2000

Post-Petition Earnings and Individual Chapter 11 Debtors: Avoiding a Head Start

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Recommended Citation
Available at: http://ir.lawnet.fordham.edu/flr/vol68/iss5/11
A fresh start is all that they can ask for. The Bankruptcy Code\(^1\) ("Code") gives debtors the opportunity to clean their slates of past mistakes and begin a new financial life. Individual debtors may avail themselves of three primary types of proceedings under the Code. Chapter 7 forces the debtor to liquidate most of his assets and uses the proceeds from the liquidation to satisfy creditors. Any remaining debt is generally discharged. Under Chapter 13, the debtor has the exclusive right to propose and file a repayment plan. If the bankruptcy court confirms the debtor's plan and the debtor performs under its terms, the debtor is discharged of all debts not provided for by the plan. Chapter 11, similar to Chapter 13, allows the debtor to propose and file a plan of reorganization under which debts are paid. In Chapter 11, however, this right is not exclusive to the debtor because creditors can also file a plan of reorganization after a period of exclusivity has expired. Debtors can propose a plan that makes distributions from property of the estate, although the provisions of Chapter 11 do not require the use of estate property to fund the plan.\(^2\) The Chapter 11 debtor receives his discharge when the bankruptcy court confirms the plan, though he still must abide by the plan's terms.

Although individual debtors are eligible to file for bankruptcy protection under Chapter 11 of the Bankruptcy Code regardless of whether they are engaged in business,\(^3\) courts are not equipped to deal with individual debtors under this chapter because its provisions are aimed at business debtors.\(^4\) For example, Chapter 11 does not require

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\(^1\) Many thanks to Mom, Dad, and my brother, Tom, for all of their support. Special thanks to Professor Susan Block-Lieb for her invaluable expertise, input, and cheerleading that enabled me to write this monster. I would also like to thank the Hon. Adali S. Hardin, Jr., United States Bankruptcy Judge for the Southern District of New York, for planting the seed that became a Note.

\(^2\) See id. §§ 1101-1174.


\(^4\) See In re Weber, 209 B.R. 793, 797 (Bankr. D. Mass. 1997) ("Since the Supreme Court held in Toibb v. Radloff ... that an individual debtor not engaged in business is eligible for Chapter 11 relief, bankruptcy courts have struggled to determine the standards for proper administration of such a case." (citations omitted)).

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that the individual debtor contribute his post-petition earnings to fund his plan of reorganization, although some courts have so required. Additional complications arise when the debtor is a sole proprietor.

When adjudicating individual Chapter 11 cases, courts have generally focused their efforts on what constitutes distributable property of the estate under section 541.\(^5\) This focus, however, is misplaced. Instead, courts should concentrate their efforts on determining whether the debtor is able to confirm a plan of reorganization under section 1129\(^6\) because there is no provision in Chapter 11 that requires that the debtor use estate property to fund his plan, and thus the precise contours of the estate do not matter in an individual Chapter 11 case. Courts' efforts to determine what should be classified as property of the estate are not completely in vain, however, because identification and valuation of property of the estate is necessary to determine whether the plan of reorganization satisfies the "best interest of creditors test."\(^7\) Courts will also have to make determinations about property of the estate if the case is converted to a Chapter 7 liquidation.\(^8\) But the primary issue in an individual Chapter 11 case should be how the individual debtor will fund a plan, not what property constitutes the estate.

In determining what constitutes property of the estate, most courts have fiercely protected the individual debtor by refusing to include in the estate the post-petition earnings of the individual debtor.\(^9\) Other courts, faced with the issue of plan confirmation, have disregarded section 541 and the debtor's fresh start by holding that the individual debtor must use post-petition earnings to fund a plan in order to satisfy section 1129(a)(3), which requires that the plan be proposed in good faith, and section 1129(a)(11), which requires that the plan be feasible.\(^10\) Although the focus for the individual Chapter 11 debtor should be plan confirmation, confirmation should not be at the expense of the debtor's fresh start.\(^11\) To satisfy both purposes of the

\(^{5}\) See, e.g., FitzSimmons v. Walsh (In re FitzSimmons), 725 F.2d 1208, 1211 (9th Cir. 1984) (holding individual debtor's post-petition earnings not included as property of the estate under section 541(a)(6), but that the earnings of the sole proprietorship were included); see also infra Parts I.B, II (discussing property of the estate and the courts' struggle with this determination).

\(^{6}\) See 7 Collier on Bankruptcy ¶ 1129.01 (Lawrence P. King ed., 15th ed. 1999); see also infra Part IV (discussing confirmation in individual Chapter 11 cases).

\(^{7}\) See infra notes 62-65, 113 (describing the "best interest of creditors" test).

\(^{8}\) See infra notes 73-81 (detailing section 1112(b) regarding conversion or dismissal).

\(^{9}\) See infra Part II for an examination of cases that have held that the post-petition earnings of the individual debtor are excluded from the bankruptcy estate and the policy rationale behind this exclusion.

\(^{10}\) See infra Part III (discussing the individual debtor and Chapter 11 plan confirmation).

\(^{11}\) See infra notes 143-51 and accompanying text (discussing the debtor's fresh start).
Code—the debtor's fresh start and payment of the debtor's debts\textsuperscript{12}—Congress should amend the Code to provide courts with stricter guidelines as to how to treat the individual debtor in Chapter 11.\textsuperscript{13}

Currently, the individual debtor in Chapter 11 is not statutorily obligated to contribute post-petition\textsuperscript{14} earnings to fund a plan of reorganization,\textsuperscript{15} in contrast to the requirements of Chapter 13.\textsuperscript{16} The individual debtor in Chapter 11 thus may propose a plan under which he retains non-exempt assets, funds the plan with property of the estate, and retains his post-petition earnings, paying creditors pennies on the dollar.\textsuperscript{17} A plan such as this may satisfy the "best interest of creditors test,"\textsuperscript{18} but does not approximate the amount the debtor would be required to contribute under a disposable income test.\textsuperscript{19} Although some courts have denied confirmation to plans under which the debtor has the ability to pay debts from post-petition earnings, but does not propose to use these earnings to pay creditors,\textsuperscript{20} there is scant statutory support for their position.\textsuperscript{21}

In order to address the uncertain treatment of the individual debtor in Chapter 11, the Senate has recently passed a series of amendments to the Bankruptcy Reform Act of 1999.\textsuperscript{22} These amendments would require the individual debtor in Chapter 11 to contribute his post-


\textsuperscript{13} The Senate has recently proposed such amendments to the Bankruptcy Reform Act of 1999. See infra Part IV for the text of these amendments and a discussion of their possible effect on individual Chapter 11 debtors.

\textsuperscript{14} For the purposes of this Note, there is no difference between the terms "post-petition" and "post-commencement" when discussing the earnings of an individual debtor.

\textsuperscript{15} Courts, however, have on occasion denied individual debtors confirmation in Chapter 11 because of the debtor's refusal to include post-petition earnings as a source of income to fund the plan. \textit{See}, e.g., Roland v. Unum Life Ins. Co., 223 B.R. 499, 506 (Bankr. E.D. Va. 1998); see also infra Part III (discussing these courts' decisions in greater detail).


\textsuperscript{17} A creditor's active role in plan confirmation in Chapter 11 cases makes this scenario unlikely. \textit{See id.} § 1102 (providing for the appointment of creditors' committees in Chapter 11); \textit{id.} § 1103 (describing the powers and duties of the creditors' committees) \textit{See generally} David B. Tate & Dwight D. Meier, \textit{Creditor's Strategies In Individual Bankruptcy Cases Under Chapter 11}, 95 Com. L.J. 255, 258-89 (1990) (describing how creditors should respond to the individual Chapter 11 debtor).

\textsuperscript{18} See infra notes 62-65 and accompanying text (discussing the best interest of creditors test).

\textsuperscript{19} See infra notes 104-06 (discussing the disposable income test).

\textsuperscript{20} See \textit{infra} notes 207-43 and accompanying text (examining cases dealing with the individual debtor and Chapter 11 confirmation standards).

\textsuperscript{21} See infra Part IV (discussing the lack of statutory support behind these courts' interpretations). In addition, the results these courts reach contradict the results of courts interpreting section 541(a)(6). See infra Part IV.

petition earnings to fund his plan of reorganization. If enacted, these amendments would add a disposable income test to the confirmation requirements of Chapter 11 for an individual debtor. This Note argues that these amendments should ultimately be enacted into law, and analyzes the reasons why.

Part I explores Chapters 7, 11, and 13 as they relate to the individual debtor, and explains how property of the estate under section 541 is defined differently under each chapter. Part II describes the debtor's "fresh start" and analyzes cases interpreting section 541(a)(6) as applied to the individual Chapter 11 debtor, regardless of whether that individual is a sole proprietor. Part III examines section 1129's standards for confirmation of a Chapter 11 plan of reorganization proposed by an individual debtor, and finds that this debtor may already be subject to a disposable income test similar to that in Chapter 13. Part IV analyzes courts' interpretations of section 1129 in light of the policies behind the Code and urges that Congress pass pending amendments that will statutorily require individual debtors in Chapter 11 to devote their post-petition disposable income toward funding their plans of reorganization.

I. OVERVIEW OF THE BANKRUPTCY CODE

The law governing the relationship between debtors and creditors existed hundreds of years before Congress enacted the Bankruptcy Code. Bankruptcy laws evolved as a mechanism to aid creditors in the collection of debts. Historically, debtors, formerly known as bankrupts, were treated as criminals and could be sold to satisfy their obligations. In the United States, Congress has enacted several bankruptcy statutes over the past 150 years pursuant to its constitutional power.

Earlier statutes provided minimal relief to debtors and creditors because only certain individuals or entities could...

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23. The disposable income test is currently found in Chapters 12 and 13, but not in Chapter 11. Compare 11 U.S.C. §§ 1101-1174 (1994) (no disposable income test) with id. § 1222(a) (plan shall include future earnings of debtor) and id. § 1325(b) (disposable income test). This test requires that the debtor fund his plan with his post-petition income above that which is needed for reasonable and necessary living expenses. See id. § 1325(b).


26. See id. at 1374-75.

27. See U.S. Const. art. I, § 8, cl. 4 (authorizing Congress to legislate "on the subject of bankruptcies"); see also Countryman, supra note 24, at 226-32 (discussing the history of the United States bankruptcy acts).
take advantage of their provisions. For example, the Bankruptcy Act of 1800 was available only to creditors who wished to involuntarily place their merchant debtors in bankruptcy. In enacting subsequent Acts, Congress expanded the applicability of the bankruptcy laws to include different types of debtors. Although creditors historically have been in a position of power, able to extract money from their debtors at almost any cost, over time, debtors have received greater bankruptcy protection with each successive enactment of bankruptcy legislation, culminating in the “debtor-friendly” Bankruptcy Act of 1978.

Two overarching purposes of the Bankruptcy Code are the protection of creditors’ interests and the protection of the debtor’s “fresh start.” Although the Code itself does not make mention of the debtor’s “fresh start,” it does provide for “discharge,” an exoneration for the debtor of all debts unpaid after the bankruptcy. The policy of protecting the debtor’s fresh start is evident in many sections of the Code and reflects a desire to allow the “honest but unfortunate debtor” a chance to start anew. Although the debtor’s fresh start remains among the most important bankruptcy policy considerations, Congress has amended the Code several times to maintain the balance between creditors’ and debtors’ rights. Thus, specific provisions within the chapters have been altered to prevent debtors from attempting to gain a benefit in one chapter where they could not gain the benefit in another. This part explores the various

28. See Countryman, supra note 24, at 228.
29. See id.
31. See Countryman, supra note 24, at 226-28; Felsenfeld, supra note 25, at 1374-78.
32. See Felsenfeld, supra note 25, at 1378-84. The Bankruptcy Act of 1898 was the first to codify the debtor’s fresh start as it exists today, by providing for discharge without creditors’ consent. See 30 Stat. 544, 550 (1898); see also Countryman, supra note 24, at 228-32 (detailing the history of American bankruptcy law).
33. See supra note 12 and accompanying text (discussing the purposes of the Code).
34. See 11 U.S.C. §§ 727(a), 1141(d), 1228, 1328 (1994).
35. For example, section 522 allows a debtor certain exemptions of property from the estate; section 524 provides for the debtor’s discharge; section 541(a)(6) excepts from the estate the post-petition service earnings of the individual debtor; and section 1328(a) grants the debtor in that chapter a broad discharge upon completion of plan payments, while section 1328(b) provides a hardship discharge where the debtor is unable to consummate the plan. See id. §§ 522, 524, 541(a)(6), 1328(a)-(b).
37. See Felsenfeld, supra note 25, at 1380 (“The bankruptcy laws thus represent a pendulum, constantly swinging between the two extremes, never reaching either and never at rest.”).
38. See, e.g., 11 U.S.C. § 1123(b)(5) (providing that individual debtors in Chapter 11 are unable to modify liens on their principal residences); see also First Federal Bank of Cal. v. Weinstein (In re Weinstein), 227 B.R. 284, 290-91 & n.4 (B.A.P. 9th
chapters of relief available to the individual debtor in bankruptcy under the current Code. It then describes how courts calculate property of the estate under section 541, a provision that is applicable to all chapters under the Code.

A. A Comparison of Chapters

1. Chapter 7

Individual debtors may file for relief under the Bankruptcy Code in Chapters 7, 11, or 13. Chapter 7 provides both the individual and corporate debtor with relief from debts through liquidation. Petitions under Chapter 7 may be filed voluntarily by the debtor or involuntarily by the debtor’s creditors. A court-appointed trustee marshals all of the debtor’s assets as of the petition date and liquidates the unencumbered, nonexempt assets to satisfy creditors’ claims. The debtor’s obligations that are not satisfied by this distribution are discharged. Exceptions to discharge exist for certain tax obligations, familial responsibilities, and other debts. Barring

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39. See 11 U.S.C. §§ 701-766. Chapter 7 may be initiated voluntarily or involuntarily. See id. §§ 301, 303(a).
40. See id. §§ 301, 303.
41. In a Chapter 7 case, a trustee is always appointed. See id. § 701 (interim trustee); id. § 702 (election of trustee).
42. Section 541 defines the property of the estate and includes in the estate all equitable and legal interests of the debtor as of the petition date. In Chapter 7, courts protect the individual debtor’s fresh start by limiting the property of the estate to the property that exists as of the filing date. See, e.g., In re Norris, 203 B.R. 463, 465 n.2 (Bankr. D. Nev. 1996) (holding that under Chapter 7, post-petition earnings are not property of the estate under section 541(a)(6)); In re DeSoto, 181 B.R. 704, 713 (Bankr. D. Conn. 1995) (same); In re Michaels, 157 B.R. 190, 196 n.6 (Bankr. D. Mass. 1993) (same).
43. See 11 U.S.C. §§ 701-766; see also infra Part I.B for a discussion of what constitutes property of the estate.
44. See 11 U.S.C. § 524. Section 524 governs the discharge of debts in bankruptcy and applies to Chapters 7, 11, and 13. See id. § 103(a). Section 524 governs the effect of a discharge of pre-petition, unsecured debts. Debts secured by liens are not discharged under the Code because the security interest survives discharge. See 4 Collier on Bankruptcy ¶ 524.02[2][d] (1999). Discharge also protects the debtor by enjoining future actions by creditors to enforce a debt that has been discharged under this section. In a Chapter 7 case, the general discharge provision of the Code, section 524, works in conjunction with section 727, which governs denial of discharge in Chapter 7. See 11 U.S.C. § 727.
45. See 11 U.S.C. § 523 (listing all of the non-dischargeable debts for the individual in bankruptcy, including, for example, judgments for death or injury caused by the debtor’s driving while intoxicated).
these restrictions, the individual debtor in Chapter 7 is free to enjoy his fresh start.

2. Chapter 11

Chapter 11 contemplates reorganization of a business debtor while allowing the debtor to remain in business. The primary goal of Chapter 11 is confirmation of a plan of reorganization. In enacting Chapter 11, Congress did not envision its widespread use by consumer debtors because of the complexity and expense of proposing a plan of reorganization. However, Congress did not rule out the possibility that Chapter 11 may provide the best option for certain individual debtors. Although Chapter 11 is a vehicle predominately used by corporations, the Supreme Court ruled in Toibb v. Radloff that individuals not engaged in business are eligible to file for bankruptcy under Chapter 11.

Chapter 11 debtors are required to formulate a plan of reorganization and submit a disclosure statement that provides the

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46. See id. §§ 1101-1174. A liquidating Chapter 11 may also be contemplated. See id. § 1123(b)(4).
47. See In re Powell, 187 B.R. 642, 647 (Bankr. D. Minn. 1995); see also 11 U.S.C. § 1141 (detailing the effects of confirmation in Chapter 11); 7 Collier on Bankruptcy ¶ 1129.01 (1999) (same).
51. See id. at 166. The Court based its reasoning primarily on the plain language of the Code. Section 109(d) states that only a person who qualifies as a debtor under Chapter 7 may be a debtor under Chapter 11, with the exception of stockbrokers, commodity brokers, and railroads. See 11 U.S.C. § 109(d). Section 109(b) provides for who may file under Chapter 7. See id. § 109(b). “Person” is a defined term under the Code. Section 101(41) defines person to include individuals, partnerships, and corporations. See id. § 101(41); Toibb, 501 U.S. at 160-61. Because individuals are defined as persons and persons are eligible to file in Chapter 11, the Court concluded that individuals could file under Chapter 11. The Supreme Court had granted certiorari to resolve a split among the circuits, some holding individuals eligible to file in Chapter 11 and others holding them ineligible. Compare Wamsganz v. Boatmen’s Bank of De Soto, 804 F.2d 503, 505-06 (8th Cir. 1986) (holding that an individual, not engaged in business, was not eligible to file Chapter 11) with In re Moog, 774 F.2d 1073, 1075 (11th Cir. 1985) (holding that individuals were eligible to file Chapter 11 whether or not engaged in business).
52. See 11 U.S.C. § 1121 (stating who may file a plan and when it may be filed); see also id. § 1122 (stating standards of classification of claims); id. § 1123 (describing what provisions the plan shall and may contain); id. §§ 1123(a)(2)-(4) (detailing that a plan shall specify impaired and unimpaired classes of claims and provide for the same treatment of each claim in a class unless the holder consents to less agreeable
interested parties with sufficient information to make an informed judgement about whether to vote to accept the plan.\textsuperscript{53} The plan of reorganization in Chapter 11 can provide any terms that the debtor wishes, including partial payment or extended payment of an existing obligation. To consensually confirm a plan under section 1129(a), the debtor must satisfy all of the requirements of that section.\textsuperscript{54} If a creditor is not satisfied with the plan, the creditor may vote to reject it.\textsuperscript{55} However, the provisions of Chapter 11 do not require that the plan be funded from any particular source. Upon confirmation of a plan in Chapter 11, the debtor receives the desired discharge and the plan provisions supercede the prior obligations of the debtor.\textsuperscript{56} If the debtor and his creditors are unable to reach a compromise on a plan of reorganization, the debtor may be able to “cram down” his plan upon certain of its creditors under section 1129(b).\textsuperscript{57}

Several provisions of Chapter 11 present particularly difficult obstacles for the debtor seeking plan confirmation. To confirm the

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\item treatment); \textit{id.} § 1124 (defining what constitutes an impairment to a claim or interest); \textit{id.} § 1129 (detailing confirmation standards).
\item See \textit{id.} § 1125.
\item See \textit{id.} § 1129(a). This section provides that the debtor must meet thirteen requirements in order to consensually confirm a plan, most of which are irrelevant to the individual debtor in Chapter 11. The provisions of section 1129(a) particularly relevant are:
\begin{enumerate}
\item The plan has been proposed in good faith and not by any means forbidden by law.
\item With respect to each impaired class of claims or interests-
\begin{enumerate}
\item each holder of a claim or interest of such class-
\begin{enumerate}
\item has accepted the plan; or
\item will receive or retain under the plan on account of such claim or interest property of a value, as of the effective date of the plan, that is not less than the amount that such holder would so receive or retain if the debtor were liquidated under chapter 7 of this title on such date;
\end{enumerate}
\end{enumerate}
\item Confirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan, unless such liquidation or reorganization is proposed in the plan.
\end{enumerate}
\item See \textit{id.} § 1125.
\item See \textit{id.} § 1141. Governed by section 523, the discharge for the individual in Chapter 11 is slightly broader than that granted for the individual under Chapter 7, because section 1141 also discharges “gap” claims arising in the period post-petition but pre-confirmation.
\item See \textit{id.} § 1129; see also \textit{infra} notes 83-92 and accompanying text (discussing non-consensual confirmation, also known as “cram down”).
\end{itemize}
plan, the debtor must satisfy the best interest of creditors test;\textsuperscript{58} must be able to carry out the terms of his plan;\textsuperscript{59} and must propose his plan in good faith and in accordance with the law.\textsuperscript{60} The debtor must also satisfy the section that deals with conversion or dismissal of a Chapter 11 case for cause.\textsuperscript{61} These requirements will be discussed in turn.

The best interest of creditors test, contained in section 1129(a)(7), protects creditors by ensuring that they will not receive less in a Chapter 11 reorganization than they would receive in a Chapter 7 liquidation.\textsuperscript{62} For purposes of applying the test, the estate is valued as of the date the petition is filed. The value of the estate is then divided among the creditors based on the priority of the creditors' claims. This valuation is the minimum amount that creditors will receive. This section applies only to members of impaired creditor classes\textsuperscript{63} because unimpaired classes will receive full value on account of their claims.\textsuperscript{64} If the court finds that impaired creditors would receive less in Chapter 11, as provided for by the plan of reorganization, than they would in a Chapter 7 liquidation, the plan is held unconfirmable.\textsuperscript{65}

The debtor must also demonstrate that the plan has a reasonable likelihood of success. Section 1129(a)(11) concerns the feasibility of the debtor's plan and requires a showing that: "[c]onfirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan, unless such liquidation or reorganization is proposed in the plan."\textsuperscript{66} The debtor's plan of reorganization that is proffered to the court for approval need not guarantee success; instead, the debtor need only submit a plan with which he is reasonably able to comply.\textsuperscript{67} Courts have determined feasibility according to "[w]hether the things which are to be done after confirmation can be done as a practical matter under the facts. . . ."\textsuperscript{68} Factors that courts consider when determining feasibility include the earning power of the debtor, the sufficiency of the debtor's capital

\textsuperscript{58} See 11 U.S.C. § 1129(a)(7).
\textsuperscript{59} See id. § 1129(a)(11).
\textsuperscript{60} See id. § 1129(a)(3).
\textsuperscript{61} See id. § 1112(b).
\textsuperscript{62} See id. § 1129(a)(7). A debtor in Chapter 13 must also satisfy the best interest of creditors test. See id. § 1325(a)(4); see also infra notes 98-107 and accompanying text (discussing Chapter 13).
\textsuperscript{63} A class of creditors is impaired if the debtor's plan proposes to alter the creditors' rights on account of his claim. See 7 Collier on Bankruptcy § 1129.03[7][a]-[b] (15th ed. 1999).
\textsuperscript{64} See id.
\textsuperscript{66} Id. § 1129(a)(11).
\textsuperscript{68} In re Ashton, 107 B.R. 670, 674 (Bankr. D. N.D. 1989) (citing In re Clarkson, 767 F.2d 417, 420 (8th Cir. 1985)); see also In re Kemp 134 B.R. 413, 415 (Bankr. E.D. Cal. 1991) ("The test is whether the things which are to be done after confirmation can be done as a practical matter under the facts.").
structure, credit availability, managerial efficiency of the debtor, and market conditions.69

Section 1129(a)(3) requires that “[t]he plan has been proposed in good faith and not by any means forbidden by law.”70 The good faith requirement of section 1129(a)(3) has at least two factors.71 First, the plan must be "proposed with honesty and good intentions,"72 and second, the debtor must have "a basis for expecting that a reorganization can be effected."72

Finally, section 1112(b) describes when a court may dismiss a case or convert it to one under Chapter 7.73 Both creditors and debtors may request a conversion or dismissal.74 Such actions are within the discretion of the court and must be in the best interest of the creditors and the estate. This section may be invoked by a party in interest or sua sponte by the court at any time during the bankruptcy proceeding.75 If a debtor is unable to confirm a plan of reorganization, the court may convert or dismiss the case under section 1112(b).76 Courts have also interpreted this provision to require dismissal or conversion where the debtor lacks the ability to formulate a plan or is financially incapable of effectuating it.77 In addition, courts have

69. See In re Kemp, 134 B.R. at 416; In re Ashton, 107 B.R. at 674 ("[F]easibility must be rooted in predictions based upon objective fact."); In re Orlando Investors, 103 B.R. at 600.
71. See In re Orlando Investors, 103 B.R. at 598.
72. Id. at 598 (quoting In re Kobel, 751 F.2d 137, 139 (2d Cir. 1984) (citing Manati Sugar Co. v. Mock, 75 F.2d 284, 285 (2d Cir. 1935))). The court held that because there was no indication that the debtor did not believe that his plan would not succeed, the good faith requirement was met. See id. at 598-99. Although the debtor in Orlando Investors was a partnership, the good faith standard of section 1129(a)(3) is equally applicable to the individual Chapter 11 debtor.
73. See 11 U.S.C. § 1112(a)-(b).
74. See id.
    on request of a party in interest or the United States trustee or bankruptcy administrator ... the court may convert a case under this chapter to a case under chapter 7 of this title or may dismiss a case under this chapter, whichever is in the best interest of creditors and the estate, for cause, including- (1) continuing loss to or diminution of the estate and absence of a reasonable likelihood of rehabilitation; (2) inability to effectuate a plan ....
76. See 11 U.S.C. § 1112(b); see also infra notes 77-81 and accompanying text (discussing section 1112(b) issues in greater detail).
77. See, e.g., In re Little Creek Dev. Co., 779 F.2d 1068, 1072 (5th Cir. 1986) (discussing conversion or dismissal under section 1112(b) for lack of good faith as including "the bankruptcy court's on-the-spot evaluation of the debtor's financial condition, motives, and the local financial realities"); In re Saleha, No. 93-00638, 1995 WL 128495, at *7 (Bankr. D. Idaho Mar. 10, 1995) (dismissing debtor's case under section 1112(b) because five unconfirmed plans evidenced an inability to effectuate a plan, which the court inferred to mean the debtor's "unwillingness to make the financial sacrifices necessary to complete a Chapter 11 plan" despite having the financial wherewithal to fund the plan).
construed section 1112(b) to permit dismissal or conversion of Chapter 11 cases that debtors have filed in bad faith. Although the current Code does not explicitly require the debtor to file his petition in good faith, it allows a court to dismiss a case “for cause.” Courts have considered a bad faith filing to constitute “cause” justifying dismissal or conversion of a Chapter 11 case. A petition filed solely to harass creditors is considered to have been filed in bad faith.

Two additional concepts are important in Chapter 11 cases—cram down and the new value exception. When a debtor in Chapter 11 is unable to confirm a plan of reorganization with creditor consent, the debtor will try to non-consensually confirm or “cram down” a plan over dissenting creditors. To effect a non-consensual confirmation, the debtor must meet the provisions in section 1129(a), except for subsection (8). In addition, the debtor must show that the plan does not discriminate unfairly against dissenting classes and that such classes are treated fairly and equitably under the plan. Fair and equitable treatment under section 1129(b) requires compliance with the absolute priority rule. The absolute priority rule requires either that the debtor pay the unsecured creditors’ claims in full, or that subordinated creditors and shareholders receive or retain no property

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78. See, e.g., In re McCormick Rd. Assocs., 127 B.R. 410, 412-17 (N.D. Ill. 1991) (discussing factors of bad faith filings and holding that the debtor filed a Chapter 11 petition in bad faith); In re Mogul, 17 B.R. 680, 681-82 (Bankr. M.D. Fla. 1982) (conceding that the Code does not require the debtor to file his petition in good faith, yet converting the case to Chapter 7 based on the “totality of the circumstances”).

79. See, e.g., In re Mogul, 17 B.R. at 682 (“[G]ood faith must be viewed as an implied prerequisite for a debtor’s ability of obtaining relief under this Chapter.”); see also Janet A. Flaccus, Have Eight Circuits Shorted? Good Faith and Chapter 11 Bankruptcy Petitions, 67 Am. Bankr. L.J. 401, 401-17 (1993) (discussing the legislative history behind section 1112(b) and the fact that the Code does not include a good faith filing requirement).

80. See, e.g., In re Little Creek, 779 F.2d at 1072; In re Martin, 51 B.R. 490, 493-95 (Bankr. M.D. Fla. 1985). These cases were decided before the Supreme Court’s decision in Toibb v. Radloff, which established the legal validity of Chapter 11 filings by individual debtors who are not engaged in business. See Toibb v. Radloff, 501 U.S. 157, 166 (1991). Despite the legal uncertainty, the courts ruled that such individuals’ filings under Chapter 11 were insufficient, by themselves, to constitute cause for dismissal. See In re Little Creek, 779 F.2d at 1072; In re Martin, 51 B.R. at 493-95.

81. See, e.g., In re Mogul, 17 B.R. at 682 (holding that because the debtor had no possibility of effectuating a plan, the “entire proceeding was instituted solely for the purpose of delay and harassment” and therefore should be dismissed).

82. See supra notes 54-72 (discussing the consensual confirmation standards under section 1129(a)).

83. Subsection (8) provides: “[w]ith respect to each class of claims or interests—(A) such class has accepted the plan; or (B) such class is not impaired under the plan.” 11 U.S.C. § 1129(a)(8); see also supra note 54 (describing section 1129(a)).


86. See id. § 1129(b)(2)(B)(i).
under the plan "on account of such junior claim or interest any property."{87}

In *Case v. Los Angeles Lumber Prods. Co.*,{88} the Supreme Court alluded in dicta to an exception to the absolute priority rule, known today as the "new value exception."{89} The new value exception allows the business debtor's subordinated claim-holders (shareholders) to retain an interest in the reorganized company, even though unsecured creditors with greater priority have not been paid in full, if the subordinated claim-holders make a new and substantial contribution of "money or in money's worth" that is reasonably equivalent to the new interests obtained in the reorganized debtor.{90} In interpreting this judicially created exception, the Supreme Court in *Norwest Bank Worthington v. Ahlers*{91} held that the new value exception could not be invoked where the proposed money's worth was "sweat equity"—future labor on the debtor's farm.{92} The Court found that a "promise to contribute future labor, management, or expertise [is] [in]sufficient to qualify for the... exception to the absolute priority rule."{93} According to the Court, subordinate claim-holders may invoke the new value exception only where the proposed new money, or money's worth, is tangible and the contribution is the reasonable equivalent of the interest retained.{94}

Without deciding whether the new value exception survived the enactment of the 1978 Code, the Supreme Court in *Bank of America National Trust & Savings Ass'n v. 203 North La Salle Street Partnership*{95} recently held that an exclusive opportunity to propose a plan of reorganization in which a new value contribution by old equity

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{87} *Id.* § 1129(b)(2)(B)(ii); see also *203 N. LaSalle St. Partnership*, 119 S. Ct. at 1416 (applying the standards set out by section 1129(b)(2)(B)(ii)).

{88} 308 U.S. 106 (1939).

{89} *See id.* at 121-22. The passage, oft-quoted, reads:

It is, of course, clear that there are circumstances under which stockholders may participate in a plan of reorganization of an insolvent debtor.... [W]e believe that to accord 'the creditor of his full right of priority against the corporate assets' where the debtor is insolvent, the stockholder's participation must be based on a contribution in money or in money's worth, reasonably equivalent in view of all the circumstances to the participation of the stockholder.

*Id.*; see also *203 N. LaSalle St. Partnership*, 119 S. Ct. at 1417 (discussing the absolute priority rule and new value exception without deciding if the new value exception survived the 1978 Bankruptcy Act's enactment).


{92} *See id.* at 204-05.

{93} *Id.* at 204.

{94} *See id.*

{95} 119 S. Ct. 1411 (1999).
is exchanged for an equity interest in the reorganized debtor was an interest in property retained by shareholders in contravention of section 1129(b)(2)(B). As such, the debtors could not cram down the plan on their creditors because outside parties were not given the opportunity to bid.

3. Chapter 13

In contrast to Chapters 7 and 11, only individual debtors may seek Chapter 13 relief. To be eligible for Chapter 13, the debtor must have a regular source of income and debt no greater than specified amounts. Chapter 13 calls for a readjustment of the debtor's obligations and requires that the debtor file a plan of reorganization with the court within 15 days of filing for bankruptcy. Chapter 13 discharges an individual's debts, not upon confirmation, but only after the completion of payments under the plan.

Furthermore, Chapter 13 compels the debtor to make his future income available for distribution in execution of the plan. Although creditors do not vote on a Chapter 13 plan, they may object to plan confirmation on the grounds, inter alia, that it is not proposed in good faith, not feasible, or does not satisfy the best interest of creditors test. If an unsecured creditor objects to plan confirmation, the

96. Section 1129(b)(2)(B) is the absolute priority rule.
97. See 203 N. LaSalle St. Partnership, 119 S. Ct. at 1423.
99. See 11 U.S.C. § 109(e). Section 109(e) describes who may be a debtor under Chapter 13 and provides for maximum debt ceilings of $269,250 for noncontingent, liquidated, unsecured debt and $807,750 for noncontingent, liquidated, secured debt. These limits also represent the aggregate limits for the debtor and his spouse. Recently, the Code was amended to reflect inflation; these debt limits are generally subject to adjustment every three years according to changes in the Consumer Price Index. See id. § 104 (supp. IV 1998). “Regular income” is income that the debtor receives with regularity and is unrelated to the type or nature of work that the debtor performs to earn her income. See In re Antoine, 208 B.R. 17, 19-21 (Bankr. E.D.N.Y. 1997).
100. See 11 U.S.C. § 1321 (only the debtor may file a plan); see also id. § 1325(a)(3) (plan must be proposed in good faith).
103. See id. § 1322(a)(1) (“The plan shall—(1) provide for the submission of all or such portion of future earnings or other future income of the debtor...”); see also id. § 1306(a) (“Property of the estate includes, in addition to the property specified in section 541 of this title—(1) all property... that the debtor acquires after the commencement of the case... and (2) earnings from services performed by the debtor after the commencement of the case...”); supra Part I.B (discussing property of the estate.) Congress permits Chapter 13 to be initiated only voluntarily, so as to avoid any violation of the Thirteenth Amendment. See U.S. Const. amend. XIII, § 1; 11 U.S.C. § 303(a) (“An involuntary case may be commenced only under chapter 7 or 11 of this title.”) (emphasis supplied).
104. See 11 U.S.C. § 1325(b)(1); supra notes 62-64; see also 8 Collier on Bankruptcy
debtor must either pay the claim in full or make his future disposable income available to fund the dissenting creditor's claim for at least three years. At the time of confirmation, the bankruptcy court must determine whether the debtor's proposed expenditures are necessary for his maintenance and support.

Both Chapters 11 and 13 allow the debtor to financially restructure itself. Both chapters require the debtor to file a plan of reorganization with the court, and both have similar plan requirements. For example, plans proposed under either chapter must treat all claim-holders in a particular class equally, and in both chapters, the plan must be proposed in good faith. Both chapters also apply the “best interest of creditors” test and require that the plan's implementation be reasonably feasible.

Chapter 13 differs from Chapter 11 in that the former may only be initiated voluntarily by the debtor, while the latter may be initiated either voluntarily or involuntarily. Whereas under Chapter 11, the

¶ 1325.01-.09 (1999) (discussing the other confirmation standards of Chapter 13).
106. See id. § 1325(b)(2)(A).
109. Compare 11 U.S.C. § 1121 (providing who may file a plan under Chapter 11), with id. § 1321 (providing who may file a plan under Chapter 13).
110. Compare id. § 1123 (stating the provisions that the plan shall and may contain), with id. § 1322 (same provision under Chapter 13).
111. Compare id. § 1123(a)(4) (providing that each claim in a class receive the same treatment), with id. § 1322(a)(3) (same provision under Chapter 13).
112. See In re Madison Hotel Assocs., 749 F.2d 410, 425 (7th Cir. 1984) (discussing Chapter 11 and 13 and the requirement in both chapters that the debtor propose the plan of reorganization in good faith).
113. 11 U.S.C. §§ 1129(a)(7)(A)(ii), 1325(a)(4). The “best interest of creditors” test is a minimum payment requirement that the creditors not receive less in Chapter 11 or 13 than they would in a Chapter 7 liquidation. See id.; see also supra note 58 and accompanying text (discussing the best interest of creditors test).
114. Compare 11 U.S.C. § 1129(a)(11) (requiring that the debtor be able to carry out the terms of his plan), with id. § 1325(a)(6) (same). The test for feasibility is whether the debtor is able to effectuate his plan as proposed. See In re Keach, 225 B.R. 264, 269-70 (Bankr. D.R.I. 1998) (finding a Chapter 13 plan unfeasible because the plan was dependent on a 37% increase in debtor’s business); In re Turpen, 218 B.R. 908, 915-16 (Bankr. N.D. Iowa 1998) (holding a Chapter 13 plan unconfirmable because the debtor could not establish his capacity to obtain credit as proposed in his plan); In re Ashton, 107 B.R. 670, 674-75 (Bankr. D.N.D. 1989).
115. See 11 U.S.C. § 303 (providing that an involuntary case may only be
creditors vote to accept or reject the plan, Chapter 13 provides for no such vote on the plan.\footnote{116} In addition, if creditors object to plan confirmation in a Chapter 13 proceeding, the debtor must provide that the objecting creditor’s claims will be paid in full, or the debtor must contribute his disposable income for three years to repay the objecting creditor’s claims.\footnote{117} Chapter 11 does not contain a disposable income test provision,\footnote{118} under which the individual debtor would be required to contribute his disposable income to fund his plan.

An individual debtor may wish to file under Chapter 11 instead of Chapter 13 for a variety of reasons. Unlike in a Chapter 11 case, a debtor is ineligible to file under Chapter 13 if he has accumulated debts above the limits imposed by Chapter 13 or if he does not have a regular source of income.\footnote{119} A debtor may also wish to file under Chapter 11 to avoid the “disposable income test,” thus shielding his post-petition income.\footnote{120} Although Chapter 11 should be available to individual debtors, it should not exist as a safe haven from application of Chapter 13’s disposable income test.

B. \textit{Section 541—Property of the Estate}

The purpose of adjudicating bankruptcy cases is to pay creditors’ claims from the debtor’s pool of assets. In order to administer those assets, an estate is created when a bankruptcy petition is filed.\footnote{121} The bankruptcy estate is thus the compilation of the debtor’s assets as of the filing date. Section 541, which applies to all chapters of the Code,\footnote{122} provides a broad inclusive list of property that becomes part of the debtor’s estate,\footnote{123} wherever such property is located and by

\footnote{116} Compare 11 U.S.C. § 1126(a) (stating that a creditor may vote to accept or reject the plan in Chapter 11), with id. § 1325(b)(1) (providing that the trustee or holder of an allowed unsecured claim may object to confirmation).

\footnote{117} See id. § 1325(b)(1)(A)-(B); see also supra notes 103-07 and accompanying text (describing the disposable income test).


\footnote{119} See id. § 109(e) (describing who may be a debtor under Chapter 13); see also supra Part I.A.3.

\footnote{120} See Tatge & Meier, supra note 17, at 256; see also supra notes 103-07 and accompanying text (discussing the disposable income test). Compare 11 U.S.C. § 1325(b)(1)(B) (including the post-petition earnings of the Chapter 13 debtor), with id. § 1141 (failing to provide for the inclusion of debtor’s post-petition earnings).

\footnote{121} See 11 U.S.C. § 541(a). Section 541 applies generally to Chapters 7, 11, and 13 of the Code. It also applies to Chapter 12 (family farmer with regular income reorganization). See id. § 103(a). Chapter 12 applies only to a particular type of debtor, the family farmer, and is beyond the scope of this Note.

\footnote{122} See id. § 103(a).

\footnote{123} All interests in property that the debtor possesses as of the petition date become property of the estate, including any interests jointly possessed with the debtor’s spouse, any interest in property that the trustee recovers for the estate, any
whomever it is held.\textsuperscript{124} Property of the estate includes all legal and equitable interests of the debtor in property as of the commencement of the case.\textsuperscript{125} Also included are any interests jointly possessed by the debtor and the debtor's spouse,\textsuperscript{126} and certain interests the debtor acquires within 180 days after the filing that would have been property of the estate had the interest existed at the time of filing.\textsuperscript{127} Moreover, property of the estate includes any interest that the estate, as distinguished from the debtor, acquires post-commencement.\textsuperscript{128} Section 541(a)(6) provides that property of the estate includes "[p]roceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case."\textsuperscript{129} This italicized portion of the statute is known as the "earnings exception," and excepts from the estate the future earnings of the individual debtor.\textsuperscript{130}

\textsuperscript{124} See id. § 541(a). The trustee or debtor-in-possession has the power to avoid certain transfers and reclaim property of the estate. See id. § 541(a)(3) (including in the estate "[a]ny interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 of this title").

\textsuperscript{125} See id. § 541(a)(1). The individual debtor is permitted to claim exemptions from property of the estate under section 522. See id. § 522. Depending on where the debtor files, the debtor may choose between the federal exemptions listed in the Code and state exemptions. Certain states have opted-out of the federal exemption scheme, thereby forcing the debtor to take the state exemptions together with certain other federal exemptions. See Owen v. Owen, 500 U.S. 305, 308-14 (1991) (holding that state bankruptcy exemptions should be treated the same as federal exemptions and discussing Florida's opt-out exemptions). Federal exemptions include, \textit{inter alia}, $16,150 for residential property and $425 in household goods and clothing. See 11 U.S.C. §§ 104, 522 (1994 & supp. IV 1998). Exempt property is excluded from the bankruptcy estate and is therefore unavailable to satisfy creditors' claims.

\textsuperscript{126} See id. § 541(a)(2).

\textsuperscript{127} See id. § 541(a)(5). This subsection contemplates interests such as inheritances. See id. § 541(a)(5)(A).

\textsuperscript{128} Section 541(a)(6) includes "[p]roceeds, product, offspring, rents, or profits of or from property of the estate," and section 541(a)(7) includes "[a]ny interest in property that the estate acquires after the commencement of the case." See id. §§ 541(a)(6), 541(a)(7).

\textsuperscript{129} See id. § 541(a)(6) (emphasis added). The italicized portion of section 541(a)(6) is often referred to as the earnings exception. See, e.g., Susan Gummow, \textit{Earnings Exception}, 98 Com. L.J. 379, 393 (1993) (arguing that the definition of earnings under section 541(a)(6) depends on the facts of the particular case). But see Louis M. Phillips & Tanya Martinez Shively, \textit{Ruminations on Property of the Estate—Does Anyone Know Why a Debtor's Postpetition Earnings, Generated by Her Own Earning Capacity, Are Not Property of the Bankruptcy Estate?}, 58 La. L. Rev. 623, 645 (1998) (arguing that the earnings exception does not arise in section 541(a)(6) alone, but is a product of the interplay between sections 541(a)(1), 541(a)(6), and 365(c)(1)).

\textsuperscript{130} Several property interests are excluded from the estate. Section 541(b)(1) excludes from property of the estate any interest possessed by the debtor that may be exercised solely for the benefit of another. For example, if the debtor holds property
Although section 541 should be applied consistently to all types of debtors under any chapter of the Code, the purposes of each chapter and the nature of the specific debtor tend to influence what the courts ultimately consider to be property of the estate. For example, in a Chapter 7 liquidation, courts do not strain to interpret section 541(a)(6) and therefore exclude the future earnings of the debtor, thus preserving the debtor's fresh start. Under Chapter 13, the property of the estate includes all of the property specified in section 541, whether acquired pre- or post-petition, and also encompasses earnings from services performed by the debtor after commencement of the bankruptcy proceedings.

Determining the property of the estate in a Chapter 11 proceeding is more complicated for the individual debtor because of the section 541(a)(6) earnings exception. To preserve the individual debtor's fresh start, most courts have refused to include post-petition earnings from services performed by the debtor in the Chapter 11 estate. Thus, although the earnings generated by a sole proprietorship are included within the estate, the personal earnings of the sole proprietor, such as a salary, are excluded. This distinction results from the courts' deference to both the policy of preserving the debtor's fresh start and to the principles of the Thirteenth Amendment. The classification of property of the estate in a Chapter 11 case involving an individual who does not own a business in trust for another, the trust corpus will not become part of the estate. See 11 U.S.C. § 541(b)(1); see, e.g., In re McCafferty, 96 F.3d 192, 197-99 (6th Cir. 1996) (holding that because the debtor possessed only bare legal title to pension benefits, while debtor's ex-spouse possessed equitable interest, only legal title passed to the estate).


132. See Toibb v. Radloff, 501 U.S. 157, 164 (1991) ("Differences in the requirements and protections of each chapter reflect Congress' appreciation that various approaches are necessary to address effectively the disparate situations of debtors seeking protection under the Code.").

133. See 11 U.S.C. §§ 701-766; see also supra Part I.A.1 (detailing Chapter 7).

134. See infra notes 143-51 and accompanying text (discussing the individual debtor's fresh start).

135. See infra notes 143-51 and accompanying text (discussing the debtor's fresh start).

136. The post-petition earnings of the individual debtor are not included in the estate, thereby giving the debtor a financial means with which to start his new life. See infra notes 143-51 and accompanying text (discussing the fresh start).

137. "Neither slavery nor involuntary servitude, except as a punishment for crime whereof the party shall have been duly convicted, shall exist within the United States, or any place subject to their jurisdiction." U.S. Const. amend. XIII, § 1. The argument is that by including the personal earnings of the individual debtor in the estate, the Thirteenth Amendment's proscription against involuntary servitude may be violated because the debtor would be working for the benefit of his creditors. See infra notes 152-53 and accompanying text (discussing the Thirteenth Amendment).
is similar to classification of property of the estate under Chapter 7. The courts generally do not include the post-petition earnings of the individual debtor who is not engaged in business as property of the estate in either Chapter 7 or 11. The fresh start should preclude courts from including in the debtor's estate the post-petition earnings of the individual Chapter 11 debtor. However, courts' interpretations of which earnings become property of the estate for these debtors are inconsistent, often varying because the debtor is engaged in business as a sole proprietor. Part II of this Note explores courts' conflicting interpretations of property of the estate under section 541 and identifies the factors behind their reasoning.

II. DEBTORS IN CHAPTER 11: VARYING INTERPRETATIONS OF SECTION 541(A)(6)

This part revisits the fresh start in the context of post-petition earnings, and examines courts' interpretations of those earnings that are deemed property of the estate for both individual Chapter 11 debtors engaged in business and those who are not. As this Note argues, the determination of whether post-petition earnings should be included in an individual Chapter 11 debtor's estate is unnecessary because there is no requirement in Chapter 11 that the debtor fund his plan with estate property. As discussed in Part III, although many courts exclude from the estate the post-petition earnings of the individual Chapter 11 debtor, they require the debtor to use these funds in determining whether the debtor's plan is confirmable.

A principal policy consideration underlying the Bankruptcy Code is the debtor's fresh start. The fresh start is the debtor's ability to resume his life free from the financial difficulties of his past, and is achieved through the discharge of the debtor's debts after he has paid the amount that he is able to pay. Courts sometimes exclude from the debtor's estate the post-petition earnings of the individual debtor in order to protect this fresh start. In Local Loan Co. v. Hunt, the

140. Section 541, defining the property of the estate, applies to all of the chapters of the Code and should be analyzed similarly in each chapter. See 11 U.S.C. §§ 103(a), 541.
141. See In re Bemish, 200 B.R. 408, 408-09 (Bankr. M.D. Fla. 1995) (holding post-petition earnings are not included in the Chapter 7 estate); In re Fernandez, 97 B.R. 262, 262 (Bankr. E.D.N.C. 1989) (same under Chapter 11); see also supra notes 143-51 and accompanying text (discussing the debtor's fresh start).
142. Section 541(a)(6) includes in the estate "[p]roceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case." 11 U.S.C. § 541(a)(6).
144. See Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934).
145. See supra note 34 and accompanying text.
146. 292 U.S. 234 (1934).
Supreme Court preserved the individual debtor's fresh start by refusing to allow a wage assignment to survive the debtor's discharge, noting that the purpose of the fresh start would be frustrated if the individual debtor were forced to contribute future earnings to pay debts. As the Supreme Court stressed:

[The] purpose of the act has been again and again emphasized by the courts as being of public as well as private interest, in that it gives to the honest but unfortunate debtor . . . a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt.

Acknowledging the importance of preserving the debtor's fresh start, the Supreme Court in Segal v. Rochelle developed a test to determine which of the debtor's post-petition earnings become property of the estate. According to the Court, if the property "is sufficiently rooted in the pre-bankruptcy past and so little entangled with the bankrupts' ability to make an unencumbered fresh start . . . it should be regarded as 'property' [of the estate]."

Another consideration that has influenced courts' narrow interpretations of post-petition earnings that are includable as property of the estate is the Thirteenth Amendment's proscription against involuntary servitude. Consistent with the Thirteenth Amendment, some bankruptcy courts will not compel a debtor to work for his creditors, and thus, refuse to include in the estate the post-petition earnings of the individual Chapter 11 debtor.

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147. See id. at 245.
148. Id. at 244 (citations omitted).
150. See id. at 379-80.
151. Id. at 380. The issue before the Court was whether the loss-carryback tax refunds of the debtor's partnership belonged to the estate or to the debtors. The Court concluded that the loss-carryback was "property" under section 70a(5) of the Act (section 70a(5) was the predecessor of section 541 of the Code) because a contingent or "postponed enjoyment does not disqualify an interest as 'property'" as defined under that section of the Act. Id. at 380.
152. The Thirteenth Amendment provides: "Neither slavery nor involuntary servitude, except as a punishment for crime whereof the party shall have been duly convicted, shall exist within the United States, or any place subject to their jurisdiction." U.S. Const. amend. XIII, § 1.
153. See, e.g., In re Markman, 5 B.R. 196, 198-99 (Bankr. E.D.N.Y. 1980) (asserting in dicta that had Chapter 13 required future income contribution for a mandatory period of time, it may have violated the Thirteenth Amendment in that "compulsory service in payment of a debt" is essentially involuntary servitude). But see Toibb v. Radloff, 501 U.S. 157, 166 (1991) (holding that "Congress' concern about imposing involuntary servitude on a Chapter 13 debtor is not relevant to a Chapter 11 reorganization" because Chapter 11 does not contain a provision including the debtor's future earnings); In re Angobaldo, 160 B.R. 140, 150 (Bankr. N.D. Cal. 1993) (finding the Chapter 11 debtor's Thirteenth Amendment argument unpersuasive because the debtor had his choice of chapters under the Code and that he "has not been compelled to labor for another against his will in the sense that there is involuntary servitude").
Aside from policy considerations such as the fresh start and the Thirteenth Amendment's proscription against involuntary servitude, another factor courts take into account in determining the property of the estate for the individual Chapter 11 debtor is whether the debtor is engaged in business. Because the earnings exception in section 541(a)(6) excludes from the estate only that income that is earned from services performed by the individual debtor, courts have questioned which property of the individual Chapter 11 debtor becomes property of the estate based on the source of the earnings, and have differentiated the debtor engaged in business from the debtor who is not.

When an individual debtor files for bankruptcy, a new entity is created: the estate. Property of the estate is comprised of the debtor's legal and equitable interests in property as of the petition's filing date. The post-petition earnings of the individual debtor are not considered property of the Chapter 11 estate because they do not exist as property on the petition date. Because the individual does not have a current interest in his future income, neither does the estate. By contrast, the post-petition earnings of a corporation, the typical Chapter 11 debtor, do constitute property of the estate. These earnings derive from the assets of the corporation — assets that are property of the debtor-corporation's Chapter 11 estate as of the date of filing its petition. Also included is any interest in property that the estate acquires after commencement of the case. Therefore, the post-petition income of the corporate debtor is deemed property of the estate.

Where the Chapter 11 debtor is a sole proprietor, the assets of the sole proprietorship become property of the estate. When equating the Chapter 11 sole proprietorship with a Chapter 11 corporation, most courts conclude that any post-petition income generated by the sole proprietorship's business assets constitutes property of the estate,
but that any income relating to the post-petition services of the individual debtor is not property of the estate.\textsuperscript{163} In the case of the individual debtor in Chapter 11 who is not operating a sole proprietorship, there is no need to engage in this bifurcated analysis because there is no business to reorganize, and section 541(a)(6) can be interpreted literally without difficulty.\textsuperscript{164}

Courts that have addressed the issue of whether post-petition earnings of the Chapter 11 debtor who is a sole proprietor become part of the bankruptcy estate under section 541(a)(6) have applied a plethora of different rationales to reach their conclusions.\textsuperscript{165} As noted, the majority of these courts have held that post-petition income derived from personal services rendered by the individual debtor are excluded from the estate, while post-petition income derived from the sole proprietor’s business assets are included within the debtor’s estate.\textsuperscript{166} A minority of courts include in the estate all of the debtor’s post-petition earnings, regardless of the source of the income.\textsuperscript{167}

The majority approach purports to accord section 541(a)(6) its plain meaning,\textsuperscript{168} yet the application of the section 541(a)(6) exception is somewhat inconsistent depending on how courts define the term “services performed.”\textsuperscript{169} The Ninth Circuit’s leading case, \textit{In re FitzSimmons}, holds that “the earnings exception applies only to services performed \textit{personally} by an individual debtor.”\textsuperscript{170} In

\textsuperscript{163} See 11 U.S.C. § 541(a)(6); see also Leif M. Clark, \textit{Chapter 11—Does One Size Fit All?}, 4 Am. Bankr. Inst. L. Rev. 167, 188, 190, nn. 129-30 (1996) (discussing the unique situation of the individual Chapter 11 debtor and the problems of defining “in business”); \textit{infra} Part II. But see \textit{infra} notes 185-200 (detailing cases that hold that post-petition earnings of the individual debtor are property of the estate).

\textsuperscript{164} An analogy can be made to a Chapter 7 corporate case, where liquidation terminates the business and precludes any possibility of reorganization by the corporation.

\textsuperscript{165} The two principal rationales are the debtor’s fresh start and avoidance of a violation of the Thirteenth Amendment. \textit{See supra} notes 142-55 and accompanying text (discussing the debtor’s fresh start and the Thirteenth Amendment).

\textsuperscript{166} \textit{See, e.g., In re Cooley}, 87 B.R. 432, 439 (Bankr. S.D. Tex. 1988) (holding that the burden of proof is on creditors to distinguish between debtor’s and business earnings); \textit{FitzSimmons} v. Walsh (\textit{In re FitzSimmons}), 725 F.2d 1208, 1212 (9th Cir. 1984) (remanding case for determination of the debtor’s personal service earnings).


\textsuperscript{168} Section 541(a)(6) includes in the estate “Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.” 11 U.S.C. § 541(a)(6).

\textsuperscript{169} \textit{See, e.g., Gummow, supra} note 129, at 381-93 (analyzing the section 541 cases and concluding that defining earnings under section 541(a)(6) depends on the specific factual situation).

\textsuperscript{170} \textit{In re FitzSimmons}, 725 F.2d at 1211 (emphasis in the original). The Ninth Circuit added the word “personally” to section 541(a)(6), which excludes from the estate earnings from the services performed by the individual debtor after the commencement of the case. \textit{See also supra} notes 129, 142 and accompanying text (discussing the text of section 541(a)(6)).
FitzSimmons, the debtor, an owner and operator of a sole proprietorship law practice, filed a Chapter 11 bankruptcy petition. The court maintained that the proceeds from the law firm that were not personally earned by the debtor became property of the estate and remanded the case for a determination of those earnings. The FitzSimmons court based its holding on the presence of the “earnings exception” in the provisions of Chapter 11 and its absence in the provisions of Chapter 13. Because the provisions of Chapter 11 are silent on the inclusion of the future earnings of the individual debtor, the court refused to include those earnings in the estate. The court also rejected the argument that section 541(a)(6) excludes from the estate all post-petition earnings of a sole proprietorship, asserting that this interpretation of the statute would “preclude operation of sole proprietorships under Chapter 11.” Without the earnings generated by the law firm, as distinct from the earnings of the debtor, there would be no estate to reorganize.

In re Altchek adopted a substantially similar approach to FitzSimmons, except that there, Judge Schwartzberg found that he “[w]as bound to uphold the laws as set forth in the Bankruptcy Code,” and refused to interpret the exception in section 541(a)(6) to mean “personal services” as the Ninth Circuit had done in FitzSimmons. The court, however, determined that the estate consisted of pre-petition property of the debtor and all proceeds and profits that accrue to the estate post-petition, but not the post-petition earnings from the services of the debtor.

One other variation to the majority approach was applied in In re Cooley. In Cooley, the debtor, a doctor with a five-surgeon practice, filed for Chapter 11 relief. The court examined the case law interpreting section 541(a)(6) and concluded that a valuation of the debtor’s services was neither practical nor required by the statute.

171. See In re FitzSimmons, 725 F.2d at 1211-12.
172. See id. at 1211 (“If Congress had intended to make the earnings exception inapplicable to Chapter 11 cases, we believe that it would have done so explicitly, as it did in § 1306.”); see also supra notes 108-20 and accompanying text (comparing Chapters 11 and 13).
173. In re FitzSimmons, 725 F.2d at 1211.
174. See id. This reasoning of the FitzSimmons court, while true to the language of section 541(a)(6), is inconsistent with the confirmation-standard cases discussed infra Part III.
176. Id. at 955 (emphasis supplied); supra note 170 and accompanying text (emphasizing that the FitzSimmons court interpolated the word “personal” into section 541(a)(6)). In practice, the approaches used in Altchek and FitzSimmons result in the same separation of income generated by the individual from that generated by the business.
177. See In re Altchek, 124 B.R. at 955.
179. See id. at 439. In fact, the court held that, “[t]he earnings exception was not drafted in terms of ‘reasonable compensation’ of an individual’s services or in terms
Distinguishing *FitzSimmons*, the court focused on the fact that the earnings exception existed not only to differentiate the individual debtor from the estate, but more important, to avoid any potential conflict with the Thirteenth Amendment. What constitutes property of the individual Chapter 11 debtor's estate, the court held, depended in part on whether the debtor contemplated reorganization or liquidation. Notably, the *Cooley* court placed the burden of proof on the moving creditor to provide evidence that the earnings in question were property of the estate and not of the debtor. Under this interpretation, all earnings of the sole proprietorship were excluded from the estate, unless the creditor could prove that the income was either derived from property of the estate or that the debtor did not earn the income by rendering his services.

A distinct minority of courts interprets section 541 very differently. *In re Herberman* is typical of courts taking this minority approach. The court in *In re Herberman* treated an individual Chapter 11 debtor, who owned a sole proprietorship, as a corporation and granted the debtor a salary, similar to what the CEO of 'services personally performed' which might have suggested a directive towards valuing an individual's 'hands-on' contributions in the form of services.”

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180. See id. at 440; see also *In re Molina y Vedia*, 150 B.R. 393, 398-400 (Bankr. S.D. Tex. 1992) (discussing section 541(a)(6) and naming the Thirteenth Amendment's proscription against involuntary servitude as a policy behind Congress's exclusion of post-petition earnings of individual debtors in Chapters 7 and 11 because of possible involuntarily filings); supra notes 152-53 (discussing the Thirteenth Amendment).

181. The estate in a Chapter 11 liquidation case, which is similar to a Chapter 7 liquidation, will include less property than the estate in a Chapter 11 proposed reorganization because property in a liquidation case will not be subject to the provisions of section 541 regarding property acquired after the petition is filed. See 11 U.S.C. § 541 (1994) (property of the estate); id. § 1123 (providing for a liquidating Chapter 11 plan); *In re Cooley*, 87 B.R. at 440; see also supra Part I.A.2 (describing Chapter 11 generally).

182. See *In re Cooley*, 87 B.R. at 441. Initially, the debtor must prove that "(1) [she] is an individual, (2) who performs services, (3) which generates earnings, (4) post petition," and then the creditor must prove that the earnings belong to the estate. *Id.* at 439; *see also In re Molina y Vedia*, 150 B.R. at 397-402. The court in *Molina y Vedia*, adhering to the reasoning in *Cooley*, reached a contrary conclusion because the doctor-debtor in *Molina y Vedia* employed no other physicians and his support staff did not generate any income for the estate. In fact, the court in *Molina y Vedia* held that the creditors did not carry their burden of proof, and as such, all of the earnings from the debtor's medical practice were excluded from the estate. See *id.* at 402-03.

183. See *id.* at 439; *see also In re Molina y Vedia*, 150 B.R. at 397-402. The court in *Molina y Vedia*, adhering to the reasoning in *Cooley*, reached a contrary conclusion because the doctor-debtor in *Molina y Vedia* employed no other physicians and his support staff did not generate any income for the estate. In fact, the court in *Molina y Vedia* held that the creditors did not carry their burden of proof, and as such, all of the earnings from the debtor's medical practice were excluded from the estate. See *id.* at 402-03.


185. 122 B.R. 273. In this case, the court considered whether earnings generated by the debtor's sole proprietorship during the period between filing the petition and confirmation of the plan of reorganization should be classified as property of the estate under section 541(a)(6). See *id.* at 275, 288; *see also In re Harp*, 166 B.R. at 750 n.10 (citing with approval and following the reasoning of *Herberman*).
of a corporate debtor would receive. The court reasoned that post-petition earnings of the individual debtor were includable as property of the estate under section 541(a)(7), which includes in the estate "[a]ny interest in property that the estate acquires after the commencement of the case," and that the section 541(a)(6) exception applied only to earnings that were "[p]roceeds, product, offspring, rents, or profits of or from property of the estate...." Because the earnings were the result of the debtor's post-petition personal services, the court found the earnings exception inapplicable.

The estate in Herberman thus included everything that the estate, including the debtor, acquired post-commencement. Because the post-petition earnings of the debtor that derived from the debtor's practice were not proceeds, product, or offspring of property of the estate, they were not excepted and were therefore included in the estate under section 541(a)(7). The court reasoned that the salary the debtor draws from managing the estate is what is protected by the earnings exception of section 541(a)(6). The Herberman court asserted that courts should administer Chapter 11 uniformly to all types of debtors, individuals and corporations alike. The court disposed of any Thirteenth Amendment issues by noting that the debtor had filed his petition voluntarily, thereby avoiding a constitutional problem.

188. In re Herberman, 122 B.R. at 278 (emphasis in case) (quoting 11 U.S.C. § 541(a)(7)).
189. Id. (quoting 11 U.S.C. § 541(a)(6)).
190. See id.
191. See id. at 278-80. This triple negative analysis is very complicated and Judge Leif Clark has conceded that the analysis does not work unless the individual debtor is engaged in business. See Reed v. Yochem (In re Reed), 184 B.R. 733, 739-40 (Bankr. W.D. Tex. 1995); Clark, supra note 163, at 182 & n.97.
192. See In re Herberman, 122 B.R. at 282-83 (stating that the court granted the debtor a salary under section 503(b)(1)(A) as an administrative expense); see also Gummow, supra note 129, at 385-86 & n.25 (quoting H.R. Rep. No. 95-595, at 355 (1977)) (arguing that legislative history indicates that the sole proprietorship debtor be employed by the estate and receive a salary); Phillips & Shively, Ruminations, supra note 129, at 637-39 (analyzing section 541(a)(6) in light of section 365(c)(1)(A), where the trustee or debtor-in-possession must assume a contract in order to bring the earnings into the estate and then employ the debtor and pay him a salary which is then excepted from the estate under section 541(a)(6)).
193. See In re Herberman, 122 B.R. at 277-78; see also 11 U.S.C. § 103(a) (providing that Chapters 1, 3, and 5 apply to cases commenced under Chapters 7, 11, 12, or 13).
194. "The debtor is presumed to be aware of all the ramifications of a chapter proceeding before voluntarily submitting himself to the regimen.... [n]or is a] voluntary petition... compelled in any legal sense...." In re Herberman, 122 B.R. at 283-84. The court also noted that there is no constitutional right to file for bankruptcy. See id. at 384; see also In re Harp, 166 B.R. 740, 748-49 (Bankr. N.D. Ala. 1993) (quoting the Supreme Court in Toibb in support of the proposition that involuntary servitude is an irrelevant contention in Chapter 11); supra note 153.
Lastly, Herberman reasoned that an individual debtor in Chapter 11, as debtor-in-possession, owes a fiduciary duty to the estate. The debtor must harmonize this duty “with his self-interested role as the entrepreneur operating the business of the enterprise,” balancing his interests with those of his creditors because “[t]here can be no ‘part’ of a debtor that is not in bankruptcy” during the pendency of a Chapter 11 proceeding. Given the special nature of the responsibilities of the individual Chapter 11 debtor-in-possession, this court believed that the best way to maintain the integrity of the Code was to have the debtor draw a salary from his own business. In practice, compensating the debtor-in-possession with a salary is easier to administer than dissecting the post-petition earnings of the sole proprietorship from the post-petition earnings of the individual debtor.

The majority approach illustrates the problems that courts have faced when interpreting section 541(a)(6) in the context of a sole proprietorship. In FitzSimmons, the Ninth Circuit interjected the word “personal” into section 541(a)(6). Consistent with FitzSimmons, courts have attempted to distinguish between post-petition income derived from a debtor’s personal services and post-petition income derived from property of the estate in order to divide the earnings according to their origin. Others have placed the burden of proving this distinction on the creditors. These courts have invoked the debtor’s fresh start and their reluctance to

(discussing the Supreme Court’s Thirteenth Amendment argument).

195. See In re Herberman, 122 B.R. at 280-82.
196. Id. at 281.
197. See id. at 281-82.
198. Id. at 279.
199. See id. at 282.
200. Compare In re Herberman, 122 B.R. at 287-88 (granting the debtor a salary from the estate), with FitzSimmons v. Walsh (In re FitzSimmons), 725 F.2d 1208, 1212 (9th Cir. 1984) (dissecting the earnings of the business from the earnings of the debtor).
201. For various commentators’ analyses of the earnings exception of section 541(a)(6) in differing contexts, see Clark, supra note 163, at 182 n.96, 97, 183-89, (arguing that Chapter 11 is sufficiently flexible to accommodate all types of debtors); Gummow, supra note 129, at 393 (concluding determination of property of the estate for individual Chapter 11 debtor engaged in business is complicated and depends on facts of each case); Jack F. Williams, The Federal Tax Consequences of Individual Debtor Chapter 11 Cases, 46 S.C. L. Rev. 1203, 1214-30 (1995) (discussing section 541(a)(6) cases and arguing that none of them were properly decided because the tax consequences of I.R.C. § 1398 were not considered by the courts in their analyses).
203. See, e.g., In re FitzSimmons, 725 F.2d at 1212 (remanding case for valuation of services “personally” earned by the individual debtor).
204. See In re Cooley, 87 B.R. at 441.
205. See supra notes 142-51 and accompanying text (discussing the debtor’s fresh start).
implicate the Thirteenth Amendment as among the policy considerations in support of their analyses. Although courts have expended much time and effort in determining what property constitutes the individual debtor's estate in Chapter 11, especially the debtor with a sole proprietorship, there is no requirement in that chapter that a debtor finance his plan with estate property. Moreover, some courts have required debtors to use the very funds that are excluded from the estate by a section 541 analysis to confirm a plan under section 1129. The next part describes the Chapter 11 plan confirmation process, and illustrates how it conflicts with courts' interpretations of what constitutes property of the estate under section 541.

III. INDIVIDUAL DEBTORS AND CHAPTER 11 PLAN CONFIRMATION

This part examines the individual debtor and plan confirmation in Chapter 11 cases, and reveals that although the provisions of Chapter 11 do not require that the individual debtor contribute post-petition earnings to fund the plan, courts often do require this contribution.

Debtors must satisfy the confirmation requirements of section 1129(a) in order to reap the benefits of Chapter 11. This obligation has proven to be particularly difficult for the individual Chapter 11 debtor regardless of whether the debtor is engaged in business. This Note focuses on the requirements of good faith and feasibility because these requirements are the most basic to confirmation and are most often violated by individual Chapter 11 debtors. Section 1129(a)(3) requires that the plan of reorganization be proposed in good faith and not contrary to law. Although good faith is not defined under the Code, "a plan is considered proposed in good faith if there is a reasonable likelihood that the [p]lan will achieve a result consistent with the standards prescribed under the Code."212

The debtor's ability to fund a plan of reorganization is the primary factor that courts consider when determining whether the individual

206. See In re Molina y Vedia, 150 B.R. 393, 398-401 (Bankr. S.D. Tex. 1992); In re Cooley, 87 B.R. at 437-38; see also supra notes 152-53 and accompanying text (discussing the Thirteenth Amendment).

207. See 11 U.S.C. § 1129(a) (1994); see also supra notes 54-60 and accompanying text (describing the confirmation standards of section 1129(a)).

208. See infra notes 211-43 and accompanying text (discussing the individual debtor and confirmation proceedings).

209. See supra notes 70-72 and accompanying text for a discussion of good faith under Chapter 11.

210. See supra notes 66-69 and accompanying text for a discussion of feasibility under Chapter 11.


212. In re Kemp, 134 B.R. 413, 414 (Bankr. E.D. Cal. 1991) (citations omitted); see also In re Madison Hotel Assocs., 749 F.2d 410, 425 (7th Cir. 1984) (applying a similar good faith standard to a corporate Chapter 11 debtor).
debtor has proposed his plan in good faith. Remarkably, some courts have construed section 1129(a)(3) to require the individual debtor to contribute post-petition earnings in funding a plan of reorganization, even though there is no such requirement in Chapter 11 and the post-petition earnings of the individual debtor are not considered property of the estate. These courts acknowledge that post-petition income earned from the individual debtor's personal services is not property of the estate under section 541(a)(6), but nevertheless consider how the debtor has previously spent the excluded funds when deciding whether a plan has been proposed in good faith. As one court has noted, "[i]f the debtor's plan provides that the debtor will use his substantial income to make heavy mortgage payments on a lavish house, to pay for luxury cars, and to generally support an extravagant lifestyle, the plan may not meet the confirmation requirements of 11 U.S.C. § 1129(a)."

The court in In re Weber also acknowledged that "[i]n practical reality, individual debtors will generally need to utilize some portion of the very post petition earnings which are excluded from the estate in order to fund a confirmable plan of reorganization." In addition, the court observed that "[t]he difficulty lies in determining how to measure whether a financial commitment is sufficient." The Weber court applied Chapter 13's disposable income test, finding that it provided a suitable guideline to determine whether the debtor's plan had proposed sufficient funding from post-petition income to satisfy

214. See Roland v. Unum Life Ins. Co., 223 B.R. 499, 503-06 (E.D. Va. 1998); In re Weber, 209 B.R. 793, 798-800 (Bankr. D. Mass. 1997); In re Harman, 141 B.R. 878, 889 (Bankr. E.D. Pa. 1992); In re Kemp, 134 B.R. at 415 (holding that the individual debtor had not proposed his plan in good faith because he was financially "capable of making payments substantially higher than he has offered in his Plan" and therefore denying confirmation of the debtor's plan). But see In re Flor, 166 B.R. 512, 515-16 (Bankr. D. Conn. 1994) (holding that debtor's plan, which was to be funded with post-petition income, violated section 1129(a)(3) because Connecticut law proscribed assignment of future wages).
216. In re Fernandez, 97 B.R. at 263. Moreover, the court noted that although there is no "disposable income" test in Chapter 11, the ability to pay is a factor in determining whether a plan has been proposed in good faith. See id.
217. 209 B.R. at 800 (holding the individual debtor's plan unconfirmable because, as proposed, it did not diminish the debtor's lavish lifestyle and only purported to pay creditors a five percent dividend).
218. Id. at 798 n.7; see also In re Keenan, 195 B.R. 236, 242-43 (Bankr. W.D.N.Y. 1996) (finding that lack of funds with which to finance a reorganization, where the debtor does not contribute post-petition earnings to the plan, may result in conversion or dismissal); In re Powell, 187 B.R. 642, 647 (Bankr. D. Minn. 1995) (same); In re Altchek, 124 B.R. 944, 956 (Bankr. S.D.N.Y. 1991) (same).
220. See supra notes 103-07 and accompanying text for a description of the disposable income test in Chapter 13.
the good faith requirement.\textsuperscript{221}

When considering whether to convert a case from Chapter 11 into a Chapter 7 liquidation, or whether to dismiss it altogether,\textsuperscript{222} courts have also examined the individual debtor’s ability to pay in relation to good faith under section 1112(b),\textsuperscript{223} governing conversion or dismissal of a case for cause. Granting a motion to convert or dismiss is appropriate where the court determines that the plan is unconfirmable.\textsuperscript{224} For example, in deciding a creditor’s section 1112(b) motion to convert the case to one under Chapter 7, the court in \textit{Rundlett}\textsuperscript{225} stated that “the debtor’s plan must be tenable and must reflect that the debtor will fund the plan with income that does not already constitute property of the estate.”\textsuperscript{226} In making these remarks, the court implied that the individual debtor’s post-petition earnings, which are not included as property of the estate under section 541(a)(6), must be used to fund the plan.\textsuperscript{227}

Section 1129(a)(11) requires that the debtor’s plan, as proposed to the court, be feasible.\textsuperscript{228} Although this standard does not require guaranteed success, the debtor must be able to carry out the plan that he has proposed.\textsuperscript{229} In the individual-debtor context, courts

\textsuperscript{221} See In re Weber, 209 B.R. at 798-99. The court was reluctant to apply the disposable income test without noting that Chapter 13 could only be initiated voluntarily, while Chapter 11 may be initiated involuntarily and the court stressed that individual debtors who have accumulated too much debt, thus making them ineligible for Chapter 13, should not receive more favorable treatment in Chapter 11 than in Chapter 13. See id. at 799.

\textsuperscript{222} See supra notes 73-81 and accompanying text for a discussion of conversion or dismissal under section 1112(b).

\textsuperscript{223} See In re Rundlett, 136 B.R. 376, 381 (Bankr. S.D.N.Y. 1992) (discussing good faith and dismissing the case under section 1112(b) because the debtor had the ability to pay yet did not propose sufficient payments in his plan); In re Tejano, 135 B.R. 686, 688 (Bankr. D. Kan. 1991) (same); In re Devine, 131 B.R. 952, 956 (Bankr. S.D. Tex. 1991) (same); In re Canion, 129 B.R. 465, 470 (Bankr. S.D. Tex. 1989) (same); In re Khan, 34 B.R. 574, 579-80 (Bankr. W.D. Ky. 1983) (same). If a court finds that the debtor’s plan is unconfirmable under section 1129, the court may have the debtor amend the plan, or the court may dismiss or convert the case under section 1112(b) for cause, including an inability to effectuate a plan. See 11 U.S.C. § 1112(b)(1994).

\textsuperscript{224} See In re Rundlett, 136 B.R. at 381 (citing Toibb v. Radloff, 501 U.S. 157 (1991)).


\textsuperscript{226} Id. at 380-81; see also In re Tejano, 135 B.R. at 688 (“If an individual without a business is to file a chapter 11 case, then reorganization must ordinarily be the goal and the debtor must devote his [post-petition] income to that goal.”).

\textsuperscript{227} See In re Rundlett, 136 B.R. at 381; see also supra Part I.B (describing section 541 and property of the estate). Judge Schwartzberg had previously engaged in the exercise of determining whether the post-petition earnings of an individual Chapter 11 debtor with a sole proprietorship became property of the estate. See In re Altchek, 124 B.R. 944, 956 (Bankr. S.D.N.Y. 1991).

\textsuperscript{228} See 11 U.S.C. § 1129(a)(11); see also supra notes 66-69 and accompanying text (describing section 1129(a)(11) and feasibility).

interpreting section 1129(a)(11) look to the same factors as they would when determining whether a corporate debtor's plan is feasible. Ascertaining whether a debtor's plan is feasible is highly fact-sensitive and will necessarily depend on the facts of each case. Individual debtors who propose to fund their plans without including their post-petition earnings, and who do not have any other means with which to pay creditors, risk rejection of their plans by the bankruptcy court.

Courts also consider the feasibility requirement of section 1129(a)(11) when the individual debtor is unable to consensually confirm a plan and seeks to "cram down" the plan over objecting creditors. An individual debtor may violate the absolute priority rule by attempting to cram down a plan that proposes retention of some of his non-exempt property while not providing for full payment to his creditors. The individual debtor in this situation is deemed to be a "junior creditor" and cannot retain any property on account of his interest unless all other claims above him are satisfied.

The leading case analyzing the individual debtor and non-consensual confirmation or "cram down" under section 1129(b) is Norwest Bank Worthington v. Ahlers, in which the Supreme Court held that "sweat equity" did not constitute new value in order to cram down a plan on creditors. Adhering to the ruling in Ahlers, bankruptcy courts have concluded that the contribution of the debtor's post-petition income is an insufficient source of "new

is to prevent confirmation of visionary schemes).

value.”\textsuperscript{238} to justify deviation from the absolute priority rule.\textsuperscript{239} Although the Supreme Court in \textit{Ahlers} held only that the “promise of future services” on the debtor’s farm was inadequate as new value,\textsuperscript{240} these courts have extended the holding in \textit{Ahlers} so that even a commitment of wages or future income will not satisfy the new value exception. These courts reason that new value must come from an outside source, whereas future income derives from the debtor himself.\textsuperscript{241} Courts have also opined that new value must be contributed “up front,” either on the plan’s confirmation date or on its effective date, and because the debtor must work before he is able to receive future income, he is unable to meet the up-front requirement.\textsuperscript{242} Thus, where the individual debtor wants to cram down a plan and offers future wages as “new value” so that he may retain property, courts find the new value insufficient and hold the plan not feasible and therefore, unconfirmable.\textsuperscript{243}

Individual debtors face a variety of problems in confirming their plans of reorganization, whether they seek to confirm consensually or non-consensually. Good faith and feasibility are the main obstacles in the path of the individual debtor on the road to confirmation, in that these requirements often require the debtor to contribute his post-petition earnings to fund the plan, even though a section 541 analysis would exclude these funds from the estate. The next part compares section 541 and the confirmation requirements of section 1129 and argues that Congress should amend the Code to bring conflicting interpretations of these sections in line with one another.

\textsuperscript{238} See supra notes 88-97 and accompanying text for a discussion of the new value exception to the absolute priority rule.


\textsuperscript{240} See \textit{Ahlers}, 485 U.S. at 202-09.

\textsuperscript{241} See \textit{In re Rocha}, 179 B.R. at 307; \textit{In re Harman}, 141 B.R. at 887 (speculating that a money gift from a friend or relative may satisfy the outside capital requirement for the individual debtor in Chapter 11 cram down).

\textsuperscript{242} See \textit{In re Kovalchick}, 1995 WL 118171, at *5-*7; \textit{In re Pecht}, 57 B.R. at 140.

\textsuperscript{243} See supra note 239 for an examination of individual Chapter 11 debtor cram down cases. Most of the cases dealing with section 1129(a)(11) in the individual debtor context also deal with the issue of non-consensual confirmation.
IV. THE SENATE’S PROPOSED AMENDMENTS: RECONCILING SECTION 541 AND THE CHAPTER 11 CONFIRMATION STANDARDS

Part II described courts’ interpretations of section 541(a)(6) in determining what constitutes property of the individual Chapter 11 debtor’s estate, while Part III detailed the confirmation standards of Chapter 11 for the individual debtor. This part analyzes both sections of the Code in light of the goal of confirmation and introduces the Senate’s recently passed amendments that would require the individual Chapter 11 debtor to contribute his post-petition earnings, in the form of a disposable income test, to fund his plan. This Note argues in favor of the passage of these amendments.

If the individual Chapter 11 debtor seeks consensual confirmation of his plan and does not propose to fund the plan with post-petition income, the plan will most likely be unconfirmable, because it does not meet the provisions of section 1129(a) regarding good faith and feasibility. In contrast, where the debtor seeks to cram down his plan and retain any of his non-exempt property, he will be unable to confirm if he proposes to fund the plan with his post-petition earnings. If he proposes to fund the plan with future earnings, he cannot confirm non-consensually, and if he does not propose funding with future earnings, then he cannot confirm consensually. The individual debtor thus finds himself in a conundrum.

Notwithstanding courts’ confusion as to whether post-petition income constitutes property of the individual Chapter 11 debtor’s estate, courts have not construed Chapter 11’s confirmation standards to turn on this distinction. Whereas section 541 governs property of the estate in all cases under Chapters 7, 11, 12, and 13, the boundaries of this section as applied in Chapter 11 are amorphous. Despite the focus of creditors, debtors, and courts, the precise contours of the property of the estate have little consequence to the ultimate goal of confirmation. Section 541 is thus a red herring in individual

244. See supra notes 207-31 and accompanying text (discussing individual Chapter 11 consensual confirmation cases).
245. See supra notes 233-43 and accompanying text (analyzing individual Chapter 11 non-consensual confirmation cases).
246. See supra notes 136-38 and accompanying text (examining property of the estate in Chapter 11); supra note 181 (discussing liquidating Chapter 11 cases).
247. Valuation of the debtor’s estate under section 541 is important for a variety of reasons, including determining whether the “best interest of creditors test” is met for plan confirmation under Chapter 11 or 13, and in the circumstance where the case is converted to one under Chapter 7. Compare 11 U.S.C. § 1129(a)(7) (1994) (providing that creditors of a Chapter 11 debtor not receive less than they would in a Chapter 7 liquidation), with id. § 1325(a)(4) (same in Chapter 13); compare id. § 1112(b) (stating that a case may be converted to Chapter 7), with id. § 1307 (same); see also 7 Collier on Bankruptcy ¶ 1129.03[7](b)(1) n.91 (15th ed. 1999) (describing that the liquidation value of property of the estate should be included in all Chapter 11 plans to aid in determining if the best interest of creditors test is satisfied).
Chapter 11 debtor cases because Chapter 11 does not require that estate property be used to fund the plan of reorganization. Judge Kaplan, in In re Keenan,248 understood this and refused to decide whether the property at issue in that case was property of the individual debtor's estate.249 Instead, Judge Kaplan ruled that the individual debtor in Chapter 11 may use estate property for personal needs and that if the use of these funds was "wanton," creditors could attempt to have the case dismissed or converted.250

There is no statutory provision in Chapter 11 relating to the inclusion or exclusion of post-petition income of the individual debtor, either as property of the estate or as a pre-requisite to plan confirmation.251 Chapter 11 contains no requirement that either property of the estate or property other than that constituting the estate be used to finance the debtor's reorganization.252 If the debtor in Chapter 11 is able to fund a plan and the creditors are paid, the source of the financing makes no difference.253

Nor does Chapter 11 include a disposable income test,254 although courts often introduce one when deciding whether to confirm an individual debtor's plan.255 Courts that have interpreted section 1129(a) to require that the individual debtor fund his plan with post-petition earnings to satisfy the good faith and feasibility requirements have effectively written a disposable income test into Chapter 11.256 If Congress had intended, by the inclusion of the good faith requirement, that courts should impose a disposable income test on the individual debtor, then the disposable income test in Chapters 13 would be redundant, because this Chapter also includes a good faith requirement for plan confirmation.257 Courts' interpretations of the confirmation standards of section 1129 to require that individual debtors contribute post-petition earnings to their plans are consistent with the general policy of not tolerating debtors who abuse the Code, but inconsistent with the plain language of the Code. Congress should

249. See id. at 240-44; see also supra note 218 (discussing the holding in Keenan).
252. See In re Keenan, 195 B.R. at 243 (discussing that there is no mandate that the debtor fund his plan with estate property or post-petition income).
253. See id.
254. The disposable income test requires that the debtor contribute his post-petition income above what is needed for the support and maintenance of the debtor and his dependents. See supra notes 103-07 and accompanying text for a discussion of the disposable income test in the Chapter 13 context.
256. See id.
therefore amend the Code to conform the plain language of the statute with the courts' results, as these results correctly refuse to allow the individual debtor to abuse the Code by attempting to gain a benefit in Chapter 11 by avoiding a disposable income test, where the debtor would be subject to such a test in Chapter 13.

The Senate has recently passed amendments to its version of the Bankruptcy Reform Act of 1999. Currently, these amendments include in the estate the post-petition income of the individual Chapter 11 debtor and require him to use this income to fund his plan of reorganization. These amendments are needed in order to bring the plain language of the Bankruptcy Code in line with both the courts' results and the policies behind the Code. The first of the Senate’s amendments to Chapter 11 creates a new section, section 1115, entitled “Property of the Estate.” This section provides:

In a case concerning an individual, property of the estate includes, in addition to the property specified in section 541-

(1) all property of the kind specified in section 541 that the debtor acquires after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7, 12, or 13, whichever occurs first; and

(2) earnings from services performed by the debtor after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7, 12, or 13, whichever occurs first.

This proposed amendment would define property of the estate for the individual Chapter 11 debtor to include the debtor's post-petition earnings. The proposed language tracks the language of comparable provisions in Chapters 12 and 13, specifically sections 1207 and 1306.

The second of the Senate’s amendments would require that the debtor's plan of reorganization draw upon his post-petition earnings.

259. Other amendments may be necessary, such as an amendment regarding the stay against co-debtors. Such amendments are beyond the scope of this Note.
260. The Senate has also proposed an amendment to section 541(a)(6). This amendment alters the section to read:

Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor (other than an individual debtor who, in accordance with section 301, files a petition to commence a voluntary case under Chapter 11) after the commencement of the case.

S. Rep. No. 106-49, at 395 (1999). This amendment is important because it limits the application of the Chapter 11 disposable income test to voluntarily initiated petitions and thus avoids a possible violation of the Thirteenth Amendment's proscription against involuntary servitude. See supra notes 152-53 and accompanying text for a discussion of the Thirteenth Amendment.
Thus, section 1123(a) would be annexed to provide:

(8) in a case concerning an individual, provide for the payment to creditors through the plan of all or such portion of earnings from personal services performed by the debtor after the commencement of the case or other future income of the debtor as is necessary for the execution of the plan.\(^{263}\)

This amendment would require that the individual debtor's plan commit any of the debtor's future earnings as necessary for implementing the plan of reorganization.

The last of the Senate's amendments modifies the confirmation standards of section 1129. Section 1129(a) would be appended to include:

(14) In a case concerning an individual in which the holder of an allowed unsecured claim objects to the confirmation of the plan:
- (A) the value of the property to be distributed under the plan on account of such claim is, as of the effective date of the plan, not less than the amount of such claim; or
- (B) the value of the property to be distributed under the plan is not less than the debtor's projected disposable income (as the term is defined in section 1325(b)(2)) to be received during the three-year period beginning on the date that the first payment is due under the plan, or during the term of the plan, whichever is longer.\(^{264}\)

This proposed amendment obligates the debtor to either pay an objecting creditor's claim in full or contribute his disposable income to the plan. The language of this amendment tracks the language of section 1325(b)(1), except that the individual Chapter 11 debtor must contribute his disposable income for at least three years, or longer if his plan so provides.

The final amendment to section 1129 is inserted at the end of subsection 1129(b)(2)(B)(ii) and provides: "except that in a case concerning an individual, the debtor may retain property included in the estate under section 1115, subject to the requirements of subsection (a)(14)."\(^{265}\) This amendment would allow the individual debtor to retain property and non-consensually confirm or "cram down" a plan of reorganization if he pays dissenting creditors' claims in full or contributes his disposable income for three years to fund his plan. The amendment would have the effect of overruling the Supreme Court's ruling in *Norwest Bank Worthington v. Ahlers*\(^{266}\) that future labor does not constitute new value. It also overrules cases that have interpreted *Ahlers* to mean that future income or post-petition earnings cannot constitute new value in order to invoke the absolute

\(^{264}\) Id.
\(^{265}\) Id.
\(^{266}\) 485 U.S. 197 (1988).
They are overruled because the individual debtor is permitted under the Senate's proposed amendments to cram down his plan over dissenting creditors if he either pays their claims in full or contributes his post-petition disposable income to fund his plan.

These proposed amendments are consistent with the general policy of Congress and the courts of not permitting a debtor to take advantage of the provisions of the Code; thus, they provide the debtor with a "fresh start," but not a "head start." For example, courts repeatedly respond to Chapter 7 debtors who have the ability to pay their creditors either substantially or in full by dismissing their cases under section 707 for substantial abuse. Congress has several times reacted to abuse of the Code by amending its various provisions to prevent debtors from gaining more favorable treatment in one chapter than they could in another.

Neither Congress nor any court believes that Chapter 13, with its disposable income test, provides the individual debtor with any less of a fresh start than the debtor would receive in Chapters 7 or 11. In fact, the opposite is true; payment to creditors is consistent with the debtor's fresh start, as evidenced by dismissals under section 707 and the judicial interpretations of section 1129 to include post-petition

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267. See supra notes 232-43 and accompanying text for a examination of the cases interpreting Ahlers.

268. See supra note 38 and accompanying text (discussing the amendment that prevented modification of residential liens in Chapter 11); infra notes 270-72 and accompanying text (describing the situations where Congress has taken action to prevent abuse of the Code).

269. "[A]llowing a debtor to escape debts that he has the ability to repay would provide a 'head start' rather than the 'fresh start' envisioned." In re Zaleta, 211 B.R. 178, 180 (Bankr. M.D. Pa. 1997).

270. See, e.g., In re Kamen, 231 B.R. 275, 277-79 (Bankr. N.D. Ohio 1999) (finding substantial abuse to dismiss under section 707 where debtors accumulated in excess of $140,000 in credit card debt to maintain a lifestyle above their means); In re Rodriguez, 228 B.R. 601, 603-06 (Bankr. W.D. Va. 1999) (holding that debtor's ability to pay creditors in full within 10 months under Chapter 13, coupled with post-petition purchase of new truck, equaled substantial abuse to dismiss under section 707). See generally In re Zaleta, 211 B.R. at 180-83 (holding ability to repay debts is primary factor in determining substantial abuse). Currently pending in Congress is an amendment that would codify courts' interpretations of section 707(b), dismissal for substantial abuse, on account of the debtor's ability to repay his debts. See 145 Cong. Rec. S11088, § 625 (daily ed. Sept. 21, 1999) (statement of Sen. Hatch). ("[This bill] provides us with the opportunity to prevent people who can repay their debts from 'gaming the system' by using loopholes that are presently in place.").

271. For example, the 1994 amendments to the Code harmonized the treatment of debtors in Chapter 11 with the treatment of debtors in Chapter 13, by preventing Chapter 11 debtors from modifying liens on their principal residential property where they could not modify these liens in Chapter 13. See 11 U.S.C. § 1123(b)(5) (1994); H.R. Rep. No. 103-835, at 46 (1994), reprinted in 1994 U.S.C.C.A.N. 3340, 3354 ("This amendment conforms the treatment of residential mortgages in chapter 11 to that in chapter 13 . . . ."); see also supra notes 37-38 and accompanying text (discussing this amendment); supra note 237 (describing the addition of Chapter 12 to the Code, providing for family farmers, in reaction to the Ahlers case).
earnings of the individual debtor. Non-payment, on the other hand, provides the debtor with a head start and should not be tolerated, as it is an abuse of the Bankruptcy Code. These amendments, if passed, will prevent individual debtors in Chapter 11 from abusing the Code by requiring that they contribute their post-petition earnings to fund their plans and pay their creditors. In addition, the amendments will facilitate the determination of property of the estate under section 541 for the individual Chapter 11 debtor because the debtor's future earnings will be available to satisfy creditors' claims. Moreover, these amendments will stop inconsistent interpretations of the Bankruptcy Code's provisions, specifically post-petition earnings of the individual debtor, because regardless of whether the debtor is engaged in business, those earnings would now constitute property of the Chapter 11 estate and will be used to satisfy creditors' claims. Thus, the overriding policies of the Code will be reflected by the consistency of its internal provisions, and the delicate balance between creditors' and debtors' rights once again restored to equilibrium.

CONCLUSION

In interpreting the Code, courts have faced difficulty in balancing the competing interests of creditors and debtors. Courts must weigh opposing policy considerations to find a solution that will achieve a result consistent with the debtor's fresh start, equitable payment to creditors, and a refusal to allow abuses of the Code. This tension is exemplified in courts' interpretations of post-petition earnings under section 541(a)(6) for the individual debtor with a sole proprietorship, and the competing interpretations of section 1129 that require the debtor to use funds excluded from the estate under section 541 in order to effectuate plan confirmation.

When faced with confirmation of an individual Chapter 11 debtor's plan, most courts already require that the debtor pledge his post-petition income to the plan as a pre-requisite to granting discharge and conferring the fresh start. This is consistent with the underlying policy of not allowing a debtor to receive more favorable treatment in one chapter than he could receive in another. There is currently no statutory provision in Chapter 11 that supports either the inclusion or exclusion of these funds in the debtor's plan. Congress should adopt the amendments recently proposed by the Senate and formally subject the individual Chapter 11 debtor to a disposable income test. This amendment would provide courts with guidance on how to treat the individual debtor in Chapter 11 and facilitate a more uniform interpretation of the Bankruptcy Code.

272. See, e.g., In re Harman, 141 B.R. 878, 888-89 (Bankr. E.D. Pa. 1992) (holding debtor’s plan unconfirmable because debtor would maintain excessive lifestyle while creditors would not be paid).