ABOUT CHAPTER 13

A. REQUIREMENTS OF A CHAPTER 13 PLAN

The plan is the core of a Chapter 13 case. It is the mechanism by which the debtor can exert control over his/her financial future. Essentially, the debtor must set out how he/she intends to pay creditors The plan should be clear on its face–anyone reading the plan should understand how the creditors are being paid. There is a required plan for both the Northern and Southern Districts and a copy of each is attached to these materials.

The plan is the debtor's proposal to deal with his/her creditors–**all** of his creditors. A debt not provided for in the plan is not discharged. *Cen-Pen Corp. v. Hanson*, 58 F3d 89 (4th Cir. 1995). So, there are no claims "outside the plan"–there may be some direct pays for which the debtor has proposed and the Court has allowed the debtor to be his/her own disbursing agent.

1. Length

If the debtor's annual income is under the state median income, then the debtor may file a plan that runs 36 months to 60 months. However, unless the plan pays 100%, it must run at least 36 months.

If the debtor's income is above median income, then the debtor must file a plan that runs 60 months.

A debtor in either category may shorten the time frame by paying 100% of the allowed unsecured claims in a shorter period.

2. Plan Payments

Plan payments begin 30 days from the filing of the petition.

The plan payment is initially determined by the amount of disposable income. However, a plan must also meet the "best interests of creditors" test, which means that even if all of the debtor's disposable income is paid into the plan, if creditors would receive more in a Chapter 7 liquidation case, plan payments must be increased or supplemented to provide to creditors that amount. This is most commonly seen in a cases with retired debtors on retirement income but who own a house free and clear and the value of the real estate is greater than the allowed exemption.

3. Direct pay vs. through the plan

Both Judges require that if there is a pre-petition arrearage on the mortgage payment, the on-going mortgage payment should be paid through the plan. I generally object if the plan deviates from this requirement. Direct pays are allowed on unimpaired claims–i.e., no default–and claims secured by collateral which is worth more than the obligation.

4. Secured claims

Pursuant to 11 U.S.C.§1325(5)(B)(i)(I) the plan must provide that the secured creditor retains its lien until the claim is paid in full or the debtor receives his/her discharge as well as provide that if the case is dismissed or converted, applicable state law will control.

5. "910 claims"

Under 11 U.S.C.§1325(5), hanging paragraph after (9):

> For purposes of paragraph (5), section 506 shall not apply to a claim descried in that paragraph if the creditor has a purchase money security interest securing the debt that is the subject of the claim, the debt was incurred within the 910-day preceding the date of the filing of the petition, and the collateral for that debt consists of a motor vehicle. . .acquired for the personal use of the debtor, or if collateral for that debt consists of any other thing of value, if the debt was incurred during the 1-year peiod preceding that filing.

This is referred to as the anti-cramdown provision. What it does is require the debtor to pay the balance owed on the vehicle which he or she purchased in the last 2½ years. It also provides that the creditor, since 506 doesn't apply, does not receive pre-confirmation interest on the claim and doesn't get attorney fees. It does NOT prevent the debtor from modifying the note by changing the interest rate per *Till* and paying for the claim over the life of the plan pursuant to 11 U.S.C. §1325(5)(B)(iii)(I) which requires that secured claims receive equal monthly payments over the life of the plan.

6. Non-dischargeable claims

11 U.S.§1322, (10) provides that the plan must provide that post-petition interest continues to accrue on non-dischargeable unsecured claims HOWEVER, the interest cannot be paid on such claims unless the debtor pays 100% on all allowed claims.

B. HOW TO COMPUTE A CHAPTER 13 PLAN

In my mind, there are eight claim components to a plan:

1. Administrative claims–the trustee fee and attorney fees.

One is dear to my heart, and one is dear to debtor's counsel's heart. The

trustee fee should be calculated at 10% of the amount paid into the plan. If my fee is reduced, the difference goes to unsecured creditors. If you calculate the fee at less than 10%, the plan works only on paper.

Attorney fees need to be consistent with the Statement of Financial Affairs and the Rule 2016 Disclosure Statement.

2. Priority claims

Priority claims must be paid in full, unless the holder of the claim accepts other treatment, [11 U.S.C. 1322(a)(2)], provides the same treatment for all claims in the same class, and is a five-year plan. [11U.S.C. 1322(a)(4)].

It makes sense for the debtor to maintain domestic support claims directly–and cure any arrearages in the plan. Under the Code, the debtor must keep those domestic support obligations current or risk not receiving a discharge. *See* 11 U.S.C. 1325(a)(8). Tax claims also must be paid in full over the life of the plan. Only in Chapter 13 can the debtor stop the accrual of penalty and interest by paying the claim over the life of the plan. There is case law that says that if the debtor elects to make direct payments on pre-petition tax claims while in a Chapter 13 case, interest continues to accrue. If the case is converted or dismissed, the taxing authorities re-calculate interest from the beginning of the case.

3. Mortgage claims

In a Chapter 13 case, the debtor can cure the arrearage of a mortgage over a “reasonable period, ” which is generally the life of the plan.

The plan may provide that the debtor will file an adversary proceeding to get rid of junior liens on the debtor's residence–if the lien is unsupported by the value of the property.

4. "910 claims"

As noted before, these claims must receive the principal owed at filing but the interest rate may be reduced.

5. Other Secured claims

EACH secured claim must be treated–whether it is paid by the debtors or the trustee. Generally speaking, with the exception of claims secured solely by the debtor's principal residence and "910 claims," claims are valued pursuant to 11 U.S.C. §506, the value of the collateral paid as the secured claim with interest per *Till v. SCS Credit Corp*., 124 S.Ct. 1951(2004), in which the Court determined that the correct interest rate in Chapter 13 proceedings is the national prime rate plus a risk factor of between 1 to 3 per cent. The balance of the claim is treated as an unsecured claim.

6. Lease claims

If the debtor has leased property, that must be disclosed and provided for–whether it is a surrender or retain.

7. Special category claims

These include co-debtor claims, which may be paid in full at contract rate interest or claims which would otherwise be non-dischargeable in a Chapter 7 case which can be dealt with in a Chapter 13 plan. In a case converted from Chapter 7, this would also include the Chapter 7 trustee fees.

8. Unsecured claims

Each plan may not have a claim in each category. One of the beauties of Chapter 13 is that it is not a one-size-fits-all approach. Each plan can be crafted to fit the debtor and his/her lifestyle–although not too extravagantly!

My rule of thumb for plans: Tell me to whom I am to write the check, for what amount and for what reason.

11 U.S.C.§1324(b) provides that the confirmation hearing may be held no earlier than 20 days after the date of the meeting of creditors and not later than 45 days after the date of the meeting of creditors.

My office files a written recommendation and workup before most of the confirmation hearings. Generally speaking, a plan will not be confirmed before the bar date for general unsecured creditors, which allows time for both a payment history to be established and to determine whether the plan is feasible based on timely filed claims.

To be confirmed:

1. A plan must meet all the statutory requirements

2. The debtor must be current on payments

3. And the debtor must show:

1. The case was filed in good faith 11 U.S.C. §1325(a)(7) [Note: this is different than the plan having been filed in good faith];

2. The debtor is current on all domestic support obligations; 11 U.S.C. §1325(a)(8);

3. The debtor has filed all federal, state, and local taxes as required by 11 U.S.C. §1308; 11 U.S.C. §1325(a)(9);

4. The debtor is current on payments made directly pre-confirmation. 11 U.S.C. §1326(a)(1)(B) and (C). This requires that the debtor provide to the

trustee documents proving the payment including the amount and the date of the payment.

C. POST-CONFIRMATION DEFAULT

The debtor has a responsibility:

1. To give copies to the trustee of post-petition tax returns and file a new statement of income and expenditures along with the source of the debtor's income at the time. 11 U.S.C. §521(f)(4). This requires the debtor to disclose the identity of any other person contributing to the household in which the debtor resides and must disclose how the income and expenses were calculated.

2. To maintain post-petition domestic support obligations;

3. To get permission to sale property or acquire new debt;

4. To not run afoul of securities regulations or engage in criminal or tortious activity which causes death or serious physical injury (11 U.S.C. §522(q)).

5. To maintain plan payments, whether directly to the creditor or to the trustee.

D. POST-PETITION DEBT

To acquire post-petition debt requires that the debtor obtain court approval. It has never been my policy to write letters to state that the debtor is allowed to finance a new car, etc.

There are forms available on both Courts' websites for this procedure.

E. DISMISSAL AND CONVERSION ISSUES

1. Conversion

Pursuant to 11 U.S.C. §1307(a), the debtor may convert a Chapter 13 case to a Chapter 7 at any time. But the U.S. Supreme Court has rejected that as an "absolute right.." In a recent decision, the Supreme Court held that a bankruptcy court may deny conversion where there is fraud or other evidence of bad faith. *Marrama v. Citizens Bank*, ___ U.S. ___, 127 S. Ct. 1105; 166 L. Ed. 2d 956 (2007).

Conversion may not always be in the debtor's best interest.

In order to benefit from the Chapter 7 after conversion, the debtor must be eligible to receive a Chapter 7 discharge. *See, In re Hiatt,* 312 B.R. 150 (Bankr. S.D. Ohio 2004)(prior Chapter 7 discharge rendered debtor ineligible for discharge in case converted from Chapter 13 to Chapter 7, where the filing of the Chapter 13 was within 6 years [now 8 years] of the previous Chapter 7 case).

To convert from Chapter 7 to Chapter 13, the debtor must meet the eligibility requirements of §109(e), including the debt limits. And be acting not in bad faith. *Marrama v. Citizens Bank*, ___ U.S. ___, 127 S. Ct. 1105; 166 L. Ed. 2d 956 (2007).

If a case is converted **to** chapter 7, 11 U.S.C. §348(d) specifically states that when a case is converted under §§1112, 1208 or 1307, almost all claims against the estate or the debtor shall be treated as if they were pre-petition claims. Thus, post-petition debts incurred during the Chapter 13 can be

discharged when the case is converted to Chapter 7. *See, In re Weinstock*, 43 Collier Bankr. Cas. 2d (MB) 573, 1999 U.S. Dist. LEXIS 18480 (E.D. Pa. November 12, 1999).

However, the case law authority states that upon conversion **from** a Chapter 7 to a Chapter 13, there is no right to include post-petition debts (incurred after the filing of the Chapter 7) in a Chapter 13 case. *In re Weinstock,* 1999 Bankr. LEXIS 453 (Bankr. E.D. Pa. April 27, 1999), *aff'd, In re Weinstock*, 43 Collier Bankr. Cas. 2d (MB) 573, 1999 U.S. Dist. LEXIS 18480 (E.D. Pa. November 12, 1999).

2. Dismissal

As a general rule, the Chapter 13 debtor has the right, **if** the Chapter 13 case had not been converted from another Chapter, to the dismissal of the case at any time, subject to some case law limitations. 11 U.S.C. §1307(b)

There is a split of authority as to a debtor's right to dismiss when faced with a motion to convert. Some courts have held that a Chapter 13 debtor's right to voluntary dismissal under §1307(b) is absolute. *See, In re Molitor*, 76 F.3d 218, 220 (8th Cir. 1996)(citing cases). Other courts have held that §1307(c) (authorizing conversion for cause) curtails a right to voluntary dismissal. The District Court decision in *In re McCraney,* 172 B.R. 868 (N.D. Ohio 1993) upheld the Bankruptcy Court's decision vacating the debtor's voluntary dismissal, and reopening the case for cause. This approach appears to be consistent with the recent Supreme Court decision in *Marrama v. Citizens Bank,* ___ U.S. ___, 127

S. Ct. 1105; 166 L. Ed. 2d 956 (2007).

Keep in mind when considering dismissal as an option that if the debtors voluntarily dismiss, they may run afoul of 11 U.S.C. §109(g)(2), which prohibits the debtors from filing a new Chapter 13 case for 180 days if the case is voluntarily dismissed after a motion for relief from stay is filed.

The debtor does not have a statutory right to dismiss a Chapter 7 case. A voluntary dismissal of a Chapter 7 case is governed by Section 707(a), which states as follows: "The court **may** dismiss a case under this chapter **only** after notice and hearing and **only** for cause, including . . . ." (Emphasis added.)

11 U.S.C. §707 provides three instances when a debtor's actions would lead to dismissal. These are not the exclusive grounds for dismissal. However, it should be noted that there are three instances set forth in the Bankruptcy Code dealing with situations where the debtor's actions would permit dismissal on a motion by a creditor. *See, In re McCullough,* 229 B.R. 374, 376 (Bankr. E.D. Va. 1999). 11 U.S.C. §707(a) provides no examples of what would be adequate grounds for debtors to obtain dismissal of their own cases.

To the extent that a debtor can seek voluntary dismissal of a Chapter 7 case, it is the debtors' burden to make the showing of cause, "and the Court should deny the motion if there is any showing of prejudice to creditors." *In re Haney*, 241 B.R. 430, 432 (Bankr. E.D. Ark. 1999)(citing cases).

However, happily for debtors who are in Chapter 7 and wishing they weren’t, there are more opportunities under BAPCPA for "automatic dismissal" of

cases based upon the failure to file various documents.

F. DISCHARGEABILITY OF DEBTS

The following debts are excepted from discharge in a Chapter 13 case:

Loans to a pension fund

II support claims,

II taxes;

or debts incurred to pay taxes to any government unit;

W taxes the debtor should have withheld (trust fund taxes);

W fraudulent, unfiled or late filed tax obligations;

W fraud claims;

These are claims arising from false pretenses or representation or from actual fraud, including certain claims presumed to be nondischargeable for the purchase of luxury goods or use of credit cards, and from false or fraudulent financial statements in writing regarding a debtor's or insider's condition. 11 U.S.C. §523(a)2)

W unlisted debts

These include claims not listed or scheduled in an asset case or in time to permit a timely non-dischargeable debt complaint to be filed;

W defalcation, larceny or embezzlement debts

W long term debts

W student loan obligations, expanding non-dischargeable student

loans to for profit and non-governmental entities. 11 U.S.C. § §523(a)(8)(B).

W DUI obligations

W criminal restitution and criminal fines

W restitution or damages from a civil action due to willful or malicious injury to a person

In addition, there will be NO discharge at all under Chapter 13 if:

1. the debtor received a discharge in a Chapter 7, 11 or 12 cases within 4 years of the filing of the Chapter 13 case 11 U.S.C. §1328(f)(1)

2. the debtor received a discharge in a Chapter 13 case within 2 years of filing the present case 11 U.S.C. §1328(f)(2); This was supposed to prevent back-to-back filings, but most commentators say that the two-year period begins to run with the order for relief in the first case, so there are few cases which are going to be prohibited from new filings under this provision.

3. the debtor failed to complete an educational course concerning personal financial management as approved by the United States Trustee 11 U.S.C. §1328(g)

4. the debtor does not certifies that all amounts due to support obligations are fully paid. 11 U.S.C. §1328(a).

NOTE: The fact that the debtor cannot receive a discharge does not mean that the Chapter 13 case cannot be filed or a plan be confirmed. The plan can be confirmed and completed. I would file a report of completion. The debtor simply

won’t receive a discharge. The U.S. Trustee’s Office will file an adversary proceeding at the beginning of any Chapter 13 case to determine if the debtor is eligible for discharge to make sure that all parties are clear that the debtor will not receive a discharge at the end of the case.

What kind of discharge is available in Chapter 13 anyway?

The debtor will still receive a discharge on the following debts–and these are not dischargeable in any other chapter.

1. Tax “gap claims” specified in 11 U.S.C. §507(a)(3);

2. Tax debts specified in 11 U.S.C.§507(a)(8)(A), (B), (D), (E), (F), and (G)–after full payment.

Note that prior to October 17, 2005, "full payment" meant that priority tax claims had to be paid 100% over the life of the Plan, but they did not have to be paid interest because the interest was discharged. *See, In re Smith,* 196 B.R.565 (Bankr. M.D. Fla. 1996). Under the present Code, trust fund taxes, taxes due on late tax returns filed within two years of the bankruptcy, and taxes due from tax evasion situations, interest will continue to be owed by the Debtor, even after repayment of 100% of these tax claims. *See, Keith M. Lundin, Chapter 13 Bankruptcy, 3d Ed*., §513.1 at 513-4 to 513-5 (2000 and 2006 Supplement). Taxes that are a priority claim because they came due within three years of the bankruptcy filing or within the 240-day assessment rule [§507(a)(8)(A)], or excise taxes [§507(a)(8)(E)] or were for a "pecuniary loss penalty" [§507(a)(8)(G) – which may include the 100% penalty for "responsible

parties" failing to pay corporate taxes--remain dischargeable in a Chapter 13, and as long as "full payment" is provided for in the Plan, interest will be discharged, just as it was pre-BAPCPA. *See, Keith M. Lundin, Chapter 13 Bankruptcy, 3d Ed.*, §548.1 at 548-2 to 548-3 (2000 and 2006 Supplement).

3. Debts for willful *and* malicious injury by the debtor to another entity or property of another entity. (One trustee pointed out that this would not include as dischargeable a debt for a willful *or* malicious injury.)

4. Debts for a fine, penalty or forefeiture to a governmental unit not compensation for an actual pecuniary loss, other than a tax penalty;

5. Debts which were or could have been listed or scheduled in a prior case in which the debtor waived discharge or was denied discharge pusuant to 11 U.S.C. 727(a)(2), (3), (4), (5, (6) or (7);

6. Debts in a judgment, order or decree issued by a federal depository institution’s regularly agency arising from fraud or defalcation;

7. Debts for malicious or reckless failure to fulfill any commitment to a federal depository institution’s regulatory agency to maintain capital;

8. Debts incurred to pay a tax to the United States or to a governmental unit other than the United States which would be nondischargeable under 11 U.S.C. 523(a)(1);

9. Debts to a spouse, former spouse, or child of the debtor and not of the kind defined as a domestic support obligation incurred in the course of a divorce or separation;

10. Debts for a fee or assessment due and payable after the order for relief to a condominium, co-cop or homeowner's association in connection with the debtor's continued legal, equitable or possessory ownership interest;

11. Debts of a prisoner imposed by any court under 28 U.S.C. §1915 for filing a case, motion, complaint or appeal;

12. Certain debts owed to a pension, profit-sharing, stock bonus or other plan qualified under ERISA and/or the IRC;

13. Debts for violation of federal or state securities laws, or for fraud, deceit, or manipulation in connection with the purchase or sale of securities.

G. DISCHARGE

1. Requirements

To receive a discharge, the debtor must complete the plan, which generally means make all the payments which are due under the confirmation order.

In addition, the debtor must demonstrate that he/she

1. Did not receive a discharge in a case filed under chapter 7, 11, or 12 during the 4-year period preceding the date of the order for relief in the present Chapter 13 case or in a prior Chapter 13 case during the 2-year period preceding the date of such order.

2. Has paid all DSO payments have been made–both pre-and post-petition.

3.Has not incurred any civil or criminal liabilities and there are no pending

proceedings in which the debtor may be found guilty of criminal bankruptcy violations or liable for civil SEC violations, civil RICO violations or any criminal act, intentional tort, or willful or reckless misconoduct that caused serious physical injury or death to an individual during the course of the case;

4. Has completed a debtor education course BEFORE making the last payment of his/her plan, and

5. If the debtor is making any direct payments to creditors, that he/she is current on those payments.

AN OPTION TO CONSIDER--A 70% PLAN.

Under Section 727(a)(9), the Court shall grant a discharge in a Chapter 7 case, unless the debtor received a discharge in a Chapter 13 case within the past six years unless in the Chapter 13 case, the debtor paid 100% of the allowed unsecured claims in such case; OR paid 70 percent of such claims and was proposed by the debtor in good faith and was the debtor's best effort. So, if a debtor completes a less than 70% Chapter 13 Plan, he/she cannot receive a Chapter 7 discharge for six years from the date of the filing of the Chapter 13.

If a Chapter 13 Plan cannot be completed as confirmed, the debtor may be eligible for hardship discharge under Section 1328(b). The debtor has to file a motion seeking such discharge and bears the burden of proof to show that

(1) the debtor's failure to complete such payments is due to circumstances for which the debtor should not justly be held accountable;

(2) the value, as of the effective date of the plan, of property actually

distributed under the plan on account of each allowed unsecured claim is not less than the amount that would have been paid on such claim if the estate of the debtor had been liquidated under chapter 7 of this title on such date; and

(3) modification of the plan under section 1329 of this title is not practicable.

Essentially, in order to qualify for a hardship discharge, the failure to complete the Plan payments must not be the fault of the Chapter 13 debtor, and the "best interest of creditors" (a.k.a. the "liquidation test") must be met based upon the monies that were actually distributed to unsecured creditors, and there’s nothing else the debtor can do.

A hardship discharge is almost identical to a Chapter 7 discharge, except that the personal liability of the Chapter 13 debtor for long term debts not scheduled to be paid during the pendency of the Chapter 13 Plan – like a home mortgage – are not discharged by a hardship discharge.