected, Based on Limitations of Due Process Rather Than Contractual Terms*, 46 AM. BANK. L.J. 165, 169-70 (1972).

45. The position of the secured creditor is further enhanced by the usual practice whereby creditors lending money to consumer debtors will obtain a security interest on all of the debtors assets, irrespective of the size of his own claim. COMMITTEE REPORT, *supra* note 21, at 127.

46. Bankruptcy Act of 1898, *supra* note 1, §§ 614 and 658(2).

it becomes enforceable.⁴⁷ Where an individual debtor is involved, the requirements for a valid reaffirmation are much more onerous.⁴⁸ The most meaningful appears to be the requirement that the debtor appear at a hearing where he is to be given an explanation by the court of his rights with respect to the debt.⁴⁸ Thus, the likelihood of an effective reaffirmation is significantly diminished.

Even more innovative is that no longer will creditor's approval be a prerequisite to plan confirmation.⁴⁹ A plan will be confirmed by the bankruptcy court upon a finding that the value of property to be distributed in respect to unsecured claims is not less than the amount that would be paid if the estate were liquidated, and with respect to secured claims, if it finds that any one of the following has occurred: (1) the debtor has accepted the plan, (2) the secured creditor retains a lien securing the creditor's claim (during the period of the plan), as well as receiving no less than the fair market value of the collateral, or (3) the debtor surrenders the property securing the claim.⁵⁰ Because the drafters of the Reform Act have balanced competing interests in favor of debtors seeking rehabilitation in this situation, increased use of the wage earner section can be expected.

47. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 524(c). Where individual debts are involved, the following additional restrictions on reaffirmation have been added: (1) the reaffirmations must not relate to a debt that is secured by real property, and (2) the court must approve the agreement, as not imposing an undue hardship on the debtor or his or her dependents, as being in the best interest of the debtor, or having been entered into in good faith and in the settlement of litigation commenced by the creditors to contest the dischargeability of the claim, or was entered into in connection with the redemption of property under § 722. Under § 722, however, the debtor is given the right to redeem personal property intended for personal family or household use which is either exempt or has been abandoned by the bankruptcy trustee.

48. *Id.* § 524(d). Under existing case law a reaffirmation could be created without new consideration. A valid reaffirmation only required an intent to repay the old debt. *See* cases cited in 1A COLLIER, *supra* note 43, 17.33 n.4. By statute, the promise to repay is often required to be in writing. *See, e.g.*, VA. CODE ANN. § 11-2.01 (Repl. Vol. 1978).

49. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. §§ 1324 and 1325.

50. *Id.* § 1325(a). The amount of the secured creditors claim will be limited to the fair market value of the collateral. The remainder of the claim will be treated as an unsecured claim. *Id.* § 506(a). Since § 1325(a)(5) provides for what is in effect mandatory acceptance by secured creditors, where they receive value which is not less than the amount of such claim, the question of what is fair market value is likely to become the focus of heated disputes among the parties.

E. *The Plan's Feasibility*

To support wage earner plans under both Acts, the debtor must convince the court that his plan is feasible given his income and contemplated payments.⁵¹ Under the present Act, however, eligibility for Chapter XIII plans is limited to debtors who are wage earners, i.e., individuals whose principle income is derived from salary or commissions.⁵² Likewise, this income is unavailable for use in designing the debtor's plan where he also has employment related income. Thus, a self-employed person cannot file, nor theoretically can a person whose income is derived from a pension plan or social security payments.⁵³

In one of the most significant changes with respect to Chapter 13 under the Reform Act, the term "wage earner" has been replaced by the phrase "individual with regular income." Under this definition, a self-employed individual (including the small business owner who formerly was restricted to Chapter XI) as well as an individual whose income is derived from fixed sources such as retirement benefits or welfare payments would be allowed to apply for relief under this section.⁵⁴ If the income which is embraced under this expanded definition represents an additional source of income, as where salary of a spouse represents the main source of income, the amount of

51. Bankruptcy Act of 1898, *supra* note 1, § 656. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1325(a)(6). The latter refers to the debtor's ability to make future payments under the plan. It is not clear whether this is intended to place a higher burden on the debtor seeking confirmation of his plan.

52. Bankruptcy Act of 1898, *supra* note 1, § 606(8).

53. Actually courts have been liberal in this construction of the phrase "wage earner". See *In Re Bradford*, 268 F.Supp. 896 (N.D. Ala. 1967) (sole income was derived from social security benefits); *In Re Reed*, 368 F.Supp. 615 (E.D. Va. 1968) (a carpenter who was paid by the amount of work he produced, and for whom no one had been withholding income taxes).

54. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 101(a). The definition does, however, limit eligibility to individuals who, on the filing date, have non-contingent liquidated, unsecured debts of less than \$100,000 and noncontingent liquidated, secured debts of less than \$350,000. The need for this provision arises from the expansive definition of individuals who are eligible to participate under Chapter 13. Formerly self-employed individuals were confined to Chapter XI arrangements. To insure that larger businesses proceed under Chapter 11, the Act presumes that Chapter 13 is an inappropriate method of relief. COMMITTEE REPORT, *supra* note 21, at 119.

Also excluded from the class of eligible debtors are stock brokers and commodity brokers. Here, the rationale is that they should be prohibited from using the customer protection provisions of Chapter 7. *Id.* at 312.

funds which can be used in designing a plan is increased.⁵⁵ In this manner, plans which heretofore might have been considered "unfeasible" will now be acceptable for confirmation.

Although completion of the wage earner plan is not required under current law within a specified time period,⁵⁶ administrative costs diminish the utility of plans longer than three years in duration.⁵⁷ Many debtors, however, will be unable to repay all creditors completely within a three year period. Rather than designing an extension plan which lasts longer than three years in order to meet the requirement of feasibility, composition plans⁵⁸ which contemplate completion within three years should be a more suitable alternative. Although current interpretation of a section of the present Bankruptcy Act has limited the use of composition plans, this situation is expected to change in view of the new provisions enlarging the right to a straight bankruptcy discharge⁵⁹ (where debtors had previously been under a Chapter 13 plan) and the restriction whereby plans proposed under the Reform Act may only exceed three years in duration in cases in which a special showing has been made to the court.⁶⁰

55. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 302(a).

56. Section 661 of the Bankruptcy Act, *supra* note 1, has often been misinterpreted to include a requirement that plans be capable of completion within three years. (This section allows a debtor to apply for a discharge after three years where he has been unable to complete obligations contemplated under the plan). COMMISSION REPORT, *supra* note 13, at 160.

57. These costs include both trustee's and attorney's fees as well as reimbursement for actual and necessary costs and expenses. In addition, a portion of all payments made by the debtor is allocated to the referees' salary and expenses fund. Bankruptcy Act of 1898, *supra* note 1, § 40(c)(2). Under the Reform Act, however, no portion of any payment is allocated to this Fund. See note 123 and accompanying text *infra*.

58. A composition is a plan providing for payment of less than the full amount of debts owed, with interest to the date of commencement of the case. This is in contrast to an extension plan which provides for payment of the full amount of debts owed by the debtor with interest to the date of commencement of the case.

59. See notes 35 and 36 and accompanying text *supra*. The dictum of *Perry*, *supra* note 35, seems to be the major reason why many plans are extensions which should be compositions. Thus, the high mortality rate of wage earner plans. COMMISSION REPORT, *supra* note 13, at 160-61. See also *Cyr, Setting the Record Straight for a Comprehensive Revision of the Bankruptcy Act of 1898*, 49 AM. BANK R. L.J. 160 (1975), showing that before changes were made in wage earner plan implementation in Bangor, Maine, 95 percent of all plans were extension plans of which 60 percent would generally fail. Under the new program, composition plans were encouraged wherever appropriate. Experience under the new program reflects a failure rate of 10 percent. *Id.* at 155-60.

60. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1322(c).

F. *The Stigma of Straight Bankruptcy*

In many cases, the wage earner plan provides an attractive alternative to straight bankruptcy and the resulting stigma on the discharged debtor. The relative ease with which one may obtain credit after a discharge in straight bankruptcy suggests, however, that the stigma may be minor insofar as the "credit community" is concerned.⁶¹

It is possible that pressure from other sectors of the community, namely friends, relatives, and neighbors, particularly in small communities, may make the stigma a very real fact of bankruptcy.⁶² Apart from these social factors, some state laws, typically state motorists responsibility laws, have discriminated against bankrupts, undoubtedly imposing another specie of stigma. Under the Reform Act, any state law which discriminates against bankrupts is prohibited.⁶³

G. *The Moral Obligation*

The wage earner plan, by permitting the debtor to repay his creditors, affords the debtor a means of fulfilling his moral obligation while avoiding the straight bankruptcy discharge which is often perceived as unfair or even fraudulent to creditors. To the extent

61. One study of bankruptcy suggests that credit is made more available to Chapter XIII debtors than to straight bankruptcy debtors. Nonetheless, credit is made available to about 50 percent of straight bankruptcy debtors. D. STANLEY & M. GIRTH, *BANKRUPTCY: PROBLEM, PROCESS, REFORM* 64 (1974). This is explained by the fact that after discharge the creditor is aware that the debtor will be given a "clean slate" and that he will be unable to declare bankruptcy for a predetermined length of time. Compare Section 4-505(a)(7) of H.R. 32, *supra* note 35 (another bankruptcy proposal), which permitted a waiver of its five year bar to discharge provision where the court found that undue hardship would result to the debtor by denying him the right to discharge, and the cause of his situation results from matters not within his control.

62. See Haden, *Chapter XIII Wage Earner Plans-Forgotten Man Bankruptcy*, 55 Ky. L.J. 564, 605 (1967).

63. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 525. This section codifies the rule of *Perez v. Campbell*, 402 U.S. 637 (1971), which held that a state motorists responsibility law was violative of the Supremacy Clause of the U.S. Constitution because it required that even discharged bankruptcy debtors obtain releases from judgment creditors (where the initial claim accrued from a motor vehicle accident) before suspension of an individual's drivers license would be terminated. Compare, *Elmore v. Hill*, *supra* note 41, where the court required the suspension of the bankrupt's drivers license despite the discharge he had received in bankruptcy where the claim involved was not provable for failure of liquidation. VA. CODE ANN. § 46.1 - 459 (Repl. Vol. 1974); Bankruptcy Act of 1898, *supra* note 1, §§ 17, 63.

that a debtor motivated by these feelings can complete payment under a wage earner plan, such factors serve the decision making process as effectively as most substantive considerations.

IV. H.R. 8200: CHAPTER 13 - ADJUSTMENT OF DEBTS FOR AN INDIVIDUAL WITH REGULAR INCOME

A. *Commencement of Relief*

Relief under Chapter 13, the new wage earner plan section, (now called the Individual Repayment Plan) will be initiated by the filing of a petition in the bankruptcy court according to the Rules of Bankruptcy Procedure. A petition may be an original petition or a petition to convert from a pending liquidation case.⁶⁴

H.R. 8200 provides that the Chapter 13 trustee will be responsible for advising the debtor in the performance of his duties under the plan, for the establishment of a feasible plan and for monitoring the plan during the period of the extension.⁶⁵ Normally these functions will be the responsibility of a standing trustee—that is, the trustee to whom all Chapter 13 cases in the district are assigned. In areas where there is no standing trustee, the private trustee will assume these responsibilities, unless the district is one in which the pilot program of United States Trustees is in operation, in which cases these functions shall be performed by the latter. The delegation of these functions is designed to enhance the role of the trustee in Chapter 13 cases to more than that of a mere disbursing agent; rather, he is entrusted with considerable responsibility for the successful completion of the plan.⁶⁶

While most petitions under Chapter 13 will be original petitions, provision is made for converting both voluntary and involuntary liquidation proceedings into Chapter 13 plans.⁶⁷ As noted earlier,⁶⁸ all individual debtors with the exception of farmers may be forced into straight bankruptcy. If this occurs and the debtor is otherwise

64. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. §§ 301, 706(a) and 1321.

65. *Id.* § 1302(c) and § 1502(c).

66. BANKRUPTCY REFORM ACT of 1978; S. REP. NO. 989, 95th Cong., 2d Sess., 139 (1978). The trustee's role, however, is limited to giving advice on matters of a non-legal nature.

67. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 706(a).

68. See note 22 *supra* and accompanying text.

eligible, a petition may be filed causing conversion of the involuntary proceeding.⁶⁹

A husband and wife may file a petition jointly whether or not both spouses are eligible to file under Chapter 13.⁷⁰ This section modifies current practice⁷¹ in that it broadens the case of eligible petitioners. Thus, where one spouse cannot qualify, for whatever reason, if the other spouse is a debtor with regular income, a joint petition can still be filed. This section recognizes that the resources and expenditures of both husband and wife in most instances will be essentially the same.⁷²

A plan may be filed with the debtor's petition⁷³ or within such time as the Bankruptcy Rules prescribe.⁷⁴ During the period which follows the filing of the petition, however, the debtor will be protected by the provisions of the Act affording an automatic stay of most debt collection actions.⁷⁵

B. *Provisions Relating to the Plan*⁷⁶

Three provisions are mandatory in all Chapter 13 plans submitted for confirmation. First, the debtor must declare that he will submit future earnings or income to the supervision and control of the trustee. Through this provision, the trustee is allowed to exercise considerable control over all income and expenditures of the debtor.⁷⁷

69. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 706(a).

70. *Id.* § 101, 11 U.S.C. § 109(e), § 302.

71. CHAPTER XIII RULE 13-111. Presumably a provision comparable to section (b) allowing joint administration of separately filed cases will be adopted.

72. *Hearings Before the Subcommittee on Civil and Constitutional Rights of the House Committee of the Judiciary on H.R. 31 and H.R. 32*, 94th Cong., 1st and 2d Sess., Part 3 at 1317, (1975-1976) (statement of Conrad Cyr). [Hereinafter cited as *Hearings on H.R. 31 and H.R. 32*].

73. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1321.

74. COMMITTEE REPORT, *supra* note 21, at 428.

75. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 362. The principal exception to this rule is that the automatic stay will not operate against motions to collect alimony or to enforce separation agreements. *Id.* § 362(b)(2).

76. *Id.* § 1322.

77. *Id.* § 1322(a). Unless the court actually requires the debtor to turn over his pay check to the trustees, experiences from current practice indicate that this provision alone is not particularly effective in promoting completion of plan. This is because a debtor frequently may convey to the trustee an intent to fulfill his obligation, while actually he seeks delay of payments required by the plan without formally modifying the plan. See Official Form 13-6 which includes a provision for making payments to the trustee either by the debtor or by his employer.

Most plans currently being confirmed in the Richmond area include an optional provision giving the court substantial control over the debtor. This provision, which still may be popular after the enactment of H.R. 8200, requires the debtor to obtain the court's permission before becoming indebted in excess of \$400. Failure to obtain this permission may result in dismissal or conversion to straight bankruptcy. Control such as this is justified by the fact that new creditors may not be covered by the plan,⁷⁸ nor may they be able to levy on any of the debtor's assets without the court's permission.⁷⁹

Under the second mandatory provision, all claims entitled to priority⁸⁰ under the allowance section must be paid in full under the plan unless the holder of the claim agrees to different treatment. Among the claims entitled to priority are taxes, and administrative expenses incurred in the Chapter 13 proceeding.⁸¹

A third and final mandatory provision requires that the plan give the same treatment for any claims which have been placed in the same classification.⁸²

Of the provisions of Chapter 13 plans which will now be permissible, the following deserve special comment:

(1) the plan may provide for debts secured by real property only if the real property is *not* the debtor's principle residence.⁸³ The benefit to debtor here is less than self-evident; perhaps a realization

78. CHAPTER XIII RULE 13-305, under the present law, and H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1305 under the new law, govern the allowance of post-petition claims.

79. Under these provisions, taxes which arise after filing of the petition, and debts necessary for the performance of the plan, are allowable post-petition claims. Obviously, the latter require the court (or under the new Act, the trustee) to evaluate the circumstances surrounding the incurrence of the obligation. While it would appear that an express provision for post-petition claims is unnecessary, inclusion of a provision such as that described above is well-advised. As to the debtor, such a provision serves to remind him that post-petition debts will normally not be allowable—that is, during the period of extension, he must live within the budget he has established. Similarly, it serves to remind him of the cancerous consequences of credit splurging while he is under the plan. As to the court (or under the new Act, the trustee), such a provision lessens the need for its supervision thereby eliminating an otherwise inflexible situation.

80. Bankruptcy Act of 1898, *supra* note 1, §§ 611, 658(2). *Hallenbeck v. Penn. Mutual Life Ins. Co.*, 323 F.2d 566 (4th Cir. 1963). H. R. 8200, *supra* note 7, § 101, 11 U.S.C. § 362, as noted, continues this treatment.

81. *Id.* § 1322(a)(2). See 26 U.S.C. § 7122 (1954), allowing the Secretary of Treasury to compromise tax claims whenever liability or collection appears uncertain.

82. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1322(a)(3).

83. *Id.* § 1322(b).

that most of these debts could never be completed within the plan period prompted a provision for curing of defaults on such property,⁸⁴ in favor of dealing with them directly in the plan. In any case, this treatment continues that of current law.⁸⁵

(2) the plan may provide for classification of claims into groups which do not discriminate unfavorably against any particular class.⁸⁶ This is in recognition of the need for an option in the way claims of varying creditors are to be treated. This presents a marked departure from current law⁸⁷ where, for example, unsecured creditors are to be treated in the same manner. Thus, the debtor may have suffered substantial medical expenses not covered by insurance. Yet, his other unsecured debts may not be so intolerable. In drafting his plan, it would be permissible to classify his unsecured debts into two groups: one relating to medical bills, and a second covering all other unpaid debts. Under the plan, a different payment schedule could be provided for each class as long as all debts within the same class receive the same treatment.⁸⁸

(3) the plan may use the property of the estate to provide for payment of claims against the debtor.⁸⁹ This would include using exempt property or property on which there is a secured claim where the creditor has been otherwise satisfied.

In drafting the debtor's plan, counsel is encouraged to provide for as much flexibility as possible. The provision discussed above,⁹⁰ allowing the debtor to obtain credit without obtaining prior approval in all cases, is but one example of the type of provisions suggested. Another appropriate provision would allow the debtor to

84. *Id.* § 1322(b)5. See 124 CONG. REC. H11106 (daily ed., Sept. 28, 1978)(statement of Rep. Edwards).

85. Bankruptcy Act of 1898, *supra* note 1, § 606(1).

86. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1322(b)(1).

87. Bankruptcy Act of 1898, *supra* note 1, § 646(1).

88. *Hearings on H.R. 31 and H.R. 32, supra* note 72, Part 3 at 142. Similarly, claims necessary for the performance of the plan which have been allowed as post-petition claims should be classified with those claims which are required to receive immediate payment under the plan (*i.e.*, administrative expenses). See H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 364(b), § 507(a)(1), § 1328. While it would appear that the authority to include such claims in the plan as administrative expenses would be limited to the situation where the trustee has incurred the debt, such a clause would seem to be permissible under either §§ 503(a) or 1322(b)(10). *Id.*

89. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1322(b)(8).

90. See notes 77 and 78 and accompanying text *supra*; see also note 88 *supra*.

be granted a moratorium in making payments under the plan without having to apply to the court for permission. Here, the danger to be avoided would be a creditor's attempt to assert his right to have the case dismissed or converted to a liquidation proceeding.⁹¹ Provision also should be made for the trustee to decide whether such action is desirable under certain restricted guidelines. Likewise, the debtor may be in a predicament whereby a moratorium is not effective, and the only realistic solution is to provide for obtaining funds which have reached the hands of the trustee. Again, a clause in the plan allowing such action without the need to obtain court approval would be appropriate.

As noted earlier,⁹² the Reform Act changes present law by imposing a time limit under which all plans must be completed. The plan may not permit payment over a period exceeding five years, and periods in excess of three years may only be granted with court approval.

C. *Protection of Creditors*

The first meeting of creditors⁹³ affords the creditor an opportunity to confront and, if necessary, interrogate the debtor.⁹⁴ In a significant departure from present law, however, the new Act provides that the bankruptcy judge will not be present at this hearing. Rather, the first meeting will operate like a deposition session, with the debtor's attorney, or the trustee presiding. Objections made to claims will be resolved by the bankruptcy judge at a later hearing.⁹⁵ In its attempt to facilitate practice, the Reform Act follows the present Rules of Bankruptcy Procedure by allowing all claims properly filed unless objected to by a party in interest.⁹⁶

At the hearing on confirmation the court tests the debtor's plan against the statutory requirements of Chapter 13 to determine if the plan should be confirmed.⁹⁷ The standards for confirmation have

91. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1307(c).

92. *See* note 60 and accompanying text *supra*.

93. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 341(a).

94. *Id.* § 343.

95. *Id.* §§ 341(c), 502 (b). *See* 124 CONG. REC. S17432-3 (daily ed. Oct. 6, 1978) (statement of Sen. De Concini).

96. CHAPTER XIII RULE 13-307(b). H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 502(a).

97. *Id.* §§ 1324 and 1325. After hearing any objections filed within the time so fixed, the court shall confirm a plan if all fees and charges then required pursuant to section 123 of title

been substantially borrowed from the present Act⁹⁸ in that compliance with the procedural requirement is only effective where feasibility can be shown. The provision of the present Act⁹⁹ requiring that confirmation of the plan be denied if the debtor has done any acts which would bar a discharge under a straight bankruptcy proceeding has been eliminated. The rationale is that creditors are better served by allowing the debtor to attempt to repay the debt; moreover, the fact that he has forfeited his right to a straight bankruptcy discharge may actually provide him with greater incentive to perform under the plan.¹⁰⁰

At this hearing the court also will consider the objections of creditors. In contrast to the provisions of the present Act denying confirmation of a proposed plan until it has been accepted by a majority in number and amount of unsecured and secured creditors "affected" by the plan, and by all secured creditors whose claims are dealt with by the plan, creditors will have only limited input in determining whether or not a proposed plan will be confirmed. As noted earlier,¹⁰¹ it will be possible for a plan to be confirmed without the approval of creditors so long as the court is convinced that all claims are dealt with adequately under the plan.

D. *Post Confirmation Procedures*

A confirmed plan will be binding on all creditors.¹⁰² Creditors will be barred from attacking the provisions of a confirmed plan even where they have been unable to participate in the proceedings leading to confirmation. In addition, the court may use its injunctive powers to prevent harassment by creditors who continue to seek enforcement of their pre-confirmation rights.¹⁰³

Likewise, in an effort to protect the debtor during the period of

28 U.S.C. and all amounts then required pursuant to the plan have been paid, if the court is satisfied that the provisions of the Chapter have been complied with, that the plan has been proposed in good faith, that the provisions for secured and unsecured creditors (discussed at notes 47-50 and accompanying text *supra*), are adequate and that the debtor will be able to meet payments under the plan.

98. Bankruptcy Act of 1898, *supra* note 1, § 656.

99. *Id.* § 656(a)(3).

100. COMMISSION REPORT, *supra* note 13, Part 2 at 208.

101. See notes 47-50 and accompanying text *supra*.

102. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1327.

103. *Id.* § 362.

the plan, the drafters of the Reform Act have sought to remedy a problem under the present Act whereby a co-obligor or co-surety could exert pressure on the debtor in the situation where the former has been compelled to pay off the petitioner's debts by creditors who are unwilling to wait for payment pursuant to the plan.¹⁰⁴ Therefore, Chapter 13 provides for a moratorium on collections from co-debtors (by creditors) until the case is closed, dismissed, or converted to one for liquidation.¹⁰⁵ During this period, however, the creditor will be protected against both the expiration of the statute of limitations on his action against the co-debtor,¹⁰⁶ as well as the deterioration of collateral, if any, securing his obligation.¹⁰⁷

Notwithstanding this protection, it may become apparent that the debtor will be unable to fulfill his obligations under the plan. If this problem does arise, the debtor may apply to the court for modification of the plan, including if necessary, the permission to convert an extension plan into a composition plan.¹⁰⁸ Thus, the Act has attempted to encourage completion of a debtor's commitment whenever possible.

On the other hand, after confirmation the debtor may also apply to the court for the purpose of seeking a dismissal of the case or of a conversion to a liquidation proceeding.¹⁰⁹ The court at any time may also dismiss the case, or convert it to a liquidation proceeding whenever it is in the best interest of creditors or of the estate.¹¹⁰ The debtor's failure to pay fees and charges, material default of the provisions of the plan by the debtor, and among others, unreasonable delay by the debtor which is prejudicial to the creditors is sufficient cause under the Reform Act for the court to dismiss the

104. COMMITTEE REPORT, *supra* note 21, at 121-23.

105. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1301. This provision is limited in application only to consumer type debts. *Id.* § 1301(a).

106. *Id.* § 108(c).

107. *Id.* § 1301(c)(3).

108. *Id.* § 1329. Despite common parlance, the drafters have avoided any reference to plans as either "extension" or "composition" plans. Here reference is made simply to modifying the plan within the guidelines set forth under §§ 1322 and 1325.

109. *Id.* § 1307(a), (b). The right to convert to a rearrangement proceeding is limited to the period preceding confirmation of the plan. *Id.* § 1307(d). The right to request conversion to a rearrangement proceeding is given to any party in interest. Both the broader discharge provisions (discussed at note 127 *infra*) and the convenience afforded by Chapter 13, in contrast to that of Chapter 11, require that such conversation be avoided.

110. *Id.* § 1307(a).

case or to require that it be converted to one for liquidation.¹¹¹

Within 180 days after the order granting confirmation of the plan, a party in interest may raise the question of fraud in the procurement of the plan. The court will hold a hearing on notice to all parties in interest.¹¹² If after the hearing, the confirmation is set aside, the court may proceed to either dismiss the case or convert the case to one for liquidation. At this time the court also may receive proposals of the debtor to modify the plan. If the debtor's modified plan is confirmed, the debtor will follow the procedure outlined in sections 1323 through 1325 for obtaining confirmation of a modified plan. If the proposed plan is not confirmed, the court may either dismiss the case or convert it to one for liquidation. This is the procedure even where a converted liquidation case is involved.¹¹³

E. *Claims and Distribution*

As under present law, in order for a claim to be allowed, a proof of claim for each debt will be required to be filed, whether it be by the debtor, creditor, or trustee.¹¹⁴ Generally, the creditor seeking payment of his claim will file the proof of claim. A claim will be discharged notwithstanding the failure to file a proof of claim, so long as the debt is provided for in the debtors plan.¹¹⁵

Because the date of the petition is the date for the determination of claims,¹¹⁶ interest will be limited to that amount which had accrued at that time. However, certain claims will be allowed even where liability has accrued after the date of the petition: (1) claims

111. The court also has this power before confirmation of the plan. This conforms to CHAPTER XIII RULES 13-112 and 13-215. It improves the former, however, by substituting "the debtors failure to prosecute the proceedings" with "unreasonable delay prejudicial to creditors" as a possible grounds for dismissal or conversion prior to confirmations.

112. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1330.

113. Under the present rules of procedure, if the debtor (whose plan has been revoked for fraud) has filed his petition in a pending straight bankruptcy case, and the modified plan is not confirmed, the court shall enter an order directing that the pending bankruptcy case proceed. Where an original Chapter XIII proceeding is involved, however, the court may dismiss the case or adjudicate the debtor a bankrupt without his consent. Where fraud is not involved, however, the debtor in an original Chapter XIII proceeding cannot be adjudicated a bankrupt without his consent. CHAPTER XIII RULE 13-215.

114. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 502(a).

115. *Id.* §§ 1328(a), 502(a), 727(b) (for liquidation cases).

116. *Id.* § 502(b)(2).

arising from executory contracts and unexpired leases, which have been rejected;¹¹⁷ (2) claims for taxes which arise after the date of the petition;¹¹⁸ (3) claims which are the result of the debtor's needs for property or services required by him to assure proper performance of the plan;¹¹⁹ and (4) claims for property recovered under the preference avoiding powers of the trustee, where applicable.¹²⁰

In order for the Chapter 13 program to be moderately self-supportive and for attorneys, whether in their capacity as representative of the debtor, or as the bankruptcy trustee, to be willing to practice under this section of the Act, it is imperative that the debtor be sincere in meeting obligations to these groups. For this reason, certain claims will be given priority before remaining creditors can receive dividends under any plan. Priority of payment under this section¹²¹ is given to the actual necessary¹²² costs and expenses of preserving the estate, compensation and reimbursement awarded to officers of the estate,¹²³ including both the trustee, and

117. *Id.* §§ 365, 502(g). This right is particularly powerful in that it gives the trustee authority to revise contracts even where those contracts have anticipated the possibility of insolvency by the debtor. For a discussion of this power under the present Act, see Countryman, *Executory Contracts in Bankruptcy*, 57 *MIN. L. REV.* 439 (1973). In rejecting or assuming executory contracts, or unexpired leases, the trustee must act before confirmation of the plan. Consistent with present law on this matter, H.R. 8200 rejects the proposal of H.R. 32, *supra* note 7, § 4-602(a)(1) which mandated a sixty day limitation period in which the decision to act affirmatively, was required to be made. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 365(d)(2).

118. *Id.* § 1305(a)(1).

119. A claim arising under this section will not be allowed if the holder of the claim knew or should have known that prior approval by the trustee of the debtor's incurring of the obligation was necessary, and seeking such approval was practicable, and approval was not obtained. *Id.* § 1304(c).

120. *Id.* §§ 502(i), 550.

121. *Id.* §§ 507(a)(1), 1325(a)(2), 1326(a)(1).

122. Under CHAPTER XIII RULE 13-106(6)(1), the debtor can apply for permission to pay the filing fee in installments. If this occurs, the court may authorize payment of the installments in the plan or otherwise.

Under H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 727, failure to pay filing fee has been eliminated as a bar to discharge in liquidation proceedings, thus eliminating the impact of *United States v. Kras*, 409 U.S. 434 (1973), in which the Supreme Court denied the debtor the right to file bankruptcy *in forma pauperis*. For reasons which should be readily apparent, no parallel provision has been added under Chapter 13. In this regard, it should be observed, that the court may require the debtor to pay the filing fee before confirmation. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1325(a)(2).

123. *Id.* § 503(b). This represents a departure from current law in that priority of payment for a portion of the bankruptcy judge's salary, which would be paid into the Referees Salary

attorneys representing the debtor.¹²⁴ Where the United States Trustee serves as trustee, the compensation to which a trustee is normally entitled is to be paid to the United States treasury.¹²⁵

F. *The Discharge*

On completion of all payments specified by the plan, the debtor will be granted a discharge on all debts provided for by the plan as well as those which were not allowable as claims against the estate. The effect of the discharge will be the same whether granted in accordance with a composition or an extension plan.¹²⁶ The discharge granted under Chapter 13 is more comprehensive than that contained in liquidation proceedings in that the only exceptions to discharge are alimony, maintenance and child support obligations. Thus, filing a Chapter 13 plan can result in the debtor obtaining a discharge on debts which would not have been dischargeable if he had filed under the liquidation sections.¹²⁷

If completion of the plan is not possible, the debtor may apply at any time for a discharge providing he can show that his failure to complete payments was due to circumstances arising after confirmation for which he is not responsible. This provision¹²⁸ departs from the present Act¹²⁹ which requires the debtor to wait three years before making such a request. Thus, the alternative, before the three year lapse, had been to apply for a dismissal or a conversion to straight bankruptcy unless modification was acceptable. Under the new Act, the debtor need only show the court that modification of the plan is not feasible. If a discharge is granted under this sec-

and Expense Fund, has been eliminated. This represents the general agreement that the bankruptcy system no longer need to be completely self-supporting. COMMITTEE REPORT, *supra* note 21, at 187, 540.

124. This continues the policy of Bankruptcy Act, *supra* note 1, § 659(4), and Bankruptcy Rule 219 under which the court is allowed to scrutinize the compensation received by the debtor's attorney for his services. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 328. In Richmond, the Bankruptcy Court has adopted \$400 as the ceiling for attorney's fees in wage earner proceedings. Local Rule 5(d), Bankruptcy Court, Richmond, Virginia. The expansion of the role of the standing trustee, who now must perform debtor counseling services, may produce an even lower standard fee.

125. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 15324, § 15330.

126. *Id.* § 1328(a).

127. *Cf.* §§ 1328(a)(2) and 523(a).

128. *Id.* § 1328(b).

129. Bankruptcy Act of 1898, *supra* note 1, § 661.

tion, however, it would only be effective with respect to unsecured claims which are not exempted from discharge. Thus, the Chapter 13 "hardship" discharge is less comprehensive than the discharge obtainable had the debtor completed payments pursuant to the plan.¹³⁰

G. *The Trustee*

Whenever the number of Chapter 13 cases justifies the practice, the court will appoint a trustee to whom all Chapter 13 cases will be assigned. In other cases, the court will appoint a private standing trustee.¹³¹ Furthermore, the new Act fails to incorporate legislative proposals whereby creditors would have been permitted to elect a trustee in lieu of a standing trustee.¹³²

In those pilot districts where the U.S. Trustee System will be in operation, the U.S. Trustee will appoint the standing trustee, and will serve as trustee in all cases where the number of Chapter 13 cases does not justify the use of a standing trustee.¹³³ In the pilot districts, the U.S. Trustee will assume full responsibility for supervision of the performance of all standing trustees and is empowered to remove a trustee from office for cause.¹³⁴

130. Cf. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1328(c)(2), and 1328(a)(2).

131. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1302(a).

132. As originally drafted, § 1302(a) permitted creditors to elect a trustee in Chapter 13 cases in the same manner as other cases. The justification lying in that Chapter 13 was no longer limited to wage earners; rather, debtors owning small businesses could also qualify. COMMITTEE REPORT, *supra* note 21, at 106. Legislative history for the sudden change, however, is lacking although cause may in part be found in the amendment to § 341(c) of H.R. 8200, *supra* note 7, § 101, which permits the first meeting of creditors to be conducted by the bankruptcy trustee. See note 95 and accompanying text *supra*.

133. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 151302(a)(1).

134. *Id.* § 224, 39 U.S.C. § 586(b). The compensation of the trustee under the present Act is limited to 5 per cent of the total payments made under all plans. It is further limited so that the maximum compensation of a trustee shall not exceed the maximum compensation of a full-time bankruptcy judge. Guidelines for Chapter XIII Administration prescribed by Judicial Conference Memorandum, No. 346, Supplement No. 4, April 21, 1972. See also Advisory Committee Note, CHAPTER XIII RULES 13-201, 13-209 and Bankruptcy Act § 659(3). Section 326(b) of H.R. 8200, *supra* note 7, § 101, also limits the compensation of the trustee to 5 per cent of all payments made under the plans which he handles. At least one commentator has suggested, however, that the trustee should be given a salary based on the caseload he handles. *Senate Hearings on S.235 and S.236, supra* note 24 (statement of Hon. Joe Lee).

H. *Property of the Estate*

The new Act includes both a definition of the property included within the debtor's estate and, in addition, provides various rights for the debtor with respect to the estate which it establishes.

The estate now includes both property and income from services acquired after the commencement of the case.¹³⁵ The debtor is to remain in possession¹³⁶ of the property of the estate and is given the right to act independently of the trustee in many transactions. Such transactions include the right to use, sell or lease property in other than in the ordinary course of business after adverse parties are given notice and hearing. The debtor must, subject to limitations discussed earlier,¹³⁷ obtain approval before he incurs credit that he expects to have included in the plan.¹³⁸

Furthermore, where the debtor is self-employed and incurring trade credit in the production of income,¹³⁹ the debtor, unless otherwise specified by the court, is given the exclusive right to use property held under leases, or which is subject to a lien, during the pendency of the case,¹⁴⁰ and in addition, he is allowed to sell¹⁴¹ or lease property in the ordinary course of business without the need for obtaining the permission of either the trustee or the court. The self-employed debtor also is permitted to negotiate for and obtain credit necessary for the functioning of his trade or business. The provisions for the self-employed debtor closely resemble those provisions available to the debtor in a rearrangement proceeding under

135. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1306(a). The statutory pattern reflects a curious omission: the debtor's plan may use all sources of income so long as the stream is sufficiently regular and predictable. Within that category would conceivably fall both social security income and guaranteed payments. Yet, the bankruptcy court's jurisdiction over future income is limited to "earnings from services performed by the debtor." Compare the treatment under the present Bankruptcy Act, *supra* note 1, §§ 70(a) (definition of property of the estate), § 611, and § 658(2) (both defining the court's jurisdiction over the debtor's property in Chapter XIII cases.)

136. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 1306(b).

137. *Id.* § 1303.

138. *Id.* § 1305(c). See note 78 and accompanying text *supra*.

139. *Id.* § 1304(a).

140. H.R. 8200, *supra* note 7, § 101, 11 U.S.C. § 363(c). The right to use, sell or lease is restricted to non-cash collateral. *Id.* § 363(a).

141. *Id.* §§ 1304(b), 363(b).

Chapter XI of the present Bankruptcy Act where no receiver has been appointed.¹⁴²

V. CONCLUDING REMARKS

Whether the number of wage earner proceedings increases with the enactment of H.R. 8200 will not be a true indication of its success. Many debtors, particularly where no-asset cases are involved, cannot be expected to benefit from this type proceeding. For this reason, inquiry should be made into whether the Act has provided a remedy accessible by the type of debtor it has been designed to aid.

Under the Reform Act, the debtor confronted with the prospect of insolvency has a path leading to relief that is well defined, if not in fact cushioned with inducements of nectar. It is evident that the drafters have emphasized a public policy approach that opts in favor of the debtor seeking some form of relief, whether it be in the form of a "fresh start" or "rehabilitation," rather than one which favors the interests of creditors seeking realization of their claims. The latter, it would seem, should have little cause to complain, for the equities underlying consumer bankruptcies can only be said to have been recognized.

142. Bankruptcy Act of 1898, *supra* note 1, § 342. These provisions follow from the changes expanding eligibility for wage earner proceedings to the self-employed. See *Hearings on H.R. 31 and H.R. 32*, *supra* note 72, Part 3 at 1324, 1414.