Educational Materials
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SYMPOSIUM

BAPCPA at Ten

Presented by: NCBJ – National Conference of Bankruptcy Judges
WELCOME AND INTRODUCTION OF THE SPEAKERS
Hon. Colleen A. Brown – U.S. Bankruptcy Court, D. VT (moderator)

1. HOW COURT AND LAWYER INVOLVEMENT SHIELDS CONSUMERS FROM THE WORST EFFECTS OF BAPCPA
   Angela Littwin - University of Texas School of Law

2. PROTECTING NEST EGGS AND OTHER RETIREMENT BENEFITS IN BANKRUPTCY POST-BAPCPA
   Tara Twomey – The National Consumer Law Center

3. TREATMENT OF DIVORCE / FAMILY CLAIMS, POST-BAPCPA AND THE CHANGED ROLE OF THE TRUSTEE IN CONSUMER CASES
   Lynne Riley - Casner & Edwards LLP, Boston, MA

4. STATE COLLECTION REMEDIES VS. BANKRUPTCY PREFERENCE RECOVERY: PRE- AND POST-BAPCPA POLICY
   Lawrence Ponoroff – University of Arizona James E. Rogers College of Law

5. FILING CHARACTERISTICS AND SUCCESS RATES OF INDIVIDUAL CHAPTER 11 DEBTORS PRE- AND POST-BAPCPA
   Anne Lawton – Michigan State University College of Law
Adapting to BAPCPA: How Court and Lawyer Involvement Shielded Consumers from BAPCPA’s Worst Effects

Angela Littwin, Professor, University of Texas School of Law

“[T]he most striking feature of consumer bankruptcy practice is that it exists. It not only exists—it is a booming practice area, one of the few where middle to lower-middle class consumers are not only served, but are the mainstay of the practice.” —Jean Braucher

To paraphrase the late Professor Jean Braucher, who is missed throughout the bankruptcy community, the most striking feature of post-BAPCPA consumer bankruptcy practice is that it continues to exist and provide relief for middle to lower-middle class consumers. This is not to minimize the damage BAPCPA inflicted. Attorney fees have risen significantly, and the most comprehensive study to date suggests that BAPCPA played a causal role. This may have left reputable attorneys vulnerable to price undercutting by lawyers and petition preparers who cut corners. In addition, a recent analysis by the Federal Reserve Bank of New York suggests that BAPCPA caused a large, permanent drop in the number of consumer Chapter 7 cases, with below-median-income consumers experiencing the largest filing decline. Nevertheless, BAPCPA has not been the complete catastrophe for consumer bankruptcy that many predicted, and approximately one million consumers per year still seek bankruptcy relief. This presentation considers the questions of why and how consumer bankruptcy avoided disaster.

Why?

I argue that a key factor in preventing catastrophe is that consumer bankruptcy is a judicial system, not an administrative one. Bankruptcy judges and lawyers want consumer

2 See Lois R. Lupica, The Consumer Bankruptcy Fee Study: Final Report, 20 AM. BANKR. INST. L. REV. 17, 85-89 (2012). Professor Lupica has conducted the most comprehensive study of the post-BAPCPA increase in consumer bankruptcy attorney fees. Regression analysis in the pin-cited pages suggests that BAPCPA caused this upward trend.
3 Id. at 92-93 & 111-114.
4 Stefania Albanesi & Jaromir Nosal, Insolvency after the 2005 Bankruptcy Reform, FEDERAL RESERVE BANK OF NEW YORK STAFF REPORTS, 9-12 (Staff Report No. 725, April 2015).
5 Administrative Office of U.S. Courts, Table F, Bankruptcy Filings (March 31, 2015).
bankruptcy to be effective and made sure that system continued to run smoothly. This stands in sharp contrast to administrative safety-net programs, which have a long, troubled history in the United States. Programs such as welfare, Social Security disability, and even benefits for veterans tend to create technical barriers that dwarf those imposed by BAPCPA and leave claimants mired in bureaucracy for years at a time. These systems are relevant because BAPCPA was not an isolated event. Rather, it was part of a broader trend, known as “bureaucratic disentitlement,”6 in which policymakers who do not have the political leverage to eliminate part of the safety net instead erect procedural hurdles that make its benefits more difficult to access. Key BAPCPA features, such as limiting judicial discretion, imposing steep paperwork requirements, and attacking consumer lawyers, are all part of the “bureaucratic disentitlement” playbook. From this perspective, BAPCPA’s unintended consequences – immense costs and procedural hurdles for consumers without a corresponding increase in distributions to creditors7 – may very well have been intended. Death by a thousand paper(work) cuts may have always been the point.8

Despite the obvious differences between consumer bankruptcy and the administrative redistributive programs, they are all subject to this type of attack because they are part of the government safety net and thus trigger a fundamental moral anxiety: the fear that they enable a strategic few to receive something for nothing while others work for what they get. When the rates of program usage rise, this anxiety can harden into a conviction that beneficiaries must be abusing the system. But the definition of abuse becomes confused—applying both to specific non-needy persons taking advantage of a program’s generosity and to the entire growing population of beneficiaries, who must be abusing the system because there could not possibly be such a large number of people in genuine need. In other words, increasing system use becomes the evidence of abuse. Consumer bankruptcy is particularly vulnerable to these arguments because the consumer credit industry has a permanent stake in encouraging them.

Yet despite BAPCPA, consumer bankruptcy remains significantly more accessible – meaning that consumers are less likely to be denied relief for procedural or cost reasons – than administrative safety-net programs. I argue that the difference is judicial. Factors such as paid attorneys, high-quality judges, and the prestige-enhancing association with its corporate cousin help separate consumer bankruptcy from welfare programs. Debtor attorneys

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7 Lupica, *supra* n. 2, at 90-91.
8 See, e.g., Ronald J. Mann, *Bankruptcy Reform and the “Sweat Box” of Credit Card Debt*, 2007 U. ILL. L. REV. 375 (2007) (arguing that BAPCPA’s most important effect would be to delay the bankruptcy filings of insolvent consumers rather than to screen out high-income debtors).
contribute to the smooth running of the system, protect their clients from overreaching, and lobby against bankruptcy legislation that could potentially harm consumers further. Judges drawn from the top tiers of the legal profession provide another bulwark against the type of long-term decline seen in administrative programs. And the relationship with corporate bankruptcy helps attract a high caliber of professionals to all areas of the field. In contrast, administrative safety net programs suffer from shortages of lawyers available to help claimants navigate their immense procedural hurdles. Additionally, the caliber of the administrative officials who make benefits decisions tends to decline over the life of a program. Currently, a significant portion of the frontline decision makers in these administrative benefits systems lack college degrees. The cumulative effect of these trends is that the quality of decision making tends to be poor. Claimants suffer through multiple rounds of appeals, remands, and further appeals before reaching a final result. Paradoxically, consumer bankruptcy may be a judicial system that accomplishes its administrative functions more effectively than many administrative programs do.

How did consumer bankruptcy survive relatively intact?

The short answer is that professionals in all roles adapted. I am still in the process of interviewing consumer bankruptcy professionals about the strategies they developed – and welcome volunteers – so what follows is a very preliminary outline. Because so many of BAPCPA’s provisions were directed at the lawyers who represent consumer debtors, I am beginning with them, although I have already learned of some surprising challenges other professionals have faced.

Consumer Attorney Strategies:

- Not surprisingly, hiring more staff, investing more in training themselves and their staff members, spending more time on each case
- Investing more heavily in technology
- Covering the immediate post-BAPCPA case drought with funds from the pre-implementation rush
- Growing their businesses with referrals from attorneys who left the field

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Other Mitigating Factors:

- Due diligence and audits were much less of a problem than expected.
- Once several key issues reached the circuit level, things returned to normal for some lawyers.
- Technology may have limited the damage caused by BAPCPA’s increased paperwork requirements.
  - Legal software made the paperwork easier than expected.
  - Clients increasingly had computers or other electronic means of retaining documents.
- Some of the initial judicial decisions limited the reach of the most feared BAPCPA provisions.

Changes in the composition of the debtor bar:

- Anecdotally, many lawyers left the field, mostly “dabblers” or those near retirement. This may appear to be a negative development, but the resulting referrals to the remaining full-time bankruptcy practitioners may have enabled many to survive.
- Few new lawyers appear to be entering the field. This is a troubling trend that implicates the long-term sustainability of consumer bankruptcy practice. It could also result in a backlash when the next consumer-credit crisis occurs and there are not enough bankruptcy specialists to meet the demand.
Protecting Nest Eggs and Other Retirement Benefits in Bankruptcy

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Synopsis
The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) made significant changes in the treatment of retirement benefits, assets, and contributions. The numerous retirement-related amendments included in BAPCPA generally provided greater protection to consumer debtors. They addressed the growing gap between the anachronistic provisions of the Code and the shifting ways in which Americans save for retirement. BAPCPA brought uniformity and clarity to the exemption of retirement funds, which had long been subject to a patchwork of state laws and judicial decisions. Congress clarified that social security benefits, often considered disposable income prior to BAPCPA, were no longer included in "current monthly income" under 11 U.S.C. § 101(10A)(B). But ten years after the enactment of BAPCPA, outstanding questions remain. For amendments that seemed clear, the devil is often in the details.

- While social security is not disposable income, is it nevertheless bad faith not to contribute such benefits to a chapter 13 plan?
- Can a debtor voluntarily contribute social security benefits to make the plan feasible?
- Can the debtor later decide to stop contributing social security benefits?
- Funds used to repay retirement loans are not projected disposable income, but are retirement account distributions also off the table?
- Finally, the area showing the deepest splits among the courts is the debtor’s ability to make voluntary retirement contributions during chapter 13.

I. Change in the Way Americans Save for Retirement

A. Dramatic Shift from Defined Benefit Plans (“DB”) to Defined Contribution Plans (“DC”)

1. 1983 – workers with: DB – 62%, DC – 12%

2. 2010 – workers with: DB – 19%, DC – 68%
[From Center for Retirement Research at Boston College]
3. Risk distribution pros and cons
   a. Shift in investment risk from corporations and government to households
   b. Employer insolvency risk

B. Retirement Savings Crisis

1. Americans are living longer – for those who reached age 65 in 2011, they are expected to live, on average, another 21 years to age 86.

2. Three strategies for retirement savings
   a. Save during retirement years
      Aon Hewitt, The Real Deal: 2012 Retirement Income Adequacy at large Companies; Employment Benefit Research Institute
   b. Spend less in retirement
   c. Delay the age of retirement

II. Pre-BAPCPA Treatment of Retirement Assets and Benefits

A. Plans Subject to ERISA and Patterson

1. Purpose behind the Employment Retirement Income Security Act (ERISA) is to make certain that "if a worker has been promised a defined pension benefit upon retirement—and if he has fulfilled whatever conditions are required to obtain a vested benefit—he actually will receive it." Patterson v. Shumate, 504 U.S. 753, 765 (1992).

2. 11 U.S.C. § 541(a). Estate created upon filing of the petition. Property of the estate is broadly construed and includes all legal or equitable interests in property whether tangible or intangible, real or personal as of the commencement of the case. Some property specifically excluded from the estate.
   a. Section 541(c)(2) excludes property that is subject to a “restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law.”

3. In Patterson v. Shumate, 504 U.S. 753, 760 (1992), the Supreme Court held that the anti-alienation provision in “ERISA-qualified” pension plans was a restriction on transfer enforceable under “applicable non-bankruptcy law.”
a. Is the plan “subject to ERISA”?
   i. Employee benefit plan established by an employer engaged in interstate commerce (with limited exceptions)
   ii. “Each pension plan shall provide that benefits provided under the plan may not be assigned or alienated…” 29 U.S.C. § 1056(d)(1).

b. Must the ERISA trust be entitled to favorable tax treatment under IRC § 401? See In re Sewell, 180 F.3d 707 (5th Cir. 1999) (ERISA plan not required to be tax qualified); Matter of Baker, 114 F.3d 636 (7th Cir. 1997); In re Handel, 301 B.R. 421 (Bankr. S.D.N.Y. 2003) (if plan’s restriction on alienation is enforceable under ERISA, it need not be tax-qualified to be excluded from estate under 541(c)(2)).

c. Was plan operated in violation of ERISA? Courts have split on whether there is an equitable exception to ERISA’s anti-alienation provision. Compare Matter of Baker, 114 F.3d 636 (7th Cir. 1997) (plan remained subject to ERISA despite debtor’s violations of ERISA fiduciary duties in his capacity as plan trustee), and In re Handel, 301 B.R. 421 (Bankr. S.D.N.Y. 2003) (debtor could rely on anti-alienation clause although he exercised control over plan assets in violation of ERISA requirements), with In re Harris, 188 B.R. 444 (Bankr. M.D. Fla. 1995) (debtor's interest in profit sharing plan was property of the estate, as plan was not administered in compliance with ERISA and IRC), and In re Lane, 149 B.R. 760, 765-66 (Bankr. E.D.N.Y. 1993) (debtor-employer's interest in benefit plan was not excluded from property of the estate since plan failed to meet minimum contribution requirements). See also In re Guidry, 493 U.S. 365 (1990) (refusing to impose equitable limitation on ERISA anti-alienation provision).

4. Tricky areas

a. Qualified Domestic Relation Orders (QDROs) – An alternate payee under a QDRO is considered an ERISA plan beneficiary. See 29 U.S.C. § 1056(d)(3)(J); Nelson v. Ramette, 322 F.3d 541 (8th Cir. 2003). But BEWARE of property interests that arise after the filing of a complaint/petition for divorce, but before a divorce decree or QDRO is issued. Compare Ostrader v. Lalchandani, 279 B.R. 880 (B.A.P. 1st Cir. 2002) (interest in ERISA plan not property of the estate where bankruptcy filed after divorce commencement but before QDRO entered), and In re West, 507 B.R. 252 (Bankr. N.D. Ill. 2014) (defective QDRO did not deprive debtor of ability to exempt interest in ex-spouse’s pension plan under state law exemption), and In re Remia, 503 B.R. 6 (Bankr. D. Mass. 2013) (divorce judgment gave debtor interest in funds that could be exempted even in absence of QDRO),
with In re Burgeson, 504 B.R. 800 (Bankr. W.D. Pa. 2014) (in the absence of QDRO, debtor was not a beneficiary of ex-spouse’s pension plan, but had only an equitable claim under state law and that claim was property of the estate).

b. Employee/owners – Yates v. Hendon, 541 U.S. 1 (2004) (sole shareholder and president of professional corporation could qualify as “participant” in ERISA pension plan sponsored by corporation as long as plan covered one or more employees other than himself and his wife). See 29 C.F.R. § 2510.3-3(c)(1) (corporation’s sole owner is not an “employee” for purposes of ERISA); Private Capital Investments v. Schollard, No. 07-CV-0757C SR, slip op. at 1 (Bankr. W. D. N.Y. June 10, 2014) (finding an owner and sole employee of ERISA anti-alienation provision is valid as long as there is another non-spouse employee–like a daughter); In re Lane 149 B.R. 760 (Bankr. E.D.N.Y. 1993) (holding that because debtor is and always had been the only participant in the retirement plan, it cannot be subject to the provisions of ERISA).


B. Exemptions and Rousey

1. The purpose of exemption law is to allow debtors to keep those items of property deemed essential to daily life. In the bankruptcy context, exemptions serve the overriding purpose of helping the debtor to obtain a fresh start by maintaining essential property necessary to build a new life. See H.R. Rep. No. 95-595, at 117 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6078 (purpose of this scheme is to provide “adequate exemptions and other protections to ensure that bankruptcy will provide a fresh start.”).

2. Section 522(d)(10)(E) – “payment under a stock bonus, pension, profit-sharing, annuity, or similar plan or contract on account of illness, disability, death, age, or length of service, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor…”

4. State law exemptions


c. Illinois, 735 ILCS 5/12-1006; In re West, 507 B.R. 252 (Bankr. N.D. Ill. 2014) (interest in retirement plan property of the estate, but exempt under state law).


e. Wis. Stat. § 815.18(3)(j); In re Kirchen, 344 B.R. 908 (Bankr. E.D. Wis. 2006) (inherited IRA not exempt).

C. Projected Disposable Income and Social Security

1. Majority of courts interpret disposable income broadly to include Social Security benefits. Hagel v. Drummond, 184 B.R. 793 (9th Cir. 1995) (social security disability benefits had to be included in calculating disposable income); In re Cornelius, 195 B.R. 831 (Bankr. N.D.N.Y. 1995) (social security received on behalf of minor daughter was disposable income); In re Schnabel, 153 B.R. 809 (Bankr. N.D. Ill. 1993) (social security benefits were disposable income).

      (a) The right of any person to any future payment under this subchapter shall not be transferable or assignable, at law or in equity, and none of the moneys paid or payable or rights existing under this subchapter shall be subject to execution, levy, attachment, garnishment, or other legal process, or to the operation of any bankruptcy or insolvency law.
      (b) No other provision of law, enacted before, on, or after April 20, 1983, may be construed to limit, supersede, or otherwise modify the provisions of this section except to the extent that it does so by express reference to this section.
   (emphasis added).

III. BAPCPA Retirement Provisions

A. Tax-Qualified Retirement Plans

Congress enacted a broad package of retirement-related provisions in the 2005 amendments that protected tax-qualified retirement plans. See 11 U.S.C. §§ 362(b)(19), 522(b)(3)(C), (b)(4), (d)(12), 523(a)(18), 1322(f). Section 362(b)(19) excepts from the automatic stay withholding from the debtor’s income for repayment of loans from tax-qualified accounts. Section 522(b)(3)(C) and 522(d)(12) protect retirement funds in certain tax-exempt accounts. Section 522(b)(4) establishes a presumption in favor of exemption when the retirement fund has received a favorable determination from the Internal Revenue Service, and also applies the exemption to certain transfers from one tax-exempt account to another. Section 523(a)(18) excepts from discharge retirement plan loans. Finally, section 1322(f) limits the ability of a debtor to alter the terms of a retirement plan loan in a chapter 13 plan and specifies that funds used to repay those loans are not “disposable income” for purposes of the chapter 13 projected disposable income test. 11 U.S.C. § 1325(b)(5); see Hamilton v. Lanning, 560 U.S. 505 (2010) (discussing the projected disposable income test in chapter 13).

All of these sections have their origins in an amendment to the Consumer Bankruptcy Reform Act of 1998, known as the “Hatch Amendment.” See H.R. 3150, 105th Cong. (1998); 144 Cong. Rec. S10596-01 (September 18, 1998) (Amendment 3600: Protection of Retirement Savings). According to Senator Hatch, one of the co-sponsors of the amendment, the statutory language was designed to: “Provide a uniform exemption for all types of tax-favored qualified pension plan assets in bankruptcy including Roth IRAs whose status under current bankruptcy law is uncertain, protect retirement assets that are in the process of being rolled over into new qualified plan, and protect loans from pension funds in bankruptcy.” Id. Approval of the amendment was unanimous, see id., and the language of the amendment carried through seven more years of congressional debate on bankruptcy reform virtually unchanged, and was finally enacted as part of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23, § 224 (2005).

1. Retirement Funds Exemption

   a. Section 522(b)(3)(C) applicable in opt-out states; section 522(d)(12) available under federal exemption scheme: “retirement funds to the extent that those funds are in a fund or account that is exempt from taxation under section 401, 403, 408, 408A, 414, 457 or 501(a) of the Internal Revenue Code of 1986.”
b. Devil in the Details
   i. Is the fund or account exempt from taxation?
      
      In re Miller, 500 B.R. 578 (B.A.P. 8th Cir. 2013) (individual retirement annuity funded by a direct rollover from another tax-qualified IRA was tax-exempt under IRC § 408(b) and therefore exemptible in bankruptcy under 522(b)(3)(C)).

   ii. Whether operation of plan or account renders it unqualified?
      An IRA loses its tax-exempt status if the owner "engages in any transaction prohibited by section 4975" of the tax code. I.R.C. § 408(e)(2)(A).

      • Daley v. Mostoller, 717 F.3d 506 (6th Cir. 2013) (agreement granting lien on all accounts, including IRA, did not cause IRA to lose tax exempt status); see also IRS Announcement 2011-81, 2011-52 I.R.B. 1052 (mere existence of a "cross-collateralization agreement," as the IRS calls it, does not by itself disqualify an IRA from exempt status).

      • In re Plunk, 481 F.3d 302 (5th Cir. 2007) (court could consider disqualifying event—payment of personal bills from plan assets—occurring after IRS last determination).

      • In re Willis, No. 09-82303-CIV, slip op. at 1 (S.D. Fla. April 6, 2010), aff’d sub nom. 424 Fed. App’x. 880 (11th Cir. April 21, 2011) (IRA funds not exempt because debtor engaged in prohibited transactions causing assets to lose tax-exempt status).

   iii. Are inherited IRAs exempt?
      Rameker v. Clark, 134 S. Ct. 2242 (2014) (IRA funds debtor had inherited from her late mother were not “retirement funds,” as that term was used in bankruptcy exemption statute).

      But see state law exemptions

B. Social Security Benefits

1. 58 million Americans received approx. $816b in Social Security benefits in 2013; average retirement benefits - $1269; approximately 35% of Americans over 65 rely completely on Social Security.

2. Social Security Not Projected Disposable Income

   a. Disposable income test: Trustee or holder of an allowed unsecured claim may object to confirmation if the debtor does not propose to pay to unsecured creditors all of his or her projected disposable income to be received during the applicable commitment period. 11 U.S.C. § 1325(b)(1)(B). Section 1325(b)(2) defines disposable income as “current monthly income received by the debtor ... less amounts reasonably necessary to be expended.” In turn, “current monthly income” is defined as “the average monthly income from all sources that the debtor receives . . . derived during the 6-month period” prior to filing the bankruptcy petition. 11 U.S.C. § 101(10A)(A).
b.  *Baud v. Carroll*, 634 F.3d 327 (6th Cir. 2011); *Mort Ranta v. Gorman*, 721 F.3d 241 (4th Cir. 2013); *Beaulieu v. Ragos*, 700 F.3d 220 (5th Cir. 2012) (stating that it makes little sense to circumvent the social security exclusion by allowing such benefits to be considered projected disposable income); *Cranmer v. Anderson*, 697 F.3d 1314 (10th Cir. 2011) (rejected the chapter 13 trustee’s attempts to characterize the receipt of social security benefits as one of those “unusual” circumstances that justified departure from the statutory formula).

3.  A Question of Bad Faith

   a.  Good faith test requires that “the plan [be] proposed in good faith and not by any means forbidden by law.” 11 U.S.C. § 1325(a)(3). The good faith standard provides a check on actions that abuse the bankruptcy system.

   b.  Courts have generally rejected attempts to reframe disposable income objections as good faith objections.

   c.  *Welsh v. Drummond*, 711 F.3d 1120 (9th Cir. 2013); *In re Thompson*, 439 B.R. 140 (B.A.P. 8th Cir. 2010) (exclusion of social security income from plan payments, standing alone, could not prevent debtors from establishing good faith); *Mort Ranta v. Gorman*, 721 F.3d 241, 253 n.15 (4th Cir. 2013); *In re Worthington*, 507 B.R. 276 (Bankr. S.D. Ind. 2014) (failure to contribute all social security benefits does not constitute bad faith); *In re Melander*, 506 B.R. 855 (Bankr. D. Minn. 2014) (chapter 13 debtors control the amount of social security benefits that are contributed to plan).

4.  Feasibility

   a.  Section 1325(a)(6) requires that the “debtor will be able to make all payments under the plan and to comply with the plan.” If the plan does not meet this standard, often called the feasibility test, confirmation may be denied. Under this test, the budget figures must show sufficient income or other financial resources to enable the debtor to make the payment proposed. A plan is considered feasible if the debtor’s net monthly income, as reflected on Schedule J, is equal to or greater than the debtor’s proposed plan payment.

   b.  *Mort Ranta v. Gorman*, 721 F.3d 241 (4th Cir. 2013). Trustee argued that if social security was not considered projected disposable income then it could not be used in determining the feasibility of the plan. The court found that nothing in the Code supports the bankruptcy court’s holding that if social security income is not part of disposable income, it cannot be used to support feasibility. To the contrary, the court cited a string of cases, legislative history, and treatises in support of its finding that social security income has historically been used to support feasibility. “We therefore hold,
in agreement with the Sixth Circuit, that ‘a debtor with zero or negative projected disposable income may propose a confirmable plan by making available income that falls outside of the definition of disposable income—such as . . . benefits under the Social Security Act—to make payments under the plan.’” (citing Baud, 634 F.3d at 352 n.19). See also In re Franklin, 506 B.R. 765 (Bankr. C.D. Ill. 2014) (debtor may voluntarily contribute social security proceeds to estate or use proceeds to fund a plan).

C. Retirement Loan Repayment as Projected Disposable Income

1. Statutory Provision - 1322(f) – any amounts required to repay loan from retirement fund account does not constitute disposable income.

2. Deduct amount in full or prorate over the plan? Compare In re Haley, 354 B.R 340 (Bankr. D.N.H. 2006) (deduction allowed in full), and In re Wiggs, 2006 WL 2246432 (Bankr. N.D. Ill. 2006) (same), with In re Kofford, No. BR 12-29134, slip op. at 1 (Bankr. D. Utah Dec. 4, 2012) (requiring debtor to prorate loan payments over the plan, but also misconstruing In re Lasowski, 575 F.3d 815 (8th Cir. 2009), which required a step up plan, not proration).

D. Retirement Contributions in Bankruptcy

1. Statutory Provision
   Section 541(b)(7): Property of the estate does not include:
   (7) any amount—
   (A) withheld by an employer from the wages of employees for payment as contributions—
   (i) to—
   (I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 or under an employee benefit plan which is a governmental plan under section 414(d) of the Internal Revenue Code of 1986;
   (II) a deferred compensation plan under section 457 of the Internal Revenue Code of 1986; or
   (III) a tax-deferred annuity under section 403(b) of the Internal Revenue Code of 1986; except that such amount under this subparagraph shall not constitute disposable income as defined in section 1325 (b)(2); or
   (ii) to a health insurance plan regulated by State law whether or not subject to such title; or
   (B) received by an employer from employees for payment as contributions—
   (i) to—
(I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 or under an employee benefit plan which is a governmental plan under section 414(d) of the Internal Revenue Code of 1986;

(II) a deferred compensation plan under section 457 of the Internal Revenue Code of 1986; or

(III) a tax-deferred annuity under section 403(b) of the Internal Revenue Code of 1986;

except that such amount under this subparagraph shall not constitute disposable income, as defined in section 1325(b)(2); or

(ii) to a health insurance plan regulated by State law whether or not subject to such title;

2. Three Views

a. Chapter 13 debtors not allowed to make voluntary post-petition retirement contributions in any amount. In re Seafort, 669 F.3d 662 (6th Cir. 2012); In re Parks, 475 B.R. 703 (B.A.P. 9th Cir. 2012).


c. Permits “continued” contributions to retirement accounts. In re Seafort, 437 B.R. 204 (B.A.P. 6th Cir. 2010), aff’d on other grounds, 669 F.3d 662 (6th Cir. 2012); In re Jensen, 496 B.R. 615 (Bankr. D. Utah 2013).

E. Retirement Account Distributions as Projected Disposable Income

1. Statutory Provision – 11 U.S.C § 101(10A)

The term “current monthly income”—

(A) means the average monthly income from all sources that the debtor receives (or in a joint case the debtor and the debtor’s spouse receive) without regard to whether such income is taxable income, derived during the 6-month period ending on—

(i) the last day of the calendar month immediately preceding the date of the commencement of the case if the debtor files the schedule of current income required by section 521 (a)(1)(B)(ii); …
2. Retirement Distributions are generally not PDI
   - Conversion of pre-petition assets from one form to another, even to cash, does not produce income.
     • In re Zahn, 391 B.R. 840, 845 (B.A.P. 8th Cir. 2008) (IRA distributions taken by non-debtor spouse not treated as disposable income and treated similarly to withdrawals from savings accounts).
     • See also Simon v. Zittel, 2008 WL 750346 (Bankr. S.D. Ill. Mar. 19, 2008) (holding that 401K distributions taken within the six months prior to filing Chapter 13 did not constitute “income from all sources” within the meaning of the § 101(10A)); In re Breeding, 366 B.R. 21, 25 (Bankr. E.D. Ark. 2007) (liquidation of two certificates of deposits did not produce income); but see In re DeThample, 390 B.R. 716, 726 (Bankr. D. Kan. 2008) (holding that a pre-petition distribution from a debtor’s 401(k) is included in a CMI, but may be disregarded when determining debtor’s projected disposable income).
   - Pension plan distributions (even those with contributory elements) may be treated differently.
     • In re Coverstone, 461 B.R. 629, 634 (Bankr. D. Idaho 2011) (voluntary contributions were but one factor of a “complex algorithm” and that the majority of the contributory pension income he was receiving at present was, ultimately, provided by his employer, and therefore, considered disposable income).
Development and Treatment of Divorce-Related and Domestic Claims in Bankruptcy

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Synopsis

The 1994 Bankruptcy Code Amendments and the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) sought to ease the impact of competing interests by providing enhanced protections to non-debtor spouses and dependents through the addition of divorce-related Bankruptcy Code provisions. These divorce and family-related provisions encompass four areas of enhanced protection: (1) diminished applicability of the automatic stay to domestic support obligation (DSO) creditors; (2) elevated priority status of DSOs; (3) expanded non-dischargeability of DSOs and other divorce-related domestic debts; and (4) heightened notice requirements to DSO creditors. These protections are further enhanced by BAPCPA’s expansion of jurisdiction to family courts and the comity that already existed between bankruptcy and family courts. Strategically timing the commencement of divorce and bankruptcy proceedings for divorcing spouses can also impact the relief afforded to families when these two areas of law intersect. And finally, repeal of the Defense of Marriage Act and now the Supreme Court’s decision that same-sex couples have an equal right to marriage (and therefore divorce) expands the availability of bankruptcy to same-sex couples and diminishes the conflict of law issues that same-sex couples previously faced regarding the adjudication of divorce and bankruptcy matters.
Outline

I. Easing the Impact of Competing Interests through Enhanced Protections

1. Automatic Stay; § 362
   a. 1994 Amendments: Petition no longer stays certain domestic relations proceedings
   b. BAPCPA: Enhanced protections
      • Filing petition no longer stays collection/payment of DSO from property that is not property of estate
      • In Chapter 13, can collect DSO from post-petition income if judicial order; can probably get order postpetition; but confirmed plan is res judicata
      • No stay for non-economic matters (custody, visitation, dissolution)
      • Exceptions to stay for domestic support creditors under Social Security Act (withholding & suspension licenses, credit reporting, etc.)
      • Mandatory relief: adjudication/enforcement of DSOs
      • For cause relief: adjudication of property rights in marital assets
         • Bankruptcy court balances prejudice to debtor’s estate against hardship incurred by movant if relief denied
         • Family court adjudicates property rights of divorcing spouses then bankruptcy court addresses impact on debtor’s case; trustee oversees/intervenes in divorce case; bankruptcy court retains jurisdiction for final review and judgment
      • Abstention and remand to divorce court

2. Elevated Priority Status of Support Claims; § 507(a)(1)
   a. 1994 Amendments:
      • Support claims upgraded from general unsecured to priority claim status
      • Ranked 7 of 9 categories
      • Precludes preference attack on support payments
b. BAPCPA:

- Defines DSO; Code § 101(14A)
- Expands scope of protected obligations
- Priority status elevated to 1 of 10
- Trustee’s “carve out” for administrative fees and expenses to liquidate assets for DSO creditor
- Trustee must give special notices to DSO creditor
- Exempt property available to DSO creditor
  - Limitation on debtor’s ability to protect exempt assets from DSO creditors; § 522(c)(1), (f)(1)
  - Exempt property subject to execution
  - Debtor precluded from avoiding DSO lien that impairs exemption
- DSO protection in reorganizations
  - Plan confirmation requires DSO payments be current § 1129 (a)(14); § 1225 (a)(7); § 1325 (a)(8)
  - Must certify post-petition DSO payments are current for discharge: § 1228(a); § 1328(a)
  - DSO arrearage paid as 1st priority unless holder agrees otherwise: § 1322 (a)(2); § 1222 (a)(2)
  - Interest allowed on arrearage if authorized under state law; all unsecured claims paid in full: § 1222 (b)(11); § 1322 (b)(10)
  - Failure to pay DSO is “cause” to dismiss or convert: § 1112(b)(4)(P); § 1208(c)(10); § 1307(c)(1)
  - But post-petition DSOs need not be current for discharge of Chapter 11 individual debtor: § 1141(d)(2), (5)

3. Expanded Nondischargeability of support, property settlement and divorce-related debts

a. Expanded Non-dischargeability of Support Claims; § 523(a)(5)

- Precludes discharge of DSO claims

- Federal law determines what debts are “in nature of alimony, maintenance and support;” bankruptcy court makes independent determination whether it’s support under federal definition
  - Intent of parties at time of divorce
    - Income/needs of parties
    - Amount/type of property division
- Number/frequency of payments
- Waiver of alimony/maintenance
- Tax treatment; ability to modify

b. BAPCPA revamped § 523(a)(15) to further strengthen rights of domestic creditors
   - Automatic exception for all non-support marital debts incurred in course of divorce or separation or in connection with divorce or separation-related agreement or decree
   - Excludes all marital and domestic relations debts from discharge
   - Only requirement: Incurred in connection with separation or divorce or related action
   - Expanded jurisdiction of family courts to adjudicate § 523(a)(15) claims
   - Timing requirement deleted – now automatic

c. Why would debtor or DSO creditor file adversary proceeding?
   - Non-DSO marital debt still dischargeable in Chapter 13; § 1328(a)
   - Non-DSO marital debt might be for fraud, breach of fiduciary duty (60 day deadline)
   - Liquidation of exempt property to satisfy DSOs; § 522(c)(1)
   - Burden of proof: preponderance of evidence for all elements on party seeking non-dischargeability

4. Trustee’s notices re: DSO creditors
   a. At case commencement
      - To DSO creditor regarding right to use services of state’s child support enforcement agency; § 704(c)(1)(A)
      - To state’s child support enforcement agency of DSO claim; § 704(c)(1)(B)
   b. When discharge granted
      - to DSO creditor and state’s child support enforcement agency of granting of discharge, address of debtor and his/her employer, any non-dischargeable claims and/or reaffirmed debts; § 704(c)(1)(C)
II. Concurrent and Exclusive Jurisdiction of Bankruptcy and Family Courts

1. Jurisdictional rules potentially enable one court to revisit/invade equitable results of the other
   - General rule is bankruptcy court’s role usually limited to determining state court decision’s impact in debtor’s case; state court decisions usually left undisturbed

2. Potential for results to collide
   - Collusion between debtor and spouse
   - Failure to adhere to state law guidelines/precedent
   - Federal definitions applicable
   - Trustee intervention to protect bankruptcy estate; reservation of final judgment in lift stay orders
   - Fraudulent conveyance and related claims under trustee’s strong arm powers
   - State law defines property rights and interests

3. Exclusive Jurisdiction
   a. Bankruptcy Court
      - Exclusive jurisdiction to determine what constitutes property of the estate and modify or terminate automatic stay; § 541; 28 U.S.C. § 1334(b),(e)
   b. Divorce Court
      - Exclusive jurisdiction to establish/modify DSO or to collect DSO from property that is not property of the bankruptcy estate; § 362 (b)(2); except that Divorce Ct bound by discharge injunction
   c. Intersection
      - Divorce court can order collection from property that is not property of the estate, but determination of what is property of the estate is within exclusive jurisdiction of bankruptcy court

4. Concurrent Jurisdiction of Bankruptcy and Divorce Courts – applying federal law
   a. Automatic Stay; § 362
      - Divorce court can determine whether matter is subject to automatic stay but must rule on applicability of stay prior to acting on underlying domestic-relations matter; 28 U.S.C. § 1334
• Intersection: Divorce court rules on *applicability* of stay but bankruptcy court retains exclusive jurisdiction to *modify* or *lift* the stay
• Impact of divorce court’s erroneous ruling that stay not applicable; decision void as modification of stay without proper jurisdiction
• Impact of divorce court’s correct ruling that stay not applicable; *Rooker-Feldman* bars bankruptcy court’s appellate review of state court judgment
b. Determining whether debt is DSO for ruling on dischargeability under § 523(a)(5)
c. Adjudicating dischargeability of property settlement and non-support marital obligations under § 523(a)(15); expanded by BAPCPA
d. Adjudicate/enforce bankruptcy discharge injunction; § 524(a)

III. Successive vs. Concurrent Proceedings

1. Benefits of joint petition
   • Ease of administration
   • stack exemptions; tenancy by entirety

2. Benefits of divorce decree before bankruptcy
   • Entry of final judgment/vesting of property

3. Impact of concurrent proceedings
   • Equitable liens and constructive trusts
     • Constructive trust established when divorce pending on petition date; *Davis v. Cox* (1st Cir. 2004)
     • No equitable rights vest upon commencement of divorce action; *Musso v. Ostashko* (2nd Cir. 2006)
     • Potential for greater inequality in property division

4. Preferential and fraudulent transfers when divorce predates bankruptcy petition
   • Preference exception for DSOs; § 547(c)(7)
   • Support, property settlement and related agreements or transfers subject to avoidance as fraudulent transfers; § 548, § 544
   • Bankruptcy courts unravel transfers/obligations made w/intent to hinder, delay or defraud creditors even if property division/support obligation blessed by divorce court
IV. Concerns Regarding Bankruptcy Discharge

1. Bankruptcy discharge issues

- Permanent discharge injunction; § 524(a)
- Prohibits state court from modifying divorce decree to reinstate discharged debts, *i.e.* circumvent discharge injunction
- State court may modify to increase support if otherwise justified
- Potential for provisions in divorce decrees and separation agreements to be voided

2. Easing concerns

- BAPCPA: Substantially curtails scope of debtor’s discharge as it relates to domestic creditors and marital debts; renders discharge inapplicable to most domestic relations debts

V. DOMA, Same-Sex Marriage, Conflict of Law Issues

1. Diminishing conflict of law issues

- Repeal of Defense of Marriage Act
  - §2 of DOMA authorized states to refuse to recognize valid same-sex marriages performed in other states, and the rights, claims, and judgments attendant to those marriages
  - Uncertainty surrounded recognition of these marriages and the rights, claims and judgment arising therefrom, in bankruptcy proceedings
- Legalized same-sex marriage
  - Coupled with repeal of DOMA, removes much uncertainty
- Conflict of law and other issues impacted by these developments
  - Joint filings; venue
    - Same-sex married couples can file jointly in all states
    - Proper venue for same-sex spouses filing jointly as long as one spouse is domiciled or has assets in filing state
  - Exemptions; special asset protections
    - Can stack exemptions; utilize tenancy by entirety if applicable; community property laws apply
  - Fraudulent transfer/resulting trust issues/presumptions
    - Presumption of gift between same-sex spouses
  - Dischargeability
    - Non-dischargeability protections for DSOs and other marital debts
  - Priority and enforcement of DSOs
    - DSO protections and enforcement mechanisms; payment of DSO and establishment of lien for DSO immune from preference attack
  - Automatic stay re: DSOs
    - Exceptions to stay for establishment and enforcement of DSOs apply to same-sex spouses/ex-spouses
TALKING POINTS—PREFERENCE LIABILITY & RECOVERY

Ponoroff

I. 1978 Act
   - Historic elimination of intent element of cause
   - Two steps forward, but one step back
   - Dichotomy between equality and deterrence as reflected, respectively, in §§ 547(b) and (c)

II. BAPCPA’s Role in the Tension between State Collection Norms and Bankruptcy’s Equality and Rehabilitation Goals

III. Preference Reform 1978-2005—Most Significant
   - Elimination of “45 days from time debt incurred” language from § 547(c)(2)
   - Enactment of § 550(c)

IV. Impact of BAPCPA on Preference and Preference-Related Laws
   - Collectively the nine amendments have either narrowed the scope of preference liability or expanded defenses
   - Preference provisions in BAPCPA reflect a shift away from a creditor cooperation model and toward a creditor competition model

V. Flawed Premises Underlying BAPCPA’s Changes to the Preference Law
   - Innocent transfers should be exempted from preference recovery—recoupment limited to circumstances where either the debtor or the creditor did something “bad”
   - Trustees routinely abuse the preference power by bringing claims of dubious value to secure quick settlements

VI. Three Key Amendments
   - Further expansion of ordinary course of business defense by disjoining subjective and objective components
   - Extension of relation back period in § 547(e)(2) for security transfers from 10 to 30 days
   - Enactment of a new low-dollar exception in § 547(c)(9) in commercial cases transfers under (currently) $6,225

VII. Ordinary Course of Business Defense
   - Interpretation of “ordinary business terms”
Irrelevance of routine nature of transfer to goals of preference law properly understood

VII. Time of Transfer in Connection with Security Interests
- Why leave it to preference law to control delayed filing situations
- Lack of justification for 200 percent increase in grace period

VIII. Low-Dollar Threshold in Commercial Cases
- In small cases *de minimis* may actually be *de maximus*
- A simultaneously over- and underinclusive approach for controlling abusive use of the preference power—even to the extent the problem exists at the level alleged
- Alternative approaches
  - Existing case management tools
  - ABI Chapter 11 Commission recommendations
    - Due diligence
    - Plead with particularity
    - Venue rules (to a point); increase floor in (c)(9) (not)

IX. Ultimate Question
- Is the purpose of the preference law to regulate culpable behavior or promote unique substantive goals in bankruptcy?
- The question concerning the purpose of the preference law as a microcosm of broader issue in bankruptcy of extent of deference to be accorded to private state law rights

X. Proposal
- Voidable preference as a strict liability offense
- Limit exceptions to situations where transfer does not result in a depletion of the estate during the preference period

XI. Summation
- BAPCPA as a step in the wrong direction in relation to preference liability—focus on deterrence rather than ratable distribution and rehabilitation
- Relationship to broader question of purposes and policy of bankruptcy law: purely procedural or advancing unique substantive goals
What Do We Know About the Individual Chapter 11 Debtor?

Anne Lawton

In this paper, I present findings from a sample of approximately 370 individual chapter 11 debtors who filed for relief in calendar years 2004 or 2007. The purpose of the study is largely descriptive, but I hope to provide data that will guide analysis of the impact, if any, of BAPCPA’s changes on individual filing patterns in chapter 11. In an earlier study of the same sample of individual chapter 11 debtors, I found that individual debtors do not fare well in chapter 11, if plan confirmation and successful plan performance are the measures of success. In this follow-up study, I provide more information about the financial characteristics of this group of chapter 11 debtors and examine what happened to their cases during the chapter 11 process.

Outline

1. **The Case Samples**
   a. Cases taken from two large samples of chapter 11 debtors drawn from all chapter 11 cases filed in the 94 U.S. judicial districts pre- and post-BAPCPA.

2. **Why file chapter 11?**
   a. Are individuals forced into chapter 11 by involuntary filings?
      i. Exceedingly rare
   b. Cases started in another chapter and converted to chapter 11
      i. Who files these motions to convert to chapter 11?
   c. Chapter 13 debt limits
      i. Did BAPCPA’s changes make chapter 11 less attractive for individuals?
         1. For approximately 25% of the total group of individual debtors (2004 & 2007), the chapter 13 debt limits posed no bar to filing
         2. But, big change from 2004 to 2007
            a. In 2004: about 1 in 3 (31%) of the debtors had liabilities below the chapter 13 debt limits
            b. In 2007: less than 1 in 5 (18%) had liabilities below the chapter 13 debt limits
3. **Debtor Characteristics**
   a. Petition identifiers?
      i. Small business debtors?
   ii. Debts as primarily business vs. primarily consumer?
      1. Percentages flipped between 2004 & 2007
         a. In 2004: more than half were consumer debtors
         b. In 2007: more than half were business debtors
   b. Measures of wealth
      i. Assets
         1. At least 90% own some form of real property
            a. Compare with home ownership rates in U.S.
         2. At least 90% have total assets of $5M or less
         3. Median personal property value lower in 2007 compared with 2004
      ii. Liabilities
         1. Almost 90% have total liabilities of $5M or less
   iii. Asset & Liability Ratios
      1. Assets to Liabilities: median figure for both years shows assets at approximately 80% of liabilities
      2. Secured debt comprises largest portion of total liabilities
         a. Example: In 2007, median figure is 77%. In other words, more than half the debtors had secured debt that was at least 77% of total scheduled liabilities.
      3. Unsecured priority debt is small portion of total liabilities
   iv. Income
      1. Median income is significantly higher than that for the average American family
      2. Expense-to-income ratio: median figure shows approximately $1 in expenses for each $1 of income.

4. **What happens during the chapter 11 case?**
   a. Formation of an official committee of unsecured creditors
      i. Rarely form in chapter 11
      ii. Very few form in individual cases – less than 5%
         1. Almost never in cases in which debtor identifies liabilities as primarily consumer
   b. Chapter 11 trustee and/or examiner appointment
      i. Rarely appointed
c. Case disposition
   i. Dismissal is the most common form of disposition although not big
difference between dismissal and conversion percentages in 2007
   ii. Plan proposal and confirmation
       1. 47% of the individual debtors proposed a chapter 11 plan
       2. Between 25% and 29% confirmed a plan
       3. Of those debtors proposing a plan, a statistically higher percentage
          confirmed and successfully performed plans in 2004 compared
          with 2007
          a. Is the difference a function of BAPCPA’s changes to the
             discharge rules?
          b. Or, is something else happening? The Great Recession’s
             impact on successful plan performance?
   4. Impact, if any, of BAPCPA’s changes on plan proposal and plan
      confirmation?
      a. Time from plan proposal to plan confirmation
         i. Section 1129(e)’s 45-day rule for small business
            debtors
      b. Time to first plan proposal
         i. Section 1121(e)’s 300-day plan-proposal deadline
            for small business debtors
   5. Does the absolute priority rule play a significant role in the plan-
      confirmation process?
   iii. Alternative measure of success
       1. Includes dismissals with some payment to creditors or resolution
          of reason for bankruptcy filing
          a. Does not significantly alter success rates
       2. What if we followed cases over time?
          a. Fairly high rate of bankruptcy re-filing among individual
             debtors
             i. Debtors who had filed for relief prior to filing
                their case
             ii. Debtors who re-filed for relief after their 2004 or
                2007 chapter 11 case
             iii. “Serial” filers: debtors who filed multiple times for
                 relief or who filed both before and after their 2004
                 or 2007 case
          b. Should we measure success over time, taking into account
             the possibility that individual debtors may need to file
             more than one bankruptcy case to successfully reorganize?
5. What, if anything, does the data tell us about reforming chapter 11 for individual debtors?