By Krispen Carroll

Tug-of-War over Post-Confirmation Appreciation in Chapter 13

Everybody likes a windfall, the happenstance of financial luck that seems to come out of the blue. American homeowners were justified to feel like they were the beneficiaries of a windfall in recent years, as home values jumped by more than 18 percent in 2021 alone.[1] However, what if the homeowner is a chapter 13 debtor? Should they be the beneficiary of that windfall, or should it be their creditors?

Logic and an adherence to bankruptcy's underlying policy of fairness strongly suggest that the chapter 13 debtor should not reap the rewards of the marketplace while their creditors receive less than full payment on their claims. Courts thus far are split in their treatment of the newly flush debtor. A careful reading of two recent cases illuminates this conflict, and shows that chapter 13 debtors should not be able to cash in on home equity until the case is complete or creditors have been paid in full.

In a chapter 13 plan, the value of a debtor's interest in real property is determined as of the time of the confirmation of their case. Using that valuation, the dividend required to be paid to unsecured creditors is determined by a hypothetical chapter 7 liquidation.[2] Thus, no further need exists to adjust the valuation of real property in most chapter 13 cases when debtors generally retain possession of their homes for the entirety of the case. Until recently, typical chapter 13 debtors may have seen little appreciation in the value of their homes during the pendency of the case.

However, this familiar landscape has changed, and many chapter 13 debtors now have homes and investment properties that have substantially appreciated in value since the time of plan confirmation. As a result, debtors who were previously content to cure and maintain a mortgage and stay in their homes during their chapter 13 case are now looking to cash in on equity from appreciation that did not exist at the time their case was filed.

The Bankruptcy Code's guidance is muddled and if anything has spurred much litigation over this issue. Courts faced with this question have had to confront the apparent contradiction between 11 U.S.C. §§ 1306 and 1327(b). One article succinctly summarized that conflict:

> In a chapter 13 case, there are three types of property: (1) property owned by the debtor before filing, (2) property acquired by the debtor before confirmation of a plan and (3) property acquired by the debtor after confirmation of a plan. Section 1306 of the Code seems to indicate that property of the estate includes all of the debtor's property acquired after commencement of the case but before the case is closed, dismissed or converted. Section 1327(b), on the other hand, states that unless otherwise provided under the plan, the confirmation of the plan vests all of the property of the estate in the debtor. Thus, the dilemma is that the "vesting" of property of the estate in a debtor upon confirmation contravenes having post-petition, post-confirmation assets included in the property of the estate until the case is closed, dismissed or converted.[3]

Attempts to reconcile this conflict have so far garnered little consensus from the bankruptcy courts. A survey of reported decisions reveals that the courts have collectively used five different approaches to resolve this dilemma, which have been outlined in the Consumer Point article in this issue. Courts have even reached conflicting outcomes applying the same approach.

Two courts have recently used the estate-replenishment approach, with different results. In *In re Marsh*, the court concluded that proceeds from the post-confirmation gains from the sale of the debtors' home were newly acquired property that replenish the estate and are available for unsecured creditors.[4] In *In re Elassal*, the court ruled that the similar proceeds were not newly acquired property and were the debtors to retain.[5] A closer examination of each decision demonstrates that not only is the *Marsh* approach the better one, it is the one that best accomplishes the purposes of the Bankruptcy Code as reflected in chapter 13.

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1 Anna Bahney, "Home Prices Skyrocketed Last Year. Two Regions Saw the Biggest Increases," CNN Business (Feb. 2, 2022), *available at* cnn.com/2022/02/22/homes/us-home-prices-case-shiller-december-2021/index.html (unless otherwise specified, all links in this article were last visited on Nov. 2, 2023).

2 *See* 11 U.S.C. § 1325(a)(4).

3 "Property of the Estate: To Be or Not to Be, That Is the Question the Trustee Asks of Thee (Part I)," *ABI Journal*, December/January 2002, *available at* abi.org/abi-journal (internal citations omitted).

4 647 B.R. 725 (Bankr. W.D. Mo. 2023).

5 2023 WL 5537061 (Bankr. E.D. Mich. 2023).

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Application of the Estate-Replenishment Theory Has Led to Conflicting Results

The estate-replenishment theory attempts to reconcile the conflict between §§ 1306 and 1327 by giving application to both statutes, but in different phases of the chapter 13 case. Under § 1327(b), pre-confirmation property of the estate converts to the debtor's sole control at the time of confirmation through vesting. However, property acquired by the debtor following confirmation does not vest in the debtor and is instead property of the estate under § 1306 and serves to replenish it. Property acquired by the debtor after confirmation cannot vest under § 1327(b), since it did not exist as part of the estate at the time of confirmation.

In *In re Marsh*, the debtors listed the value of their home at the time of filing in September 2018 as $140,000. They sold it for $70,000 above that amount in April 2022. The debtors filed a motion to retain the sale proceeds, arguing that they were attributable to post-confirmation appreciation of the home's value and thus were not property of the chapter 13 estate. The court rejected this argument and instead concluded that the proceeds from the sale of the debtors' home attributed to post-confirmation gain were "distinct from the property sold to produce them."[6] The court concluded that the relief debtors sought could only be granted, if at all, by modification of the debtor's confirmed plan and not by motion.

As in *Marsh*, the debtor in *Elassal* filed a motion to retain all of the proceeds from an approved post-confirmation sale of her residence. The value of the debtor's home had increased by nearly $200,000 between the time of filing and the sale of the residence nearly two years later. The debtor's net gain was approximately $150,000 above the allowed exemptions. The trustee objected to the debtor's motion and filed a plan modification seeking to have the debtor contribute approximately $75,000 of the sale proceeds to provide for payment in full to unsecured creditors.

The court overruled the trustee's objection to the debtor's motion and denied the proposed plan modification. Although indicating an agreement with the estate-replenishment approach used in *Marsh*, the court found that the sale proceeds were neither newly acquired post-petition property nor disposable income of the debtor. Thus, the debtor did not need to file a plan modification to retain the funds.

In both cases, the debtors exercised control over their properties and voluntarily sold property to realize the gains of appreciation accrued during the pendency of their chapter 13 plans. It is reasonable to assume that when such a sale generates funds above the amount of the debtor's exemptions, the additional funds should be considered property of the estate and made available for distribution to unsecured creditors. A debtor's interest in the proceeds from the sale of property is an after-acquired interest and legally distinguishable from the previously held interest in the property itself.

6 *Id.* at 21.

Following the approach of the *Marsh* court and the replenishment theory, the nonexempt proceeds from a post-petition sale are property of the estate, and any request to retain a portion of those proceeds by the debtor would need to be requested by plan modification under § 1329. A debtor should be required to show that retention of any excess funds was reasonable and necessary, and outweighed the competing claims of creditors in the estate.

Retention vs. Voluntary Sale of Property by a Debtor During the Chapter 13 Case

Most homeowners who file for chapter 13 do so to keep their homes and investment properties. Allowing debtors to manage their debts while staying in their homes is a basic tenet of chapter 13. While some debtors file for chapter 13 with the express intent to sell property during the case, most do so to manage mortgage and tax debt while shielding existing equity in their homes from unsecured creditors.

Debtors who comply with the terms of their chapter 13 plans and retain ownership of their homes until the time of discharge are protected from trustees or creditors taking any action or making any claim of interest against the debtor's property, or any appreciation that accrues in that property, during the life of the plan. Once the case has been completed and a discharge has been granted, the property vested with the debtor at the time of confirmation no longer falls within the purview of any bankruptcy estate. Thus, any appreciation in that property that has accrued undoubtedly belongs to the debtor.

Absent conversion to a chapter 7, neither the trustee nor any creditor can force the sale of property during chapter 13. In other words, whether there is to be a dispute over proceeds arising from a post-confirmation chapter 13 sale is *solely in the debtor's control*. The Bankruptcy Code already offers chapter 13 debtors a clear path to retaining 100 percent of any accrued appreciation in their property simply by retaining the property until case completion. The most reasonable interpretation of how §§ 1306 and 1327 intersect is to treat post-confirmation sale proceeds as after-acquired property. To find otherwise would incentivize debtors to use chapter 13 as a vehicle to allow for property to appreciate and reap the benefits of post-confirmation sales without having to share any of those benefits with creditors or even seek their permission via a plan modification.

The *Elassal* court found that "sale proceeds cannot be untethered from real property," yet cited no authority for this conclusion.[7] In fact, there is substantial contrary authority that proceeds of a sale *are a separate and distinct form of interest* from the property itself.[8] As the *Marsh* court noted, those who have reached the opposite conclusion have done so by equating proceeds with unrealized appreciation. A debtor's interest in real property is clearly not the same as an interest in cash resulting from a property sale. To "vest" property is to "place or give into the possession or discretion of some

7 Case No. 21-42801, 2023 WL 5537061, at *10.
8 *In re Barrera*, 22 F.4th 1217, 1223 (10th Cir. 2022).

person or authority."[9] Vesting bestows control of the property with the debtor, who cannot then be compelled to sell that property to realize a gain in value and provide a greater dividend to unsecured creditors. As such, vesting does not apply to interests acquired by the debtor post-confirmation.

Maybe the most notable case invoking the estate-replenishment approach, and the most compelling for why debtors should not prevail over the interests of creditors, is *In re Barbosa*.[10] In this case, the debtors had investment property with an agreed value of $64,000 at the time of confirmation. The confirmed plan allowed the debtors to cram down the secured mortgage creditor's claim based on the agreed value and required a dividend of 10 percent to unsecured creditors.

Two years later, the debtors filed a motion for the sale of the investment property free and clear of all liens for $137,500. The debtors sought to pay only the allowed cramdown amount and the 10 percent dividend required under the confirmed plan, and to retain the balance of the proceeds from the sale. The lower court rejected this approach and sided with the trustee that the increased property value inures to the benefit of the debtor's unsecured creditors. The appellate court also came down in favor of the trustee and the estate-replenishment approach, noting that this approach honored both the letter and the spirit of the Bankruptcy Code:

> Finally, as the bankruptcy judge said, it is antithetical to the bankruptcy system to allow a debtor to "strip down" a mortgage, underpay the unsecured creditors, and obtain a super discharge under section 1328(a) ... while selling the property mortgaged for a price of two times its estimated value for purposes of the "strip down," and keeping to himself the excess of the proceeds. In fact, to allow the Debtors to keep the proceeds of the sale in such circumstances effectively defeats Congress' intention to extend the application of the "ability-to-pay" standard forward throughout the duration of the plan.[11]

Conclusion

As these cases demonstrate, the ultimate winner in the tug-of-war between debtors and creditors over post-petition appreciation is an unsettled issue in chapter 13. These cases also demonstrate that all a debtor must do to ensure that a real estate windfall is shielded from unsecured creditors is to retain their homes until the case has been completed. The estate and its unsecured creditors can share in that equity, but only if the debtors choose to convert their cases to chapter 7 or opt to sell their homes while the chapter 13 is pending.

Debtors in chapter 13 retain control of their homes and cannot be compelled to sell them and share the proceeds with pre-petition creditors. However, when debtors seek to tap into their homes' appreciated value before completing their plan and deny unsecured creditors any distribution of those proceeds, equity and the Bankruptcy Code demand that courts should weigh in on the side of creditors. abi

9 "Vest," *Merriam-Webster Dictionary*, *available at* merriam-webster.com/dictionary/vest (last visited Oct. 31, 2023).
10 235 F.3d 31 (1st Cir. 2000).
11 *Id.* at 35 (internal citations omitted).

Consumer Point

By Charissa Potts

The Debtor Is Entitled to Ch. 13 Post-Petition Asset Appreciation

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Imagine this hypothetical: An honest debtor in a confirmed chapter 13 plan becomes unable to afford her mortgage payment due to circumstances beyond her control. She has a few years to go in her chapter 13 plan and decides that the responsible thing to do is sell the home and use the sale proceeds to pay cash for a smaller home.

But wait! There is a chapter 13 trustee demanding that the confirmed plan be amended to require the debtor to pay the value of the property's post-petition appreciation into her plan. Unfortunately, the Bankruptcy Code does not provide clarity on this issue, but thanks to a few decades of precedent, the better-reasoned conclusion is that post-petition appreciation realized from the sale of a property belongs to the debtor. However, the journey to this conclusion is circuitous.

The State of the Chapter 13 Estate: The Five Approaches

The first step in determining who is entitled to post-petition appreciation is determining whether appreciation is property of the estate under § 541. The answer will depend on which approach to defining "property of the estate" is used in the debtor's jurisdiction. The approaches described herein are frequently discussed in cases involving violations of the automatic stay, when the court must determine whether post-confirmation collection actions run afoul of § 362.[1]

The lack of clear direction from the Code is primarily the result of a conflict between §§ 1306 and 1327, which both purport to define property of the estate. Specifically, § 1306 incorporates the definition of "property of the estate" from § 541 and also includes all property that a debtor acquires while the chapter 13 case is pending. In contrast, § 1327 provides that all property of the estate vests in the debtor upon confirmation (unless otherwise provided in the plan), and the debtor holds this re-vested property "free and clear" from any claim by a creditor. To determine how these two sections intend after-acquired appreciation to be treated, at least five different approaches have been crafted by various jurists.

First, the "estate termination" approach holds that the estate ceases to exist once the plan has been confirmed, and all property (whenever acquired) becomes property of the debtor. This interpretation follows the wording of § 1306(a) that the property remains part of the estate until the case has been dismissed, closed or converted. Courts holding this opinion argue that even if the property is vested in the debtor, the estate can still exist — even with no property.[2]

Second, the "estate transformation" approach holds that only the property necessary to the performance of the plan remains property of the estate. This approach originates from § 1322(a)(1), which states that the debtor's plan must provide earnings or other funds to the trustee "as is necessary for the execution of the plan."[3] The lack of concrete guidance on this interpretation means that courts are free to determine the "as is necessary" portion of § 1322(a)(1) as they see fit. However, this approach appears to contradict Bankruptcy Code policy that all of the debtor's disposable income be used to fund the plan — not just a portion of it.[4]

The third approach, "conditional vesting," gives the debtor the right to use the property at confirmation, but the right does not become final until discharge. As a result, assets that the debtor acquires after confirmation are property of the estate and may be administered in the plan.[5] Courts adopting this approach reason that it results in "a legitimate *quid pro quo*": in exchange for a discharge of debts and the ability to retain all assets under the protection of the automatic stay, the debtor has a continuing obligation to disclose all pre- and post-confirmation assets and account for them under the plan.[6] This approach is the most problematic for debtors who wish to retain any appreciation in value, and is the least favored.[7]

Fourth, the "estate preservation" approach adopted the language of § 1306(a) and holds that property of the estate remains property of the estate despite its "vesting" in the debtor at confirmation.

1 *See, e.g., In re Tarby*, 2012 WL 1390201, at *5 (Bankr. D.N.J. April 20, 2012).

2 *In re Petruccelli*, 113 B.R. 5 (Bankr. S.D. Cal. 1990).

3 Cases that follow this approach include *In re Leavell*, 190 B.R. 536 (Bankr. E.D. Va. 1995); *In re Markowicz*, 150 B.R. 461 (Bankr. D. Nev. 1993); *In re Johnson*, 36 B.R. 958 (Bankr. D. Utah 1983); *In re Thompson*, 142 B.R. 961 (Bankr. D. Colo. 1992); *Telfair v. First Union Mortg. Corp.*, 216 F.3d 1333 (11th Cir. 2000).

4 *See generally* David Gray Carlson, "The Chapter 13 Estate and Its Discontents," 7 *ABI L. Rev.* 213 (2009), *available at* abi.org/members/member-resources/law-review.

5 *City of Chicago v. Fisher (In re Fisher)*, 203 B.R. 958 (N.D. Ill. 1997).

6 *Id.* at 9-10.

7 *Gilbreath v. Averitt Express Inc.*, 2010 WL 4554090 (W.D. La. 2010) (example of court that has adopted this approach).

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This approach requires wholly disregarding § 1327, but this is often justified by creating a fiction that the term "vest" (used only in § 1327) means the transfer of a possessory interest — not the transfer of title.[8]

Finally, the fifth approach, "estate replenishment," provides that all property becomes property of the debtor at confirmation, but newly acquired property "replenishes" the estate. Courts adopting this approach view it as being the best way to harmonize §§ 1306 and 1327.[9]

Does Post-Petition Appreciation of Pre-Petition Property Belong to the Estate?

If the debtor regains full control over her property at vesting, is the increased value considered post-confirmation property that refills the estate? Is it income to the debtor that must be contributed to the plan? The better answer is "no" to both questions.

In *In re Elassal*, the court held that sale proceeds cannot be "untethered" from the underlying property.[10] To reach this conclusion, the court rejected the argument that post-petition appreciation should be treated the same way in chapter 13 as it is in chapter 7 (in which the increase in value is treated as property of the estate).[11]

The *Elassal* court first noted that it is bound by §§ 1306, 1327 and 1335, rather than the provisions of chapter 7. More important to its analysis was the nature of a chapter 13, and the "bargain" struck by a debtor who agrees to contribute all disposable income over a period in exchange for retaining property.[12] It is this bargain that distinguishes chapter 13 from chapter 7 and drives the conclusion that appreciation is not an asset separate from the underlying property.

The Ninth Circuit, in *In re Burgie*,[13] was one of the earliest to address this "bargain" in the context of post-petition appreciation. *Burgie* involved debtors who sold their residence shortly after confirmation for almost $20,000 more than the amount exempted in their petition. In concluding that the trustee was not entitled to these funds, the court explained the bargain struck by a chapter 13 debtor as one in which the debtor may retain all pre-petition property, including "earnings, assets, money in the bank and real estate."[14] In return, the debtor has to commit all her post-petition disposable income to her creditors. Creditors are protected in this bargain by the liquidation analysis and are therefore guaranteed to receive what they would have received in chapter 7.

A trustee faced with this analysis is likely to press on by claiming that appreciation is not an asset, but is income that must be contributed to the plan. Again, the debtor holds the better argument here, despite the lack of clarity in the Bankruptcy Code.

Burgie draws a clear line between what constitutes "income" vs. what constitutes an "asset." The test it relies on asks whether the asset is treated as income or an income replacement. For example, a single distribution from an individual retirement account is not income, but regular disbursements from a retirement account. Similarly, a personal-injury settlement is also income — to the extent that it is necessary for the support of the debtor. Under this test, appreciation in the value of an asset is not income to the debtor, as it does not provide a stream of income, nor can it be described as an income replacement.

The Trustee Is Not Permitted to Modify a Confirmed Plan to Capture Post-Petition Appreciation

A final point that may often be overlooked in this analysis is whether a trustee can request a modification of a confirmed plan to force the debtor to contribute appreciation to the plan. Again, the better answer is "no." The path to arriving at this conclusion begins with the language of § 1321, which very simply provides that "[t]he debtor shall file a plan." This is significant in what it does not say, as it does not authorize the trustee or a creditor to propose a plan on the debtor's behalf.

When a chapter 13 trustee demands turnover of post-petition appreciation, the trustee will typically file a motion pursuant to § 1329 to modify the confirmed plan to include those funds for distribution to creditors. Several courts have viewed this as an attempt to make an end run around § 1321. Section 1329 explicitly lists the four grounds on which a debtor, trustee or unsecured creditor may move for modification of a confirmed plan,[15] but the § 1329 grounds do not include modification to capture realized appreciation. Allowing the trustee to demand a post-confirmation amendment to capture appreciation would permit the trustee to do what § 1321 clearly states the trustee cannot do.[16]

The *Euler* court was adamant that the drafters of the Bankruptcy Code clearly intended only a debtor to have the right to propose a plan dealing with assets and liabilities as they

8 *See Sec. Bank of Marshalltown, Iowa v. Neiman*, 1 F.3d 687 (8th Cir. 1993); *see, e.g., In re Kieta*, 315 B.R. 192 (Bankr. D. Mass. 2004); *In re Koonce*, 54 B.R. 643 (Bankr. D.S.C. 1985); *In re Reynard*, 250 B.R. 241 (Bankr. E.D. Va. 2000); *In re Jones*, 422 B.R. 58 (Bankr. N.D. Miss. 2009); *In re Grissom*, 137 B.R. 689 (Bankr. W.D. Tenn. 1992); *In re Antal*, 459 B.R. 248 (E.D. Mich. 2011); *In re Camacho*, 311 B.R. 186 (Bankr. E.D. Mich. 2004); *In re Elrod*, 523 B.R. 790 (Bankr. W.D. Tenn. 2015); *United States v. Harchar*, 371 B.R. 254 (N.D. Ohio 2007); *In re Aneiro*, 72 B.R. 424 (Bankr. S.D. Cal. 1987); *In re Suarez*, 149 B.R. 193 (Bankr. D.N.M. 1993); *In re Frausto*, 259 B.R. 201 (Bankr. N.D. Ala. 2000); *In re Kelly*, 358 B.R. 443 (Bankr. M.D. Fla. 2006); *In re Moore*, 312 B.R. 902 (Bankr. N.D. Ala. 2004); *In re Tibbs*, 478 B.R. 458 (Bankr. S.D. Fla. 2012).

9 *See In re Elassal*, No. 21-42801, at *5 (Bankr. E.D. Mich. Aug. 28, 2023); *In re Marsh*, 647 B.R. 725 (Bankr. W.D. Mo. 2023); *see, e.g., City of Chicago v. Fisher (In re Fisher)*, 203 B.R. 958 (N.D. Ill. 1997); *In re Mizula*, 525 B.R. 569 (Bankr. D.N.H. 2015); *In re Barbosa*, 236 B.R. 540 (Bankr. D. Mass. 1999), *aff'd sub. nom., Barbosa v. Solomon*, 243 B.R. 562 (D. Mass. 2000), *aff'd*, 235 F.3d 31 (1st Cir. 2000); *United States v. Holden*, 258 B.R. 323 (D. Vt. 2000); *In re Vastadore*, 516 B.R. 772 (Bankr. W.D. Pa. 2014); *In re Wilson*, 555 B.R. 547 (Bankr. W.D. La. 2016); *In re Lush*, 544 B.R. 575 (Bankr. N.D. Miss. 2015); *In re Mullican*, 417 B.R. 389 (Bankr. E.D. Tex. 2008), *aff'd*, 417 B.R. 408 (E.D. Tex. 2009); *In re Garcia*, 499 B.R. 506 (Bankr. N.D. Tex. 2013), *aff'd sub. nom., Garcia v. Bassel*, 507 B.R. 907 (N.D. Tex. 2014); *In re Rodriguez*, 421 B.R. 356 (Bankr. S.D. Tex. 2009); *In re Jackson*, 403 B.R. 95 (Bankr. D. Idaho 2009); *In re Gonzales*, 587 B.R. 363 (Bankr. D.N.M. 2018).

10 *In re Elassal, supra* at *10.

11 *See, e.g., Coslow v. Reisz*, 811 Fed. App'x 980 (6th Cir. 2020).

12 *Hamilton v. Lanning*, 560 U.S. 505, 508 (2010).

13 *In re Burgie*, 239 B.R. 406 (B.A.P. 9th Cir. 1999).

14 *Id.* at 410.

15 Pursuant to 11 U.S.C. § 1329, the plan may be modified to "(1) increase or reduce the amount of payments on claims of a particular class provided for by the plan; (2) extend or reduce the time for such payments; (3) alter the amount of the distribution to a creditor whose claim is provided for by the plan to the extent necessary to take account of any payment of such claim other than under the plan; or (4) reduce amounts to be paid under the plan by the actual amount expended by the debtor to purchase health insurance for the debtor (and for any dependent of the debtor if such dependent does not otherwise have health insurance coverage)."

16 *In re Euler*, 251 B.R. 740 (Bankr. M.D. Fla. 2000).

THE LIMITED LIFESPAN OF THE BANKRUPTCY ESTATE: MANAGING CONSUMER AND SMALL BUSINESS REORGANIZATIONS

Jonathan M. Seymour[*]

ABSTRACT

Congress has a great affinity for debt adjustment bankruptcies. These are bankruptcies in which a debtor keeps rather than liquidates her assets and instead repays creditors out of future income. Chapter 13, which allows individual consumer debtors to reorganize in this way, was supplemented in 1986 by chapter 12 for farm bankruptcies. In 2019, in the largest expansion of debt adjustment bankruptcies since the Bankruptcy Code was enacted, Congress made debt adjustment bankruptcy available to small businesses.

The reality is, however, that most debt adjustment bankruptcies fail. For that reason, the relative rights of debtors and creditors when tensions arise are of great importance. The bankruptcy court must know what protections a debtor may resort to if she is struggling to make payments under her plan, and whether new, unpaid creditors may undertake their own collection efforts if doing so will jeopardize the bankruptcy case. Although these questions are basic, they are unresolved. A deep split among bankruptcy courts and courts of appeals has persisted in the law of chapter 13 since the early years of the Code. This disunity threatens the bankruptcy courts' ability to coherently implement Congress's new small business bankruptcy provisions. This Article proposes a solution to this Gordian Knot, and then attempts to situate that solution within a broader normative conception of debt adjustment bankruptcy law.

Doctrinally, the key division among courts concerns the lifespan of the bankruptcy estate. Property within the estate is subject to court supervision and protected by the automatic stay. This Article defends a theory of the bankruptcy estate in debt adjustment bankruptcies known as the estate termination theory. This theory holds that the bankruptcy estate is of a limited lifespan. Once the debtor has secured court approval for a repayment plan and the case is

[*] Visiting Assistant Professor, Duke University School of Law. My interest in this subject arose out of my experiences litigating these issues while in practice in the Bankruptcy and Financial Restructuring Group at WilmerHale, where I was among counsel to the City of Chicago in the *Steenes* and *Cherry* litigation described in this article. For helpful comments and feedback, I am grateful to Stuart Benjamin, Elisabeth de Fontenay, Craig Goldblatt, Sara Sternberg Greene, Melissa Jacoby, and Steven Schwarcz, in addition to participants in the Duke Law School Junior Scholars Discussion Group, and the Duke Law School Summer Workshop Series. I thank Doo Hyun Nam and Z. Alex Xiao for valuable research assistance.

underway, she is both free from bankruptcy court supervision and without special bankruptcy court protection. Moreover, although a default rule, the early termination of the bankruptcy estate is sticky. Preserving property within the estate is possible, but the power to do so is limited. Some valid bankruptcy law purpose is necessary before property can be retained within the estate.

On a broader level, this Article attempts to situate the limited lifespan of the bankruptcy estate within a model of bankruptcy it dubs "light-touch" bankruptcy. This model emphasizes the advantages of simple, streamlined, and cheaply administrable procedures, and suggests that debtors may benefit most by being able to enjoy a financial fresh start, free from entanglement with the bankruptcy court, at the earliest possible moment during their bankruptcy cases.

INTRODUCTION

Outside of the world of big business, debt adjustment plans are Congress's favored form of bankruptcy law.[1] Congress has deployed both carrot and stick to encourage individual debtors to seek relief under chapter 13 of the Bankruptcy Code, preferring that debtors attempt to repay their debts over time rather than liquidate their existing assets.[2] As a result, hundreds of thousands of consumer debtors file for chapter 13 each year. Owners of family farms and fisheries take advantage of a similar invitation from Congress by seeking relief under chapter 12 of the Code. Congress has now taken its enthusiasm for debt adjustment plans one step further. In 2019, Congress responded to complaints that the traditional forms of business bankruptcy under chapter 11 of the Code are unworkable or prohibitively expensive for owners of small businesses by passing the Small Business Reorganization Act ("SBRA").[3] The SBRA makes debt adjustment plans available to businesses with less than $2.7 million in debt,[4] a category that may comprise more than 40% of all business debtors.[5]

The SBRA went into effect in February 2020; bankruptcy courts, therefore, are only just beginning to grapple with the applicable rules for such cases.[6] In all forms of debt adjustment bankruptcy, however, the basic mechanics of the bankruptcy case are the same. Instead of liquidating their assets, debtors keep all their pre-existing property and commit to paying their projected disposable income to their pre-bankruptcy creditors during a repayment plan that typically lasts from three to five years.[7] After making those payments, and with certain

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[1] The Bankruptcy Code describes chapters 13 and 12 of the Code as regulating the "adjustment of debts" of "an individual with regular income" and "a family farmer or fisherman with regular income" respectively. 11 U.S.C. §§ 101(18), (19A) (2019); *Id.* § 109(e). In this Article, I use the terms debt adjustment plan or debt adjustment bankruptcy to refer to a bankruptcy case filed under these chapters or under new subchapter V of chapter 11, each of which shares the same structure.

[2] Sara Sternberg Greene, Parina Patel & Katherine Porter, *Cracking the Code: An Empirical Analysis of Consumer Bankruptcy Outcomes*, 101 MINN. L. REV. 1031, 1031 (2017); H.R. REP. NO. 95-595, at 5, *as reprinted in* 1978 U.S.C.C.A.N. 5963, 5966 ("In the consumer area, proposed chapter 13 encourages more debtors to repay their debts over an extended period rather than to opt for straight bankruptcy liquidation and discharge"); *see* H.R. REP. NO. 109-31, at 12–13 (2005), *as reprinted in* 2005 U.S.C.C.A.N. 88, 99.

[3] Small Business Reorganization Act (SBRA) of 2019, Pub. L. No. 116-54, 133 Stat. 1079 (2019), (codified at 11 U.S.C. §§ 1181–1195).

[4] *Id.*; *see* 11 U.S.C. § 101(51D) (2019) (defining "small business debtor").

[5] Professor Robert Lawless estimates that approximately 40% of business debtors filing for bankruptcy under current law would qualify for relief under the SBRA. Robert Lawless, *How Many New Small Business Chapter 11s*, CREDIT SLIPS (Sept. 14, 2019), https://www.creditslips.org/creditslips/2019/09/how-many-new-small-business-chapter-11s.html. In 2019, 5,814 business bankruptcy cases were filed under traditional chapter 11, Table F-2, U.S. COURTS, https://www.uscourts.gov/sites/default/files/data_tables/bf_f2_1231.2019.pdf (last visited Feb. 19, 2019).

[6] SBRA § 5, 133 Stat. 1087.

[7] 11 U.S.C. § 1325(b) (2019) (defining projected disposable income as the debtor's projected gross

exceptions, the debtor's remaining liabilities that pre-date the bankruptcy case are discharged.[8] The statutory language in large part tracks from chapter to chapter of the Code. The pre-existing law of chapters 13 and 12, therefore, should tell us much about how small business reorganizations are to be administered.

Even if simple in concept, the law of debt adjustment plans is far from settled.[9] When all does not go according to plan, the hierarchy of rights among the bankruptcy case's stakeholders is unclear. That lack of clarity is particularly important given debtors' low rate of success in completing reorganization plans.[10] Individual debtors in as many as two-thirds of all chapter 13 cases fail to make all payments required by their plans and are forced either to dismiss their cases or convert to another form of bankruptcy relief (most likely simple liquidation under chapter 7 of the Code).[11] Similarly, about 60% of chapter 12 reorganizations do not result in a completed plan.[12] There are thousands of new small business cases expected each year. Once tensions arise in these cases, just as in the failed chapter 12 and 13 cases, the bankruptcy court must determine whose rights take precedence among three groups of parties to the case: the debtor herself; the debtor's pre-bankruptcy (or prepetition) creditors; and the debtor's new, postpetition creditors to whom she has incurred debts only after filing the bankruptcy case. Yet, the law on which bankruptcy courts must base these determinations is subject to bitter dispute.

Consider a debtor who has begun a debt adjustment bankruptcy and some months later wants to buy a truck. This may be a consumer debtor who wants to buy a truck for personal use or to drive to and from work, or a small business debtor who wants to use the truck in its business. In either case, the debtor expects to use some of her pre-bankruptcy savings to make the down payment for the truck and, thereafter, to use a portion of her income earned during the bankruptcy case to make monthly payments, while continuing to make her ongoing payments to prepetition creditors. May the debtor make these expenditures, or does the use of either pre-existing savings or current monthly income require the bankruptcy court's permission? And if the debtor's

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income less projected necessary or permitted expenses).

8 *Id.* § 1328

9 *See* David Gray Carlson, *The Chapter 13 Estate and Its Discontents*, 17 AM. BANKR. INST. L. REV. 233, 233 (2009) ("Thirty years into the life of the Bankruptcy Code, the courts still have no coherent theory of chapter 13.").

10 Greene, Patel & Porter, *supra* note 2, at 1032.

11 Greene, Patel & Porter, *supra* note 2, at 1032.

12 *See* Jamey Mavis Lowdermilk, *A Fighting Chance? Small Family Farmers and How Little We Know*, 86 TENN. L. REV. 177, 192 (2018).

prepetition creditors believe the deal is a bad one, may they object and be heard in the bankruptcy court?

Next, assume that the debtor has purchased the truck, but has fallen behind on his payments. May the auto lender repossess the truck from the debtor (as it would do if no bankruptcy case existed), or must the lender also obtain permission from the bankruptcy court? And does it matter whether taking the truck would interfere with the debtor's ability to make her continuing payments to prepetition creditors or to provide for her own needs?

The unanswered question is this: when a debtor has already finalized the details of her repayment plan and begins making payments to creditors, is the debtor fully in control of all of her other assets—meaning she is able to immediately enjoy the benefits and responsibilities of the fresh start—or does her property remain subject to bankruptcy court supervision and protection while she is making payments in accordance with her plan?

Although unresolved, this issue is fundamental to bankruptcy practice. District-by-district, debtors and creditors' rights are significantly altered as individual bankruptcy courts give effect to their own interpretations of the Code. In some districts, a debtor seeking to use her assets outside the ordinary course may be denied permission because of the potential impact that decision will have on future payments to prepetition creditors under the plan.[13] This approach ascribes paramount importance to protecting the debtor's financial health so that she is able to continue making payments under the plan to prepetition creditors and may shield the debtor's property from collection efforts by new postpetition creditors. Other courts take the opposite view, relying on the law of traditional business reorganizations under chapter 11. Debt adjustment plans are similar to reorganization proceedings in both governing statutory text and structure. In consequence, in a debt adjustment plan proceeding—as in a traditional chapter 11 reorganization—these bankruptcy courts hold that a debtor who has embarked upon a repayment plan is financially independent; she is able to deal with her assets as she chooses, but equally unable to look to the bankruptcy court for protection should some new creditor look to those assets for satisfaction.

The outcome that is chosen depends on the bankruptcy court's theory of the bankruptcy estate. When a case is filed, the Code provides that all of the debtor's property is subsumed into the bankruptcy estate—a fictitious legal entity that holds the debtor's property and places it under the bankruptcy court's

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[13] *See, e.g.*, *In re* Ward, 546 B.R. 667, 679 (Bankr. N.D. Tex. 2016).

authority.[14] But there is no consensus as to when that property leaves the estate. Four theories have been advanced, each reflecting substantially different understandings of how debt adjustment bankruptcy operates. This four-way circuit split has persisted for most of the Code's history.[15] The competing theories have primarily been developed in cases addressing debt adjustment plans of individuals under chapter 13, but the courts have found equal application in cases under chapter 12. Now that the bankruptcy courts will face these same questions once again when dealing with the restructuring of small businesses under the SBRA, this long-time legal puzzle should be resolved.

This Article attempts that task. It defends a simple view of the bankruptcy estate in debt adjustment cases known as the estate termination theory. Despite its simplicity, this theory is rarely adopted by courts. The estate termination theory holds that the bankruptcy estate is of limited lifespan. None of the debtor's property remains in the bankruptcy estate after the debtor's plan is confirmed. At least by default, the debtor's assets are both liberated and unprotected. Addressing an issue that has received less attention, this Article further argues that the estate termination theory is a sticky default rule. Otherwise stated, property may be retained in the bankruptcy estate post-confirmation only when the debtor has made a showing that this property is necessary to the fulfilment of the debt adjustment plan. This rule has been adopted by even fewer courts than have endorsed the basic estate termination theory, but this Article traces the rule's origins to brief and cryptic dicta in a Seventh Circuit decision from over twenty years ago.[16] Recently, the Seventh Circuit reiterated this conclusion in a trio of short decisions that, while forceful in their conclusions, are not especially illuminating in their reasoning.[17] This Article supplies the doctrinal underpinnings to support the court's conclusion.

Finally, this Article describes how limiting the lifespan of the estate in debt adjustment bankruptcies may be one way of implementing a model of "light-touch" bankruptcy. Under this model, Congress and bankruptcy courts should favor rules for debt adjustment bankruptcies that render them cheaper and simpler to administer. The broad intention is to minimize both the shadow of the

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14 11 U.S.C. § 541 (2019).

15 *See* Carlson, *supra* note 9, at 233.

16 *See generally In re* Heath, 115 F.3d 521, 522–23 (7th Cir. 1997) (Judge Posner suggesting that "[i]t would presumably be an abuse of discretion for the bankruptcy judge to confirm a plan that retained more of the property in the hands of the trustee than was reasonably necessary to fulfill the plan, though we need not decide that in this case..").

17 *See In re* Steenes, 918 F.3d 554, 557 (7th Cir. 2019) [hereinafter *Steenes I*]; *In re* Steenes, 942 F.3d 834, 839 (7th Cir. 2019) [hereinafter *Steenes II*]; *In re* Cherry, 963 F.3d 717, 720 (7th Cir. 2020).

bankruptcy proceeding over the debtor and the debtor's need to interact with the bankruptcy court during the bulk of the plan period. In addition to the potential for positive effects on access to bankruptcy, structuring debt adjustment bankruptcy along these lines reflects the reality that most debtors do not seek bankruptcy protection because of financial mismanagement or for strategic reasons. Those debtors should be able to realize the benefits of a financial fresh start and the resulting independence as quickly and completely as possible.

Part I of this Article sets forth the relevant statutory background. It gives most attention to chapter 13 of the Code because the vast majority of the cases discussing this issue have arisen under that chapter. It then explains that other debt adjustment bankruptcies arising under chapter 12 and the new small business bankruptcy provisions contain materially identical features. Part II discusses the four theories of the bankruptcy estate and explains that the estate termination theory both best reflects Congress's intent and best implements the policy goals of debt adjustment bankruptcy. Part III then explains why the default rule embodied in the estate termination theory is a sticky default rule. Part IV explains how early termination of the estate fits in with a broader theory of "light-touch" bankruptcy for consumers and small businesses.

I. THE DEBT ADJUSTMENT BANKRUPTCY BARGAIN

Congress has steadily expanded the availability of debt adjustment bankruptcies. Since February 2020, bankruptcy law has offered debt adjustment to three distinct categories of debtors. The oldest and by far the most widespread form of debt adjustment bankruptcy is chapter 13. Chapter 13 dates back to the enactment of the Code in 1978. It is available to individuals who earn regular income and have a total of less than approximately $1.7 million in secured and unsecured debt.[18] An individual whose debts arise from running an unincorporated business may file for chapter 13; the vast majority of chapter 13 cases, however, involve individual consumer debtors.

Congress next added chapter 12 to the Code. Chapter 12 has been available to family farmers and fishermen since 1986.[19] Chapter 12 cases, therefore, concern small businesses, albeit businesses of a specialized kind; the debtor may, as a technical matter, be either the business owner or the corporation or

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[18] The debt limits are $419,275 in noncontingent, liquidated unsecured debt and $1,257,850 in noncontingent liquidated secured debt. 11 U.S.C § 109(e) (2019). The debt limits are updated triennially. *Id.* § 104(a).

[19] *Id.* § 109(f).

partnership owned by the family farmer or fisherman.[20] Since February 2020, chapter 12 has been available to family farms with up to $10 million in debt.[21] Again, the chapter 12 debtor must earn regular income.[22]

The newest form of debt adjustment bankruptcy is for small business debtors. The Code defines a small business as a business with less than $2.7 million in noncontingent and liquidated debt.[23] Those businesses may take advantage of a new subchapter V added to chapter 11 of the Code.[24] Prior to February 2020, chapter 11 contained some special provisions applicable to small businesses, but those provisions did not disturb the central mechanics of traditional chapter 11, including most importantly, the absolute priority rule, or the rule that the business owner could not keep any value in the bankruptcy case until all of her creditors are paid in full.[25] Subchapter V now makes available a form of bankruptcy for such businesses modeled on chapter 12 of the Code—and by extension chapter 13—although one that includes a number of variations from its two progenitors.[26]

At heart, all three forms of debt adjustment bankruptcy share the same structure. That structure reflects a basic bargain between a debtor and her creditors. The debtor may retain both ownership and possession of all her property. That distinguishes debt adjustment bankruptcy from other forms of bankruptcy. In contrast, in a chapter 7 bankruptcy case non-exempt property is liquidated for the benefit of the debtor's creditors by a chapter 7 trustee, while in a traditional chapter 11 case, the value of shareholders' ownership rights in a reorganizing business may be used to repay the business's creditors.[27] In debt adjustment bankruptcy, in exchange for being able to keep her prepetition property, the debtor agrees to commit her projected disposable income pursuant to a court-approved plan over an up-to-five-year period towards paying back prepetition creditors.[28] Creditors recover more by virtue of these payments than

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20 *Id.* §§ 101(18), (19A).

21 *Id.* § 101(18). The debt limits for family fishermen are smaller. *Id.* § 101(19A).

22 *Id.* § 109(f).

23 *Id.* § 101(51D). This limit has been temporarily raised to $7.5 million by the CARES Act. *Id.* § 1182.

24 *See supra* text accompanying note 3.

25 *See* 11 U.S.C. § 1116.

26 *See* Paul W. Bonapfel, *A Guide to the Small Business Reorganization Act of 2019*, 93 AM. BANKR. L.J. 571, 575 (2019).

27 11 U.S.C. § 1306(b) ("Except as provided in a confirmed plan or order confirming a plan, the debtor shall remain in possession of all property of the estate."); *see also id.* §§ 1207(b), 1185(b) (same); *but see id.* § 704(a)(1) ("The trustee shall—collect and reduce to money the property of the estate for which such trustee serves . . . .").

28 *Id.* § 1322(a)(4); *see, e.g.*, Hamilton v. Lanning, 560 U.S. 505, 508 (2010).

if the debtor's property were liquidated.[29] If the debtor successfully completes all plan payments, she receives a discharge of most categories of debt provided for under the plan and thus exits bankruptcy keeping all of her property.[30]

A. *Debt Adjustment Under Chapter 13*

This section will explain the three core components of any debt adjustment bankruptcy—the bankruptcy estate, the automatic stay, and the plan of reorganization. The section begins with chapter 13 of the Code. Chapter 13 is the oldest of the three forms of debt adjustment bankruptcy and is overwhelmingly the most commonly resorted to by debtors.[31] Hundreds of thousands of debtors file chapter 13 petitions each year; at most a few hundred family farmers reorganize annually under chapter 12.[32] For that reason, the vast majority of decisions analyzing the lifespan of the bankruptcy estate arise out of chapter 13 cases. After discussing the estate, stay, and plan in the context of chapter 13, this section will show that each of these features is replicated in both chapter 12 of the Code and subchapter V of chapter 11.

1. *The Chapter 13 Estate and the Automatic Stay*

One essential feature of chapter 13 cases is the estate. The filing of a bankruptcy petition, whether under chapter 7 or chapter 13 of the Code, creates a bankruptcy estate.[33] The estate is a fictitious legal entity that takes title to the debtor's property and subjects it to bankruptcy court jurisdiction, supervision, and protection. In a chapter 7 case, the estate is composed of "all legal or equitable interests of the debtor in property as of the commencement of the case."[34] Those are the assets that the chapter 7 trustee may marshal and distribute to the debtor's prepetition creditors. In a chapter 7 case, therefore, the debtor turns over all of his property, except for property protected by a federal or state law exemption,[35] to the trustee at the time the bankruptcy petition is filed.[36] In a chapter 13 case, the estate comprises not only property the debtor owns "as of

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29 *See* 11 U.S.C. §§ 1325(a)(4), 1225(a)(4), 1191(a)–(b).

30 *Id.* §§ 1328, 1228, 1192.

31 Greene, Patel & Porter, *supra* note 2, at 1032.

32 *Id.*; Lowdermilk, *supra* note 12, at 179–80 n. 6 (collecting data).

33 11 U.S.C. §§ 541, 1306.

34 *Id.* § 541(a)(1).

35 *Id.* § 522(b)(1) (providing that "[n]otwithstanding section 541," an individual debtor may exempt certain property from the bankruptcy estate); *see also id.* § 522(d) (listing federal exemptions); *id.* § 522(b)(3) (incorporating state law exemptions).

36 *Id.* § 704(a)(1).

the commencement of the case,"[37] but also "all property . . . that the debtor acquires . . . before the case is closed, dismissed, or converted . . . whichever occurs first,"[38] and "earnings from services performed by the debtor after the commencement of the case, but before the case is closed, dismissed, or converted."[39] Unlike in chapter 7, however, the chapter 13 debtor remains in possession of all property of the estate,[40] and has limited rights to use and deal with that property.[41]

At the same time as the bankruptcy petition is filed and the estate is created, the automatic stay goes into effect.[42] The automatic stay "gives the debtor a breathing spell" from the collection efforts of prepetition creditors.[43] To serve that goal, the automatic stay prohibits, inter alia: "the commencement or continuation" of any "action or proceeding against the debtor that was or could have been commenced before the commencement of the case . . . or to recover a claim against the debtor that arose before the commencement of the case;"[44] the enforcement of a judgment obtained prepetition;[45] any act to create, perfect, or enforce a lien securing a prepetition claim;[46] and "any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case."[47]

The automatic stay plays a second critical role, preserving the bankruptcy estate so that assets remain available to be distributed to creditors or otherwise to be disposed of in accordance with bankruptcy principles.[48] The key provision through which this goal is implemented is section 362(a)(3) of the Code. That subsection prohibits "any act to obtain possession of property of the estate … or to exercise control over property of the estate;"[49] a companion subsection prohibits acts to create, perfect, or enforce a lien against property of the estate.[50] The most important effect of these subsections is to extend the automatic stay to

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37 *Id.* § 541(a)(1).
38 *Id.* § 1306(a)(1).
39 *Id.* § 1306(a)(2).
40 *Id.* § 1306(b).
41 *See In re* Seely, 492 B.R. 284, 290 (Bankr. C.D. Cal. 2013); *In re* Pisculli, 426 B.R. 52, 65–66 (E.D.N.Y. 2010); 8 COLLIER ON BANKRUPTCY ¶ 1303.02 (16th ed. 2020).
42 11 U.S.C. § 362(a).
43 *See* Kimbrell v. Brown, 651 F.3d 752, 755 (7th Cir. 2011).
44 11 U.S.C. § 362(a)(1).
45 *Id.* § 362(a)(2).
46 *Id.* § 362(a)(5).
47 *Id.* § 362(a)(6).
48 *See* 3 COLLIER ON BANKRUPTCY ¶ 362.03 (16th ed. 2020).
49 11 U.S.C. § 362(a)(3).
50 *Id.* § 362(a)(4).

a debtor's postpetition creditors. Prepetition creditors are already barred by the remaining provisions of section 362(a) from taking steps to collect on their claims. The stay of acts against the estate is treated somewhat differently by the Code than the remaining provisions of the automatic stay.[51] The Code provides that the stay, as created by these provisions, "continues until such property is no longer property of the estate. . . ."[52] The stay against other types of collection efforts continues until the case is closed or dismissed, or until the individual debtor receives a discharge.[53] A creditor may obtain relief from the automatic stay from the bankruptcy court for cause.[54] Nonetheless, the stay gives effect to a weighty bias in favor of preserving the status quo during bankruptcy cases, preventing creditors from disturbing that status quo without, at a minimum, subjecting their case for so doing to bankruptcy court scrutiny.[55]

Indeed, the protections of the automatic stay are remarkably comprehensive. They upend the way in which creditors deal with debtors. A landlord may be prohibited from taking steps to dispossess any tenant with an interest in the property they occupy—potentially even a tenant at sufferance or other occupant who, absent bankruptcy, could be evicted post-haste.[56] A municipal government whose ordinary practice is to impound the vehicles of residents who are delinquent on parking tickets will face sanctions if it knowingly boots the car of a chapter 13 debtor while the vehicle remains property of the estate.[57] The automatic stay is thus of enormous importance to prospective debtors. Because section 362(a)(3) of the Code ties the scope of the stay's protections, in part, to the extent of the bankruptcy estate, the reach of the chapter 13 estate itself is a question of great practical importance for chapter 13 debtors and their creditors.

Just as the Code protects the debtor by subjecting property subsumed into the bankruptcy estate to the automatic stay, it also constrains the debtor. Property of the estate is subject to the supervision of the bankruptcy court. The court must grant leave for any use or sale of estate property outside the ordinary course of business.[58] Section 1303 of the Code provides that, in chapter 13, the right to seek permission for such a use or sale of estate property belongs exclusively to

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51 *See id.* § 362(c)(1).
52 *Id.*
53 *Id.* § 362(c)(2).
54 *Id.* § 362(d)(1).
55 *See In re* Denby-Peterson, 941 F.3d 115, 126 (3d Cir. 2019).
56 *See* 3 COLLIER ON BANKRUPTCY ¶ 362.03[5] n. 46 and accompanying text (16th ed. 2020) (citing Convenient Food Mart v. Convenient Indus. Of Am., Inc., 968 F.2d 592, 594 (6th Cir. 1992); *In re* 48th Street Steakhouse, Inc., 835 F.2d 427, 430–31 (2d Cir. 1987)).
57 *See In re* Fisher, 198 B.R. 721, 722–23 (Bankr. N.D. Ill. 1996).
58 11 U.S.C. § 363; *see id.* § 1303.

the debtor and not to the chapter 13 trustee.[59] Nothing in chapter 13 explicitly authorizes most debtors to use property of the estate in the ordinary course to pay routine expenses,[60] but courts assume the debtor has that power.[61] At the beginning of the bankruptcy case all of the debtor's property is stripped from him and absorbed into the bankruptcy estate. Without the power to make ordinary course dispositions from the bankruptcy estate, the debtor would have no power to buy groceries, make rent, or pay other household expenses. Nonetheless, bankruptcy courts guard property of the estate, and may impose sanctions on debtors who too freely dispose of estate assets.[62]

The chapter 13 estate is vital in one more respect: the boundaries of the estate play a key role in determining the extent of bankruptcy court jurisdiction. Bankruptcy courts have jurisdiction over proceedings "arising under title 11, or arising in or related to cases under title 11."[63] The first two bases for jurisdiction involve different types of proceedings with some special relationship to bankruptcy.[64] The third, and broadest, basis for bankruptcy jurisdiction is "related to" jurisdiction. "An action is related to bankruptcy if the outcome could alter the debtor's rights, liabilities, options, or freedom of action (either positively or negatively)[,] and which in any way impacts upon the handling and administration of the bankrupt estate."[65] Whether an asset remains within the bankruptcy estate therefore largely determines whether the bankruptcy court may exercise jurisdiction over disputes regarding that asset.[66] Finally, while

59 *Id.* § 1303.

60 For business debtors in both chapter 11 and chapter 13, section 363(c) of the Code authorizes the trustee or debtor in possession to enter into transactions and use property of the estate in the ordinary course of business without court permission. Section 1304 grants the section 363(c) power to a chapter 13 debtor "engaged in business." *Id.* § 1304(b). There is thus a plausible negative inference that a non-commercial debtor does not have such powers—or at least, that the chapter 13 debtor cannot exercise them exclusively, independent of the trustee. There is no equivalent in chapter 13 of section 1107 of the Code, which provides a blanket authorization to the chapter 11 debtor to operate its business. *Id.* § 1107(a).

61 *E.g.*, *In re* Seely, 492 B.R. 284, 290 (Bankr. C.D. Cal. 2013); *In re* Pisculli, 426 B.R. 52, 66 (E.D.N.Y. 2010) (debtor may use estate property for "ordinary and necessary living expenses, provided such use is not in bad faith"); *see* 8 COLLIER ON BANKRUPTCY ¶ 1303.02 (16th ed. 2020).

62 *See, e.g.*, *In re Pisculli*, 426 B.R. at 59–66; *In re* Fatsis, 405 B.R. 1, 10–11 (B.A.P. 1st Cir. 2009).

63 28 U.S.C.A. § 1334(b); *see id.* § 157.

64 So-called "arising under" jurisdiction extends to rights created by the Code itself. *See* CoreStates Bank, N.A. v. Huls Am., Inc., 176 F.3d 187, 195 n.6, 196 (3d Cir. 1999); *In re* Wilshire Courtyard, 729 F.3d 1279, 1285 (9th Cir. 2013). "Arising in" jurisdiction extends to proceedings that "would have no existence outside of a bankruptcy case." *In re Wilshire*, 729 F.3d at 1285; *see In re* Marcus Hook Dev. Park, Inc., 943 F.2d 261, 267 (3d Cir. 1991).

65 Pacor Inc. v. Higgins, 743 F.2d 984, 994 (3d Cir. 1984).

66 *See In re* Fietz, 852 F.2d 455, 456–59 (9th Cir. 1988). In *Fietz*, Dale and Gloria, a former husband and wife held claims against the same defendant. *Id.* at 456. Gloria claimed that California's community property doctrine meant that both were swept into the estate created when Dale filed a chapter 13 bankruptcy case. *Id.* at 458. Gloria sought to assert her claim as a crossclaim in litigation before the bankruptcy court. *Id.* at 456. The

bankruptcy courts frequently exercise concurrent jurisdiction with other courts, the Judiciary Code provides that the bankruptcy forum has exclusive jurisdiction over property of the estate.[67]

2. *The Chapter 13 Plan*

The most significant feature of every chapter 13 case is the plan. Promptly after the initiation of a chapter 13 bankruptcy case, the debtor is required to file a plan.[68] Generally, a debtor is required to commit all of her projected disposable income to funding the plan, typically for a period of three to five years.[69] The plan must pay creditors at least as much as they would have received in a liquidation.[70] Where form chapter 13 plans are available, the plan proposed by the debtor must use the prescribed form.[71] The bankruptcy court will confirm the plan if it meets all of the requirements set forth in the Code.[72] The chapter 13 trustee distributes all funds received from the debtor to the creditors according to the terms of the confirmed plan.[73] Absent special circumstances, and excluding administrative expenses (which, in a chapter 13 case, typically comprise the debtor's attorneys' fees) only prepetition debts are included within a chapter 13 plan.[74] Postpetition creditors do not, therefore, as a general matter, receive distributions from the chapter 13 trustee.[75]

Ninth Circuit found, however, that Gloria's claim had passed out of the bankruptcy estate in Dale's chapter 13 bankruptcy case upon confirmation of the plan. *Id.* at 458. For that reason, although the bankruptcy court could decide Dale's claim, it was unable to exercise jurisdiction over Gloria's claim, and was required—notwithstanding Gloria's apparent preference for resolution of her claim in the bankruptcy court alongside Dale's—to grant a motion to dismiss that claim. *Id.* at 458–59.

67 28 U.S.C.A. § 1334(e)(1)–(2).

68 11 U.S.C. § 1321 (2019); FED. R. BANKR. P. 3015(b) ("If a plan is not filed with the petition, it shall be filed within 14 days thereafter.").

69 11 U.S.C. §§ 1322(a)(1), 1325(b)(1)(B).

70 *Id.* § 1325(a)(4).

71 FED. R. BANKR. P. 3015(c), 3015.1.

72 11 U.S.C. § 1325(a)(1).

73 *Id.* § 1326(c).

74 *Id.* § 1322(a)(4) (plan may provide for payments of unsecured claims); *id.* § 501(a) (creditor may file proof of claim); *id.* § 101(10)(A) ("creditor" means entity that has a claim against the debtor arising at the time of or before filing of the bankruptcy case); *but see id.* § 1305 (limited circumstances under which postpetition creditors may file proof of claim); *id.* § 1322(a)(6) (plan may provide for payments of proofs of claim filed pursuant to § 1305). Some chapter 13 plans also provide for "conduit payment" of the debtor's ongoing monthly mortgage payments by chapter 13 trustee. AM. BANKR. INST., FINAL REPORT OF THE ABI COMMISSION ON CONSUMER BANKRUPTCY 184–88 (2019).

75 The Bankruptcy Court for the Western District of Pennsylvania described why that must be the case:

> Prepetition creditors are bound by the provisions of a confirmed plan whether or not the claim of such creditor is provided by the plan and whether or not such creditor has objected to, accepted or rejected the plan . . . . In sharp contrast, postpetition creditors cannot be forced to participate

Confirmation of a chapter 13 plan decisively reorders the debtor's legal relationships. The debtor and every creditor are bound by the terms of the confirmed plan.[76] In effect, the plan is a contract between the debtor and his prepetition creditors.[77] The plan is also a final judgment of the bankruptcy court.[78] The res judicata effect of a confirmed plan ensures that the "balance of interests" struck at confirmation persists thereafter.[79]

In addition to the relationships between debtor and creditors, the plan impacts the chapter 13 estate. Section 1327(b) of the Code provides that "[e]xcept as provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor."[80] A companion provision, section 1322(b)(9), instructs that the chapter 13 plan proposed by the debtor shall "provide for the vesting of property of the estate, on confirmation of the plan or at a later time, in the debtor or in any other entity."[81] The precise meaning of those provisions, as the next section will discuss, has perplexed the courts for many years. The best and simplest explanation is that the Code contemplates that the debtor will regain title to all of her property from the bankruptcy estate after confirmation—of course, the debtor is still required to make plan payments out of future income to the trustee to satisfy creditors' claims.

Following confirmation, the plan may be modified at the request of the debtor, the trustee, or an unsecured creditor because plan payments are calculated based on a debtor's projected disposable income and changed circumstances may necessitate an adjustment of payment amounts.[82] If the debtor completes the plan, she receives a discharge.[83]

> in a Chapter 13 plan, although they may elect to do so voluntarily [under section 1305].

In re Weisel, 400 B.R. 457, 472 (Bankr. W.D. Pa. 2009).

[76] *Id.* § 1327(a).

[77] *See In re* Murphy, 474 F.3d 143, 148 (4th Cir. 2007) ("A confirmed Chapter 13 plan is 'a new and binding contract, sanctioned by the court, between the debtors and their pre-confirmation creditor[s].'") (quoting *In re* Penrod, 169 B.R. 910, 916 (Bankr. N.D. Ind. 1994)); *In re* Harvey, 213 F.3d 318, 321 (7th Cir. 2000); *In re* Oparaji, 698 F.3d 231, 238 (5th Cir. 2012) (a chapter 13 plan is an "exchanged for bargain between the debtor and the debtor's creditors"); *In re* Forte, 341 B.R. 859, 869–70 (Bankr. N.D. Ill. 2005) (discussing "contract between a debtor and creditors formed by confirmation of the chapter 13 plan.").

[78] United Student Aid Funds, Inc. v. Espinosa, 559 U.S. 260, 269 (2010).

[79] *In re Harvey*, 213 F.3d at 321.

[80] 11 U.S.C. § 1327(b).

[81] *Id.* § 1322(b)(9).

[82] *Id.* § 1325(b).

[83] *Id.* § 1328.

Chapter 13 provides meaningful benefits to debtors by providing opportunities for them to keep their houses, cars, or other valuable prepetition assets that might be subject to liquidation in a chapter 7 case.[84] The Supreme Court has explained this basic bargain:

> Proceedings under Chapter 13 can benefit debtors and creditors alike. Debtors are allowed to retain their assets, commonly their home or car. And creditors, entitled to a Chapter 13 debtor's "disposable" postpetition income, § 1325(b)(1), usually collect more under a Chapter 13 plan than they would have received under a Chapter 7 liquidation.[85]

But chapter 13 remains entirely voluntary.[86] A chapter 13 debtor possesses a non-waivable right to convert a bankruptcy case to chapter 7 at any time (assuming eligibility to be a chapter 7 debtor)[87] or to dismiss the bankruptcy case outright.[88] Other parties in interest may also move for conversion or dismissal of the bankruptcy case for cause, including the chapter 13 trustee, if the debtor defaults on her obligations under the plan.[89]

B. *The Debt Adjustment Bargain for Businesses*

Chapter 12 and subchapter V both share key features of chapter 13. The bankruptcy estate subsumes all the debtor's property, both prepetition and postpetition.[90] The same provisions of the automatic stay apply to provide the debtor personally with comprehensive protection against any attempt to collect a prepetition debt. But this only protects property of the estate, and not the debtor herself, from interference by postpetition creditors or others.

Similarly, the decisive legal moment in both a chapter 12 case and a small business subchapter V case is the confirmation of the plan. The plan binds all parties to the case.[91] As in chapter 13, confirmation of the plan vests all property of the estate in the debtor.[92] The plan, and indeed the plan confirmation process, may look somewhat different from chapter to chapter. Chapter 13 cases involve off-the-shelf plans presented to the bankruptcy court on pre-approved forms, and

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84 *See* Harris v. Viegelahn, 135 S. Ct. 1829, 1835 (2015).
85 *Id.*
86 *See id.*
87 11 U.S.C. § 1307(a), (g).
88 *Id.* § 1307(b).
89 *Id.* § 1307(c).
90 *Id.* §§ 1207(a), 1186(a). Section 1186 differs from sections 1306(a) and 1207 in one key respect, detailed later in this Article. *See infra* Part II.B.
91 11 U.S.C. § 1227(a).
92 *Id.* §§ 1227(b), 1141(d).

it appears that plans under subchapter V will follow this pattern,[93] while a chapter 12 plan may be individually drafted and include more bespoke provisions. Chapter 13 and 12 plans are always subject to streamlined procedures; creditors do not vote on confirmation of the plan, but merely have the right to object if they believe some provision of the plan to be unlawful or that the plan as a whole is not feasible.[94] Subchapter V contemplates that creditors will vote on plans, but provides that a plan may be confirmed without creditor approval if it meets the statutory requirements.[95]

In structure, however, plans remain—in respects material to this analysis—the same under all three types of debt adjustment bankruptcy. The chapter 12 and subchapter V debtor, like the chapter 13 debtor, commit their projected disposable income to the repayment of creditors. Because the debtor in these cases is a business, projected disposable income is defined as any income "not reasonably necessary to be expended . . . for the payment of expenditures necessary for the continuation, preservation, or operation of the business of the debtor."[96] The plan may last no longer than five years, but must pay creditors at least as much as they would have received in a liquidation of the debtor's prepetition property.[97] Just as in chapter 13, from the beginning of the case, the debtor remains in possession of estate property and, at least initially, must secure court permission to deal with that property outside of the ordinary course of business.[98] As in chapter 13, it is unresolved whether this court oversight continues after the debtor's plan is confirmed and payments are in progress, or whether instead the debtor has the right to deal with that property freely.

II. THE LIFESPAN OF THE BANKRUPTCY ESTATE

In each of these variants of the debt adjustment bankruptcy model, courts must determine the fate of the bankruptcy estate upon confirmation of a plan. Current law is fractured. That is the case even though no such dispute exists in other types of bankruptcy cases. This Section will explain the dispute over the lifespan of the bankruptcy estate in debt adjustment cases. Once again, it will begin with chapter 13 of the Code, before returning to look at the same dispute

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[93] A standard form plan has been approved for use in subchapter V cases. U.S. COURTS, B 425A, PLAN OF REORGANIZATION FOR SMALL BUSINESSES UNDER CHAPTER 11 (2020), https://www.uscourts.gov/forms/small-business-forms/plan-reorganization-small-business-under-chapter-11.

[94] 11 U.S.C. §§ 1325, 1225.

[95] *See id.* § 1191.

[96] *Id.* § 1191(d); *see id.* § 1225(b)(2)(B) (same).

[97] *Id.* §§ 1129(a)(7), 1191, 1222, 1225.

[98] *Id.* §§ 1186(b), 1207(b); *see id.* 363(b).

in the context of chapter 12 and subchapter V of chapter 11. At its root, the question of the lifespan of the bankruptcy estate is one of statutory interpretation, and accordingly that is the primary focus of this Section. For that reason, it is perhaps helpful at the outset to say a few words on the vexed question of statutory interpretation in bankruptcy. Bankruptcy is, to some extent, its own world. Bankruptcy courts are well-known for preferring purposivist interpretations of the Code, and indeed, for creative decision-making that departs from the underlying statutory text entirely.[99] In effect, a popular narrative runs, bankruptcy courts update the Code in real time, allowing for innovations that facilitate efficient and successful reorganizations but that Congress can scarcely be said to have intended or provided for in its original 1978 enactment.[100] While purposivist interpretation has far from disappeared in the higher courts,[101] the focus on the statutory text, particularly in the Supreme Court, has become increasingly prominent.[102] Although a simplification, it is not wholly unfair to characterize the key dynamic of bankruptcy litigation as a push-pull between the creative policy-driven rulings of the bankruptcy courts and the cold shock of textualism that douses those courts in those rare cases in which a bankruptcy dispute reaches the summit of the legal system.[103]

This Article does not fully embrace either approach. It more closely aligns itself with a group of the Supreme Court's recent bankruptcy decisions that, although they may certainly be characterized as textualist decisions, are focused on a structural approach to the Code.[104] These decisions focus on the way the

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[99] *See generally* Adam J. Levitin, *Toward a Federal Common Law of Bankruptcy: Judicial Lawmaking in a Statutory Regime*, 80 AM. BANKR. L.J. 1, 1–5 (2006) (discussing the debate over purposivism and textualism in the bankruptcy context).

[100] *Id.* at 1–2 (listing "common[] if contested" practices which, lacking specific statutory authorization, bankruptcy courts have relied on equitable powers to approve).

[101] *See generally* Anita S. Krishnakumar, *Backdoor Purposivism*, 69 DUKE L.J. 1275, 1275–78 (2020) (challenging the narrative that "purposivism is dead or dying"); Judge Diarmuid F. O'Scannlain, *"We Are All Textualists Now": The Legacy of Justice Antonin Scalia*, 91 ST. JOHN'S L. REV. 303, 304–06 (2017) (detailing Justice Kagan's speech on Justice Scalia and his influence on the adoption of textualism by federal jurists).

[102] Krishnakumar, *supra* note 101, at 1277–78.

[103] The most forceful endorsement of textualism in a recent Supreme Court bankruptcy case was in *Siegel*, in which the Supreme Court admonished the bankruptcy court for exercising its broad statutory and inherent powers, and further held that it "may not contravene specific statutory provisions". Law v. Siegel, 571 U.S. 415, 421 (2014); *see also* Schwab v. Reilly, 560 U.S. 770, 778 (2010) ("We conclude that the Court of Appeals' approach fails to account for the text of the relevant Code provisions and misinterprets our decision in Taylor"); *but see* Marrama v. Citizens Bank of Mass., 549 U.S. 365, 375–76 (2007).

[104] *See, e.g.*, Mission Product Holdings, Inc. v. Tempnology, LLC, 139 S. Ct. 1652 (2019); Czyzewski v. Jevic Holding Corp., 137 S. Ct. 973 (2017); *and* RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 566 U.S. 639 (2012); *cf.* George H. Taylor, *Structural Textualism*, 75 B.U. L. REV. 321, 347–50 (1995) (describing a "holistic" approach to interpretation that "derives from examination of the statute's overall structure" and arguing that "[t]he structural approach is also textualist").

different provisions of the Code fit together, such that the resulting decision gives effect to a statutory scheme that makes sense of the Code as a whole. In each case, the Court takes the text of the statute seriously. But it also assumes that Congress, in enacting the Code, "ha[d] a rational plan, that statutes are meant to *work*,"[105] and thus, that understanding the Code means understanding the theories based on which it hangs together. So too does this Article. Presented in this Article is a theory of the bankruptcy estate in debt adjustment bankruptcy cases that I believe fits more neatly with the statutory text than any other proposed theory. Beyond that, however, this Article also presents a broader theory of how Congress intended debt adjustment bankruptcy to operate and identifies how the individual components of each debt adjustment bankruptcy case fit together to make a sensible whole.

A. The Life of the Chapter 13 Estate

That courts dispute the fate of the bankruptcy estate in chapter 13 cases might seem surprising. After all, bankruptcy courts have easily been able to reach consensus on the lifespan of the estate elsewhere. In chapter 7, any estate property is liquidated and distributed to creditors (or, if of inconsequential value, abandoned back to the debtor), after which the estate ceases to exist.[106] In the chapter 11 context, although the statute does not expressly say so, courts agree that plan confirmation presumptively terminates the estate.[107] In fact, chapter 11 specifies, in language that exactly parallels one of the provisions of chapter 13, that "[e]xcept as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all property of the estate in the debtor."[108] That provision is universally understood to mean that upon confirmation the bankruptcy estate ceases to exist, property may no longer enter it, and the property in the estate is either distributed to creditors under the plan or revested in the debtor.[109] In other words, the fate of the bankruptcy estate in chapter 7 and in traditional chapter 11 is uncontroversial.[110]

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105 *See* Abbe R. Gluck, *Imperfect Statutes, Imperfect Courts: Understanding Congress's Plan in the Era of Unorthodox Lawmaking*, 129 HARV. L. REV. 62, 91 (2015).

106 *See* 11 U.S.C. § 727(b) (2019) (describing the effect of discharge).

107 *See, e.g.*, *In re* Hillis Motors, 997 F.2d 581, 587 (9th Cir. 1993); *In re* Resorts Int'l, Inc., 372 F.3d 154, 164–65 (3d Cir. 2004) (chapter 11 estate ceases to exist upon confirmation).

108 11 U.S.C. § 1141(b).

109 *See In re Resorts Int'l*, 372 F.3d at 164–165; *In re Hillis Motors*, 997 F.2d at 587 (pursuant to section 1141(b), "confirmation usually terminates the existence of the estate").

110 That does not mean that the business of bankruptcy is entirely done in chapter 11 cases upon confirmation. Sometimes assets may be transferred to a liquidating trust, so a trustee can continue the business of reducing them to cash in order to pay creditors even after the bankruptcy process itself is formally over. But it is the trust instruments, rather than the law of bankruptcy or the bankruptcy estate, that prescribes the trustee's

The same cannot be said for the fate of the bankruptcy estate in chapter 13. Rather, four theories have been advanced, each largely predicated on its own distinct understanding of the basic logic of chapter 13, and each presenting radically different consequences for the debtor, creditors, and the bankruptcy court during the post-confirmation period. In brief introduction, I will defend the estate termination theory: the notion that chapter 13 works exactly as in chapter 11. At plan confirmation, all property in the chapter 13 estate is transferred absolutely to the chapter 13 debtor and the estate terminates. Its polar opposite is the estate preservation theory, which states that no property is actually transferred out of the bankruptcy estate until the very end of the case. One intermediate approach is the estate reconciliation theory, which states that all property of the estate vests in the debtor at plan confirmation. Rather than terminating at plan confirmation, however, the estate continues to exist and is refilled with any property the debtor acquires thereafter, including all of the debtor's post-confirmation wages. Finally, the estate transformation theory, a similar intermediate approach, states that all property of the estate is transferred to the debtor at plan confirmation except for property that is necessary to the fulfilment of the chapter 13 plan.

Professor David Gray Carlson forcefully critiqued the estate preservation and estate reconciliation theories.[111] Carlson demonstrated how both theories do substantial violence to the language of the Code, and both fail as a matter of bankruptcy policy. Carlson defended a narrow version of the estate transformation approach, in which the estate is largely terminated at plan confirmation but continues to have authority over property that is actually paid by the chapter 13 debtor to the trustee pursuant to the plan. I am largely in agreement with Carlson's criticisms of the estate preservation and estate reconciliation theories, but I posit that Carlson does not go far enough. The simplest and most elegant theory of the chapter 13 estate is that it terminates in its entirety upon confirmation of the plan, absent some specific contrary court order. After reviewing the most substantial flaws in the estate preservation and estate reconciliation theories, this Section explains why the estate termination theory is preferable to the limited estate transformation theory proposed by Carlson.

actions in such a case. *See infra* note 167 and accompanying text. The question, therefore, is whether the post-confirmation world in chapter 13 looks similar—with a debtor's continuing obligations governed not by bankruptcy law itself, but by non-bankruptcy principles according to some agreement hashed out during the bankruptcy case—or whether in chapter 13 the bankruptcy case itself, and the remit of bankruptcy law proper, in continues onward following confirmation.

[111] *See* Carlson, *supra* note 9, at 233–44.

1. *Estate Preservation*

The stakes are perhaps best illustrated by beginning with the most expansive theory of the chapter 13 estate—the so-called "estate preservation theory." This theory states that the chapter 13 estate survives plan confirmation and continues in full effect until the conclusion of the chapter 13 case, whether that means the completion of the debtor's chapter 13 plan payments followed by entry of a discharge, dismissal of the case, or conversion to chapter 7. Throughout that entire period, all of the debtor's property remains property of the chapter 13 estate, regardless of whether acquired before the bankruptcy petition was filed, during the pre-confirmation period, or after confirmation of the plan.

Section 362(a)(3) of the Code prohibits creditors from exercising control over property of the estate.[112] Therefore, under the estate preservation theory, all of the debtor's property is subject to the protection of the automatic stay not only vis-à-vis prepetition creditors provided for under the plan, but also against postpetition creditors for the entire up-to-five year period of the bankruptcy case. Even if the debtor fails to pay postpetition obligations as they become due, postpetition creditors may not look to estate property unless they first appear in the bankruptcy case and file a motion seeking permission to do so from the bankruptcy court.[113] The debtor is constrained from freely dealing with the property; at a minimum, he must seek court approval for any disposition of the property outside of the ordinary course of business.[114] The property may generate administrative expenses throughout that same period, entitled to priority payment.[115] And disputes regarding that property, at least in the first instance, are decided by the bankruptcy court.[116]

Forcing creditors to go to the bankruptcy court post-confirmation is opposite to what is required in a traditional chapter 11 case. Following confirmation, under the ordinary rules of chapter 11 the bankruptcy estate "ceases to exist"[117]

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112 11 U.S.C. § 362(a)(3) (2019).

113 Precisely this question was at issue in the litigation giving rise to the Seventh Circuit's decision in *Steenes I*, 918 F.3d 554 (7th Cir. 2019). The debtors in that case took the position that the Bankruptcy Code enabled them to postpone making any payments towards any parking tickets they were issued after the date of filing of the bankruptcy case until completion of the chapter 13 plan; the City of Chicago, in the meantime, could not take its ordinary steps to respond to non-payment of tickets—ordinarily, immobilizing and impounding the debtors' vehicles—without first securing an order granting relief from stay from the bankruptcy court. *Id.* at 557–58.

114 11 U.S.C. § 363(b)(1).

115 *Id.* § 503(b)(1)(A) (providing that "the actual, necessary costs and expenses of preserving the estate" may be entitled to administrative expense status.); *cf. Steenes II*, 942 F.3d 834, 836 (7th Cir. 2019).

116 *See supra* notes 63–67 and accompanying text.

117 *In re* Resort's Int'l, Inc., 372 F.3d 156, 165 (3d Cir. 2004).

absent a specific order from the bankruptcy court that preserves the estate for a limited purpose.[118] The estate preservation theory argues that chapter 13 must differ from traditional chapter 11 in order to remain faithful to the text of the Code, particularly section 1306. That provision states that "[p]roperty of the estate includes . . . earnings from services performed by the debtor after commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7, 11, or 12 of this title, whichever occurs first."[119]

The apparent breadth of section 1306 has led some bankruptcy courts to conclude that throughout the bankruptcy case the chapter 13 estate must persist in its original form as a repository for all of the debtor's property. As one bankruptcy court observed:

> the clear language of § 1306 demonstrates that *confirmation* of a Chapter 13 plan is not relevant to determining whether property is or is not property of the estate. The relevant events in this determination are commencement of the case and either dismissal, closing or conversion of the case. If Congress had intended for confirmation to so drastically affect the expansive definition of property of the estate found in § 1306, it knew how to draft such a provision.[120]

Such an interpretation of the Code is hard to square with section 1327's direction that property of the estate "vests" in the debtor.[121] Courts adopting the estate preservation theory generally acknowledge that the ordinary meaning of "vesting" of estate property in the debtor is to transfer that property to the debtor and thus out of the bankruptcy estate.[122] But they conclude that "vest" must mean something else in the context of chapter 13.[123] "Vesting" is thus argued to mean a "fixing of rights" to property rather than a "transfer" of that property to the debtor.[124] Thus, as viewed by some courts, the debtor is vested with property of the estate after plan confirmation because he then acquires "authority . . . to propose a sale or encumbrance of estate property. . . ."[125] In the view of other

118 *See, e.g.*, *In re* Neptune World Wide Moving, Inc., 111 B.R. 457, 462–63 (Bankr. S.D.N.Y. 1990).

119 11 U.S.C. § 1306(b).

120 *In re* Aneiro, 72 B.R. 424, 429 (Bankr. S.D. Cal. 1987).

121 11 U.S.C. § 1327(b)

122 *In re* Fisher, 198 B.R. 721, 733 (Bankr. N.D. Ill. 1996), *rev'd*, 203 B.R. 958 (N.D. Ill. 1997); *see* Security Bank of Marshalltown, Iowa v. Neiman, 1 F.3d 687, 691 (8th Cir. 1993) (acknowledging that the effect of plan confirmation in chapter 11 cases is to "vest" all property of the estate, transforming such property into property of the debtor).

123 *Neiman*, 1 F.3d at 691 ("We think that the opposing line of cases is 'premised upon the mistaken belief that revesting under § 1327(b) transforms property of the estate into property of the debtor.'") (quoting *In re Aneiro*, 72 B.R. at 428–29).

124 *In re Fisher*, 198 B.R. at 733.

125 *Id.*

courts, the debtor is vested with property of the estate after plan confirmation because the debtor is then acquires "the right to future of enjoyment of the assets in that estate" "once he faithfully completes his obligations under the plan and is entitled to the discharge."[126] In either case, the estate, however, remains intact after confirmation.[127]

Although the chief argument in favor of the estate preservation theory is that it is textually preferable, giving "full effect" to section 1306, bankruptcy courts have also advanced policy arguments in favor of a long-lived chapter 13 estate.[128] Fundamental to the position of those courts is the right of the chapter 13 debtor to convert his bankruptcy case to chapter 7.[129] When a debtor converts his bankruptcy case from chapter 13 to chapter 7, he agrees to permit liquidation of his property rather than continuing to repay his creditors over time from future income; property of the estate in the converted chapter 7 case consists of property, "as of the date of the filing of the petition, that remains in the possession of or is under the control of the debtor on the date of conversion."[130] Nothing in the text of the Code, therefore, requires there to be an estate in existence at the time of conversion to provide assets for the chapter 7 trustee to liquidate.[131] Property that the debtor owned at the time of the original filing of his chapter 13 bankruptcy case becomes property of the estate in the converted chapter 7 case regardless of whether the chapter 13 estate exists at the time of conversion. But, because dispositions of estate property outside the ordinary

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[126] Woodard v. Taco Bueno Restaurants, Inc., 2006 WL 3542693, at *26 (N.D. Tex. Dec. 8, 2006). The Bankruptcy Court for the District of New Jersey subscribes to a similar view:

> At confirmation, the "vesting" of property of the estate in the debtor, as provided in § 1327(b), means that the debtor's rights and interest in the property become fixed as of the confirmation of the plan, and are effected when the provisions of the debtor's Chapter 13 plan are satisfied. . . . The act of confirmation 'vests' all of the property of the estate in the debtor to allow the debtor to take the necessary steps to comply with the confirmed plan. The statute does not state that the event of confirmation changes the characterization of the property from property of the estate into property of the debtor. Instead, it merely confirms the debtor's ability to utilize property of the estate, notwithstanding that designation, in satisfaction of the debtor's obligations under the confirmed plan.

In re Tarby, 2012 WL 1390201, at *4 (Bankr. D.N.J. Apr. 20, 2012) (internal citations omitted).

[127] *See In re Fisher*, 198 B.R. at 733.

[128] *Id.* at 727–31.

[129] *See, e.g.*, *id.* at 731.

[130] 11 U.S.C. § 348(f)(1)(A) (2019).

[131] In a case of bad faith conversion from chapter 13 to chapter 7, the Bankruptcy Code *does* provide that property of the estate in the new chapter 7 case shall comprise whatever property existed in the chapter 13 estate at the time of conversion. *Id.* § 348(f)(2). As will be discussed below, this provision does cause some difficulties for the estate termination theory which this Article defends. *See infra* note 177 and accompanying text. The rarity of post-confirmation bad faith conversions from chapter 13 to chapter 7, and the availability of other remedies to address such bad faith when it occurs, help to alleviate these problems.

course require the bankruptcy court's approval pursuant to section 363 of the Code,[132] keeping property within the estate after conversion prevents the debtor from dissipating it while his chapter 13 case remains ongoing.[133] "[B]ecause of the continuing right of the debtor to convert a Chapter 13 case after plan confirmation, the role of the estate as a reserve source of creditor payments continues after confirmation . . . the estate itself must continue, subject to the protections of the Code, undiminished by the confirmation."[134]

Carlson's article comprehensively sets forth reasons for rejecting the estate preservation theory.[135] Most importantly, the estate preservation theory seems too implausible as a textual matter to pass muster. Describing the vesting of property of the estate as merely conferring upon the debtor a right to possession of such property, or to make dispositions of that property subject to bankruptcy court approval, does not give adequate meaning to the statutory language. The debtor already has each of those rights during the pre-confirmation period.[136] Section 1306(b) confirms the debtor's right to remain in possession of property of the estate at that time, and nothing in sections 363(b) or 1303 indicates that the right of a debtor to propose dispositions of property of the estate is one that comes into effect only after plan confirmation.[137] Moreover, the narrow reading of "vest" proposed by advocates of the estate preservation theory is entirely inconsistent with what that term is universally understood to mean when used elsewhere in the Code.[138] In short, "'vesting' is a clumsy way of saying 'transferring absolutely.' Otherwise, 'vesting' means nothing at all."[139]

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132 *See supra* note 13 and accompanying text.

133 The *Fisher* bankruptcy court recited the consequences that would follow from permitting an "emancipated" chapter 13 debtor post-confirmation to "treat property of the estate as if no bankruptcy had ever occurred." *In re Fisher*, 198 B.R. at 731. If that were the case,

> after confirmation, a Chapter 13 debtor could (1) sell any unencumbered assets, (2) expend funds outside the ordinary course, (3) incur any kind of credit, including credit secured by unencumbered assets, and (4) pay legal fees to bankruptcy counsel—all without notice to any party involved in the bankruptcy and with no opportunity for a court hearing. If the debtor were operating a business, there would be no need to report on its operation. And finally, postpetition creditors, like the City of Chicago in the present case, would be free to enforce claims against the debtor's property, again without any notice to parties involved in the bankruptcy.

Id.

134 *Id.* at 732.

135 Carlson, *supra* note 9, at 240–42.

136 *See supra* notes 58–62.

137 Carlson, *supra* note 9, at 241.

138 Carlson, *supra* note 9, at 242.

139 Carlson, *supra* note 9, at 242.

Nor is preserving the chapter 13 estate for the benefit of creditors in a future chapter 7 case sound policy. Such an approach is inconsistent with the fresh start—one of the most basic policies animating bankruptcy law—and the chapter 13 bargain. The chapter 13 debtor promises to devote all of his future disposable income to repayment of creditors in exchange for the right to retain the property he owns at the time he files for relief.[140] But under the estate preservation theory, he does not really "keep" that property. Instead, all of his property is subject to a five-year guardianship overseen by the bankruptcy court, not because such oversight is necessary to serve the purposes of his chapter 13 case, but as a safeguard in case he chooses to abandon chapter 13 and resort to chapter 7. Such oversight serves only to safeguard creditors against the substantially more remote possibility of a bad faith conversion. Because the converted chapter 7 estate, in most cases, encompasses only property that the debtor owned or possessed at the time the bankruptcy case was commenced, retaining all of the property that the debtor acquires after that time within the estate does not even serve the purpose of protecting creditors against an ordinary conversion.[141] The plain text of chapter 13 ensures that when a debtor completes his chapter 13 plan, the general body of creditors are better off than if he had originally pursued chapter 7 liquidation. Rejecting the estate preservation theory means imposing upon creditors some risk that, if the debtor later chooses to convert, they will receive less than they would have received in an earlier liquidation. But it is hardly unfair to require creditors to bear that risk. Those creditors also gained the benefit of the greater upside potential afforded by the debtor's decision to first attempt to seek relief under chapter 13.

2. *Estate Reconciliation*

The estate reconciliation theory attempts to grapple with the apparent inconsistency created by sections 1306 and 1327 of the Code more carefully than the estate preservation theory, although it too ultimately falls short.[142] The estate

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[140] *See* Harris v. Viegelahn, 135 S. Ct. 1829, 1835 (2015) ("Proceedings under Chapter 13 can benefit debtors and creditors alike. Debtors are allowed to retain their assets, commonly their home or car.")

[141] 11 U.S.C. § 348 (2019).

[142] Courts that have adopted the estate reconciliation theory include the First Circuit, *Barbosa v. Solomon*, 235 F.3d 31, 35 (1st Cir. 2000), and the Eleventh Circuit, *In re Waldron*, 536 F.3d 1239 (11th Cir. 2008), as well as a substantial number of bankruptcy and district courts. *See also In re* Gonzales, 587 B.R. 363, 369 (Bankr. D.N.M. 2018) (noting the theory has "garnered a wide following" and citing cases); *In re* Wei-Fung Chang, 438 B.R. 77, 82–83 (Bankr. M.D. Pa. 2010); *In re* Powers, 435 B.R. 385, 389 (Bankr. N.D. Tex. 2010); *see generally* Peter Carpio & Jeffrey L. Cohen, *Modified Estate Transformation: When Does a Chapter 13 Estate Terminate*, 7 AM. BANKR. INST. L. REV. 213 (1999) (advocating for theory under label of modified estate transformation). The theory appears to have originated in the decision of the District Court for the Northern District of Illinois in *In re* Fisher, 203 B.R. 958 (N.D. Ill. 1997).

reconciliation theory acknowledges that to revest property of the estate in the debtor must mean to transfer that property to the debtor absolutely, such that the property exits the bankruptcy estate. [143] But it posits that revesting occurs only for property actually within the estate at the time the chapter 13 plan is confirmed.[144] Section 1327 means that at the time of plan confirmation, all of the property in the bankruptcy estate is transferred out of the estate and back to the debtor, leaving the bankruptcy estate empty. That property is no longer protected by the automatic stay, and the debtor may deal with it as he chooses. But section 1327 has no further effect after the time of plan confirmation. Section 1306 provides that the estate includes property acquired by the debtor at any time "before the case is closed, dismissed, or converted."[145] The estate reconciliation theory argues, therefore, that after confirmation the estate refills with property that the debtor acquires from the date of confirmation forward.[146] Any property that the debtor acquires from the day after the plan is confirmed until the time his bankruptcy case is concluded becomes property of the estate. The debtor must apply for court permission to use that property outside of the ordinary course of business, just as he was obligated to do for all of his prepetition property during the period before plan confirmation. And, as property of the estate, property acquired after plan confirmation is protected by the automatic stay. In the view of its progenitor, the Northern District of Illinois in *Fisher*, this interpretation "reconciles the text of the governing statutes without contradicting the language of any provision and without fatally undermining any important policy considerations."[147]

But the claim that the estate reconciliation theory resolves the textualist conundrum posed by sections 1306 and 1327 does not hold water. Section 1327 vests "*all* of the property of the estate" in the debtor.[148] Nothing in section 1327, nor in the provisions of section 541 and 1306 that set forth what assets shall comprise property of the estate, indicates that the time at which that property is acquired should have any effect on whether that property is property of the

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143 *See In re Fisher*, 203 B.R. at 962; Carpio & Cohen, *supra* note 142, at 230 (arguing that "property vesting in the debtor is no longer 'property of the estate.'").

144 *See, e.g.*, *In re Fisher*, 203 B.R. at 962; *Barbosa*, 235 F.3d at 36–37 (holding that "property of the estate *at the time of confirmation* vests in the debtors free and clear of any claims from the creditors") (emphasis added).

145 11 U.S.C. § 1306(a)(1) (2019).

146 *In re Waldron*, 536 F.3d at 1243 ("As one court has explained, some property of the estate is vested in the debtor at confirmation, under section 1327(b), but property acquired later vests in the estate, under section 1306(a), until the case ends or is converted" (citing *In re Fisher*, 203 B.R. at 962); *see also Barbosa*, 235 F.3d at 36–37.

147 *In re Fisher*, 203 B.R. at 964.

148 11 U.S.C. § 1327(b) (emphasis added).

estate. The estate reconciliation theory, therefore, continues, albeit only in part, to disregard the clear direction to revest the debtor with his property set forth in section 1327(b).

An occasional rejoinder to this critique is that section 1327(b) cannot, at the time of plan confirmation, vest the debtor with earnings or other property that he has not yet acquired.[149] In other words, "property acquired after confirmation is not subject to § 1327(b) because it was not in existence at confirmation. Therefore . . . § 1306(a) must place this property in the estate."[150] But that cannot be correct. The law frequently recognizes that interests in after-acquired property can be transferred.[151] There is no reason why confirmation of a plan that vests in the debtor all property of the estate cannot transfer to the debtor rights to those same after-acquired assets.

Although textually unsatisfying, the estate reconciliation theory's real flaws are practical in nature. It poses formidable administrative difficulties. Imagine a debtor who files for bankruptcy with a bank account into which his monthly wages are deposited. Any cash that accumulates in the bank account during the pre-confirmation period revests in the debtor upon confirmation and is no longer property of the estate. But income the debtor earns following confirmation *is* property of the estate. Months after confirmation, however, as money has been spent and deposited, it will be all but impossible for the bankruptcy court—let alone a financially unsophisticated debtor—to know which funds are the debtor's free and clear, and which are property of the bankruptcy estate. The distinction, of course, matters. The debtor who wants to make a down payment on a new car must take care to secure bankruptcy court approval before using estate property for such a transaction but is perfectly free to use his own funds for that purpose.[152]

At root, the estate reconciliation theory simply makes little sense.[153] Debtors in chapter 13 cases frequently file for relief because they hope to keep valuable

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[149] *In re Waldron*, 536 F.3d at 1243 ("New assets that a debtor acquires unexpectedly after confirmation by definition do not exist at confirmation and cannot be returned to him then."); *In re* Wei-Fung Chang, 438 B.R. 77, 83 (Bankr. M.D. Pa. 2010).

[150] *In re Wei-Fung Chang*, 438 B.R. at 83.

[151] For example, a debtor can grant a security interest in assets it will acquire in the future—in other words, a "floating lien". *See* U.C.C. § 9-204.

[152] *In re Wei-Fung Chang*, 438 B.R. at 83 (concluding that property acquired post-confirmation is property of the estate, but noting that "it is unrealistic to expect a Chapter 13 debtor, who may retain possession of his property and property of the estate for as long as five years, to keep track of how each asset is titled to ensure that he does not dispose of estate property without court approval").

[153] *See* Carlson, *supra* note 9, at 250 ("[I]f the debtor buys a car after the confirmation of the plan, the car belongs to the bankruptcy estate. The debtor dares not sell the car without court permission pursuant to section

assets—typically a home or a vehicle.[154] Those assets are returned to the debtor free and clear within weeks or months of his bankruptcy filing, as soon as his chapter 13 plan is confirmed. Absent a windfall, those assets are likely to be far more valuable than anything the debtor acquires in the post-confirmation period, while he is devoting his disposable income to the repayment of creditors under the plan. The estate reconciliation theory, therefore, does not even succeed at protecting the debtor like the estate preservation theory does. Postpetition creditors are free to pursue the debtor's house, car, or other prepetition property. Even so, it deviates from the simple rule of traditional chapter 11 in retaining after-acquired assets captive within the bankruptcy estate. "The Christmas after confirmation is a sad one under this theory, as the [estate] scoops up all the presents under the tree."[155] That retention, however, serves no readily discernible purpose. The debtor's fresh start is frustrated by the continued shadow of the estate, but the debtor still likely does not enjoy meaningful protection from postpetition creditors. If any property is to remain in the bankruptcy estate following confirmation, it must be pursuant to some more carefully calibrated rationale.

3. *Estate Transformation*

A third collection of theories, here described under the umbrella term of "estate transformation", holds that confirmation of the chapter 13 plan serves to transfer property of the estate to the debtor except for a limited category of property somehow related to fulfilment of the chapter 13 plan. The version of this theory most often adopted by bankruptcy courts argues that property of the estate revests in the debtor upon plan confirmation, except for property that is necessary for execution of the plan. A debtor with total monthly wages of $3,000 and a monthly payment under his chapter 13 plan of $500 might receive $2,500 each month absolutely, while $500 each month becomes property of the estate upon payment to the debtor. At some point, courts adopting this approach

363(b). But, the preconfirmation car could be sold post-confirmation without court permission."). Even greater confusion abounds if one concludes that proceeds of the sale of the pre-confirmation vehicle, as assets acquired by the debtor after confirmation, become property of the estate. Carlson, *supra* note 9, at 250. Under that view, the debtor obtains, in effect, the right to deal only with the "first generation" of property he owned at the time of confirmation, but as soon as he sells property or exchanges one asset for another, section 1306 captures the new property for the estate and prevents him from any further dealings without first seeking court permission.

[154] Harris v. Viegelahn, 135 S. Ct. 1829, 1835 (2015).

[155] *See* Carlson, *supra* note 9, at 250.

included the Eleventh Circuit and bankruptcy courts within that jurisdiction,[156] and, on one reading of the leading opinion, the Seventh Circuit.[157]

This approach suffers from similar practical flaws to the estate reconciliation theory. The debtor may frequently face great difficulty in actually understanding which of the assets he possesses are property of the estate, and which are his absolutely. There are several reasons for the debtor's confusion.

First, the criterion of "necessity" to execution of the plan may itself be difficult to apply.[158] The debtor will need to understand whether the "necessary" funds are limited to the precise amount of his monthly plan payment, or whether the bankruptcy court may find that it is necessary to retain additional funds within the estate to ensure that the debtor's ability to make plan payments is not disturbed by some unexpected expense.

Second, as with the estate reconciliation theory, even assuming the debtor and bankruptcy court are able to calculate what proportion of the debtor's wages or other income are necessary to the fulfilment of the plan and thus remain in the estate, actually identifying the amount of estate property within the debtor's

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156 Telfair v. First Union Mortgage Corp., 216 F.3d 1333, 1340 (11th Cir. 2000); *In re* Jemison, 2007 WL 2669222, at *5 (Bankr. N.D. Ala. 2007). The Eleventh Circuit later largely abandoned this approach in favor of the estate reconciliation approach. *See In re* Waldron, 536 F.3d 1239, 1243 (11th Cir. 2008)

157 *In re* Heath, 115 F.3d 521, 522–24 (7th Cir. 1997). In *Heath*, Judge Posner wrote in a short and somewhat cryptic opinion that the combined effect of sections 1306 and 1327 of the Code was that "while the filing of the petition for bankruptcy places all of the property of the debtor in the control of the bankruptcy court, the plan upon confirmation returns so much of that property to the debtor's control as is not necessary to the fulfillment of the plan." *Id.* These dicta are at least consistent with the estate transformation approach—although the opinion can also plausibly be read as concluding, consistent with the approach advocated by this Article, that the chapter 13 estate ordinarily terminates in its entirety upon confirmation, but may be preserved post-confirmation by means of a specific provision included in the plan or confirmation order only to include property necessary to fulfilment of the chapter 13 plan. *Id.* ("[C]onfirmation of a plan vests *all* of the property of the estate *in the debtor* unless the plan provides otherwise") (emphasis in original).

158 The Bankruptcy Court for the Eastern District of Virginia discussed the difficulty of applying the necessity criterion:

> There is also a practicable problem inherent in limiting the post-confirmation estate only to property necessary for the success of the chapter 13 plan. What property is necessary for the success of the chapter 13 plan? In a joint case, in the absence of a wage order under § 1325(c), which debtor's wages are protected by the automatic stay? In an individual case where the debtor holds more than one job, which paycheck is necessary for the success of the chapter 13 plan? Which one is not protected by the automatic stay and is subject to garnishment? There is nothing that distinguishes the debtor's paycheck from the co-debtor's paycheck or the debtor's primary paycheck from his secondary paycheck.

In re Reynard, 250 B.R. 241, 248 (Bankr. E.D. Va. 2000). The District Court for the Southern District of Georgia arrived at a similar result. *See* Thompson v. Quarles, 392 B.R. 517, 522 (S.D. Ga. 2008) ("[I]t is unclear when the new asset is 'necessary' to fund the 'plan' and whether the 'plan' is the original, previously confirmed plan, or a modified version of the confirmed plan that accounts for the value of the post-petition cause of action.").

possession at any given time will frequently be an insurmountable task. Funds necessary to make plan payments have no "independent identity" that makes them readily distinguishable from other funds belong to the debtor.[159] This variant of the estate transformation theory is viable only in a world in which the debtor's assets are not comingled and property necessary to the fulfilment of the plan is carefully segregated from all the debtor's other property. Needless to say, this ideal is unlikely to reflect the reality in which most chapter 13 debtors manage their affairs.

Carlson defends a slightly different version of the estate transformation theory. Adopting the label of the "divestment theory," Carlson proposes that the chapter 13 estate terminates upon confirmation except for "funds the debtor successfully transmits to the chapter 13 trustee for the benefit of creditors."[160] This theory narrows the scope of the post-confirmation estate even further. The chapter 13 estate does not include any of the debtor's post-confirmation wages or other income at the time those funds come into his hands. Rather, only at the time the debtor actually makes his chapter 13 plan payments are the funds transformed into property of the estate.[161]

Carlson's thesis is almost correct. Post-confirmation, property of the estate certainly does not encompass the debtor's prepetition property, or future income or other property that the debtor acquires and keeps postpetition. It also does not include, at least by default, that portion of the debtor's income that he intends to pay—or actually does pay—to the chapter 13 trustee. Carlson does not explain why he concludes that the chapter 13 estate post-confirmation must include funds in the hands of the chapter 13 trustee. Instead, it appears Carlson considers it self-evident that there must be some form of estate post-confirmation, and that the narrowest (and therefore most plausible) potential scope for such an estate is property actually in the hands of the chapter 13 trustee. Carlson's thesis, although more restrictive in scope than the alternatives discussed so far, ultimately fails to grapple with the question of why there must be a post-confirmation estate at all.

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159 *In re* Petruccelli, 113 B.R. 5, 16–17 (Bankr. S.D. Cal. 1990); *In re Reynard*, 250 B.R. at 248 ("Money is fungible.").

160 Carlson, *supra* note 9, at 233.

161 In many districts, chapter 13 plans operate pursuant to wage garnishment orders which instruct the debtor's employer to turn over the portion of the debtor's wages necessary to fund the plan directly to the chapter 13 trustee. *See* Greene, Patel & Porter, *supra* note 2, at 1066–67 (discussing differences in local practice as to employee wage orders). In such districts, there may be little practical difference in the way that Carlson's conception of the estate transformation theory operates compared to that described by the Eleventh Circuit in its *Telfair* decision and perhaps also contemplated by the Seventh Circuit in *Heath*.

Although Carlson rejects the label, it is fair to say that his theory does involve a "transformation" in the nature of the estate. Adopting Carlson's view, prior to confirmation, the estate chiefly comprises property in the hands of the debtor. At that time, the estate serves as a device limiting the debtor's ability to deal with that property (while protecting the property from postpetition creditors who might wish to pursue it). Following confirmation, property is within the bankruptcy estate only when it is in the hands of the trustee. The purpose of retaining an estate of such limited scope is unclear. And nothing in the Code alludes to or purports to provide for such a transformation. The thesis rests, at best, uneasily with the statutory provisions at issue. Unlike the distinction between pre-confirmation and post-confirmation property made by the estate reconciliation theory, the distinction between property in the hands of the debtor and property in the hands of the trustee cannot be traced back to section 1327(b). If anything, because section 1306(b) of the Code contemplates that the debtor shall remain in possession of property of the estate, Carlson's divestment theory reverses the scheme contemplated by the Code.[162]

Other courts, advocating for a variety of theories of chapter 13, have argued that the chapter 13 estate must survive confirmation in some form in order for the trustee to perform her duties. Defending the broader estate transformation theory, one bankruptcy court observed that:

> If there is no existing estate upon confirmation, then what does the Chapter 13 Trustee administer? If there is no estate over which the Chapter 13 Trustee has control, then that Trustee is nothing more than an officious intermeddler. Even 11 U.S.C. § 704(9), (made applicable to Chapter 13 Trustees by 11 U.S.C. § 1302(b)(1)), provides that the Trustee shall "... make a final report and file a final account of the administration of the *estate* [emphasis added] with the court." There must be an "estate" upon and after confirmation, and that estate

[162] One potential textual hook for the divestment theory is section 1322(a)(1) of the Code. 11 U.S.C. 1322(a)(1) (2019). That section provides that the portion of the debtor's future income necessary to fulfil the plan shall be submitted "to the supervision and control of the trustee." *Id.* Potentially, that section could be construed to provide a basis for a transformation in the estate at confirmation to include property necessary to the fulfilment of the plan. That reading of section 1322(a)(1), however, misreads the Code. Nothing in section 1322(a)(1) specifies that the property identified must remain in—or become a part of—the bankruptcy estate. Rather, section 1322 quite clearly contemplates that non-estate property may be involved in the post-confirmation payment of creditors. *Id.* § 1322. Section 1322(b)(9) speaks, without qualification, of property of the estate revesting upon plan confirmation. Section 1322(b)(8), meanwhile, provides that claims against the debtor may be paid "from property of the estate or property of the debtor"—from which follows the inference that there is no necessary connection between plan payments and the estate. *Id.*

> consists of the property and future earnings of the debtor dedicated to fulfillment of the Chapter 13 Plan.[163]

Carlson criticized the notion that the existence of an estate requires identifying any property in the hands of the debtor post-confirmation as property of the estate.[164] In effect, however, Carlson's article concludes that the property in the hands of the trustee belongs in the estate for the same reason: there must be an estate somewhere after confirmation in order for the trustee to do her job.[165] But there is no need for a bankruptcy estate to source the chapter 13 trustee's obligations. Rather, her obligations in the post-confirmation world come from the same source as those of every other party to the bankruptcy case: the plan. It is the plan that directs how much she should collect each month from the debtor, and to whom she should pay those funds. Thus, from the inception of the Code, the trustee's role in the post-confirmation world has been described as that of a "disbursing agent."[166] The Bankruptcy Rules similarly describe the trustee's role in collecting and distributing funds to creditors in accordance with the plan, again without reference to a surviving bankruptcy estate.[167]

Indeed, chapter 11 already offers an analog. Frequently, parties to a commercial chapter 11 case will have agreed upon a basic scheme of distribution before the assets to be distributed among creditors have been reduced to cash or otherwise become ready for distribution. The chapter 11 estate might, for example, possess a valuable cause of action against a third party which has not yet been litigated to judgment or settlement. Alternatively, the plan might contemplate that an unprofitable line of business will be liquidated, and the cash realized thereby distributed to creditors, without the debtor-in-possession having completed the process of selling off assets. For many years, a common solution in such cases has been to confirm a chapter 11 plan that transfers the assets in question to a trust.[168] The estate, as is usual in chapter 11 cases, still terminates upon plan confirmation, but a litigation or liquidating trustee is appointed to administer the new trust. The plan will specify how proceeds of the trust are to

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163 *In re* Root, 61 B.R. 984, 985 (Bankr. D. Colo. 1986).

164 Carlson, *supra* note 9, at 274.

165 Carlson, *supra* note 9, at 273–74.

166 H.R. REP. NO. 95-595, at 430 (1977) ("After confirmation of a plan, the court may order any entity from whom the debtor receives income to pay it, or part of it, to the trustee, who will serve as the disbursing agent under 1326."); 8 COLLIER ON BANKRUPTCY ¶ 1326 (16th ed. 2020) (similar).

167 FED. R BANKR. P. 3021 ("Except as provided in Rule 3020(e), after a plan is confirmed, distribution shall be made to creditors whose claims have been allowed, to interest holders whose interests have not been disallowed, and to indenture trustees who have filed claims under Rule 3003(c)(5) that have been allowed.").

168 *See generally* David Kuney, *Liquidation Trusts and the Quagmire of Postconfirmation Jurisdiction: The Case of the Disappearing Estate*, 14 J. BANKR. L. & PRAC. 6 ART. 3 (2005) (discussing considerations and the issue of bankruptcy court jurisdiction for liquidating trust cases).

be distributed. The source of that trustee's obligations is not, therefore, bankruptcy law governing administration of the bankruptcy estate. It is the chapter 11 plan itself, together with any documents drafted and executed pursuant to the plan that establish and regulate the trust in more detail. In sum, it is already commonplace in chapter 11, following plan confirmation, for a trustee to administer a corpus of property that is not part of the bankruptcy estate. Chapter 13 should be no different.

To the extent there is any uncertainty regarding the detail of the trustee's post-confirmation obligations, agency law can fill in the gaps.[169] Why the drafters of the Code chose to liken the trustee to a "disbursing agent" is not entirely clear; the general common law of agency does not identify a disbursing agent as a category of agent with distinct or specific obligations.[170] But the duties of a chapter 13 trustee are like enough to at least one familiar category of agent to supply any legal rules necessary to elucidate the trustee's role. The Second Restatement of the Law of Agency describes an "escrow holder" as a person who receives:

> money . . . delivered to . . . the holder [] by another and which the holder contracts to retain until the happening or non-happening of an event; if the event happens, or fails to happen, before a specified time, the escrow is to be delivered to a third person; otherwise he is to return it to the depositor.[171]

So too the chapter 13 trustee retains money paid by the chapter 13 debtor until plan confirmation,[172] following which she begins distribution of funds on hands to creditors in accordance with the terms of the confirmed plan. Upon other triggering events—principally dismissal or conversion of the case—the trustee instead returns funds currently on hand to the debtor.[173] Since it is also generally understood that the chapter 13 trustee is a fiduciary,[174] the law of fiduciary duties can similarly provide the detail necessary for the trustee to understand her duties without post-confirmation reference to the concept of the bankruptcy estate.

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169 The Code retains "long-established" and "familiar" common law principles except to the extent disturbed for some statutory purpose. *See* Isbrandtsen v. Johnson, 343 U.S. 779, 783 (1952).

170 Neither the Second nor the Third Restatements of the Law of Agency use the term. *See* RESTATEMENT (SECOND) OF AGENCY (AM. L. INST. 1958); *See* RESTATEMENT (THIRD) OF AGENCY (AM. L. INST. 2006).

171 RESTATEMENT (SECOND) OF AGENCY: AGENT OR ESCROW HOLDER § 14D cmt. a. (AM. L. INST. 1958).

172 11 U.S.C. § 1326(a) (2019).

173 *See* Harris v. Viegelahn, 135 S. Ct. 1829 (2015) (holding that conversion terminates the services of the chapter 13 trustee and thus requires her to return any funds on hand at that time to the debtor).

174 *See, e.g.*, *In re* Gutierrez, 309 B.R. 488, 499 n. 20–21 (Bankr. W.D. Tex. 2004); *In re* Morgan, 353 B.R. 599, 605 (E.D. Ark. 2006); *In re* DiRuzzo, 513 B.R. 422, 429 (Bankr. D.R.I. 2014).

Precisely identifying the best common law analog to the chapter 13 trustee is not the focus of this Article. The point is that multiple sources of law—the law of contracts, since the confirmed plan is recognized by all to be a contract; the law of fiduciary duties; and the law of agency and escrow—supply the principles necessary to define the trustee's task and resolve any uncertainties about how she is to perform it. The estate is an unnecessary concept post-confirmation. And no courts or commentators have successfully explained what benefits are gained by straining the statutory language to insist that the estate remains open, by default, as to the narrow category of property necessary to or actually used for the fulfilment of the plan, while other property of the estate revests in the debtor. The estate transformation and divestment theories, therefore, also do not successfully account for the structure of chapter 13.

4. *Estate Termination*

The best theory of chapter 13, then, is this: following confirmation of a plan, absent some contrary provision of the plan or confirmation order, the estate simply terminates. Chapter 13 operates no differently than chapter 11 in this regard—a conclusion that makes sense, given that chapter 13 is the "'personal reorganization' counterpart to the better-known Chapter 11."[175] All property within the estate at the time of plan confirmation revests in the debtor, and no additional property enters the bankruptcy estate thereafter. In the chapter 11 context, courts have not hesitated to conclude that the overall structure of the Code makes clear that the bankruptcy estate terminates upon confirmation. Although only a limited number of courts have adopted this approach in chapter 13, it best fits with the statutory text and structure in that context also.[176]

The estate termination theory is strongly supported by the legislative history. The drafters of the Code did not comment on the lifespan of the chapter 13 estate in the sections of the legislative history specifically discussing sections 1306 and 1327 of the Code—as, indeed, they similarly did not comment on the lifespan of the chapter 11 estate in discussing section 1141. Legislative history does, however, address the lifespan of the chapter 13 estate when considering whether

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[175] *In re* Heath, 115 F.3d 521, 522 (7th Cir. 1997); *see also* 8 COLLIER ON BANKRUPTCY ¶1300.01 (16th ed. 2020) (chapter 13 is "quite similar to chapter 11, with which it shares many concepts").

[176] *See, e.g.*, *In re* Jones, 420 B.R. 506, 515 (B.A.P. 9th Cir. 2009) (adopting estate termination approach); *see also In re* Petruccelli, 113 B.R. 5, 16–17 (Bankr. S.D. Cal. 1990); *In re* Sihabouth, 2014 Bankr. LEXIS 2870, at *7–8 (B.A.P. 9th Cir. 2014); *In re* Matthews, 2017 Bankr. LEXIS 117, at *15–16 (Bankr. D. Idaho 2017); *In re* Clark, 2015 Bankr. LEXIS 3564, at *9 (Bankr. E.D. Cal. 2015); *In re* Dagen, 386 B.R. 777, 782 (Bankr. D. Colo. 2008); *In re* Toth, 193 B.R. 992, 996 (Bankr. N.D. Ga. 1996), *overruled by In re* Waldron, 536 F.3d 1239 (11th Cir. 2008) *and* Telfair v. First Union Mortgage Corp., 216 F.3d 1333 (11th Cir. 2000).

that estate should be treated as a separate taxable entity from the debtor. That was thought to be unnecessary, because the chapter 13 estate was expected to be short-lived. The House Judiciary Committee report explained that "[t]he administrative reality [is] that most Chapter 13 estates will only remain open for 1 or 2 months until confirmation of the plan at which time section 1327(b) of title 11 will almost always revest title to property of the estate in the debtor."[177] Thus, the House report concluded, "[t]he duration of a chapter 13 case is so short that there is no reason to impose a duty to pay taxes on the trustee."[178] The legislative history demonstrates a contemporary understanding that revesting property of the estate in the debtor meant the closing of the estate, and *not* merely a grant of a right of possession of property of the estate or the transformation of the estate into some other form. All the available evidence suggests, therefore, that Congress anticipated that the chapter 13 estate would terminate upon confirmation of the plan.[179]

Not all the consequences of estate termination may be welcome for every debtor and creditor. As I have explained, estate termination frees the debtor to deal with her property as she chooses. But it also frees postpetition creditors to

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177 H.R. REP. NO. 95-595, at 276, *as reprinted in* 1978 U.S.C.C.A.N. 5963, 6233.

178 *Id.* at 277. It is clear that by "duration of a chapter 13 case," the House report meant the time until a plan is confirmed, not the time until plan payments are completed and the debtor receives a discharge. The committee understood that plan payments were likely to continue for a number of years after the commencement of the bankruptcy case. *See id.* at 276. Rather, it viewed the chapter 13 case as giving the debtor a brief "breathing spell in which to reach an arrangement with creditors," noting that this period would be short because "[t]he plan is filed very rapidly." *Id.*

179 To be sure, even the most persuasive interpretation of the Code, the "estate termination" model has its imperfections. The chief anomaly created by the estate termination model relates to section 348(f) of the Code, which governs conversions by a debtor from a chapter 13 case to chapter 7 case that occur in bad faith. Normally, when a debtor converts a case from chapter 13 to chapter 7, the estate in the new chapter 7 case comprises only property that was contained in the estate at the time the bankruptcy case was originally filed. 11 U.S.C. § 348(f)(1)(A) (2019). Even though section 1306 means that, prior to confirmation, property acquired after the bankruptcy filing is added to the estate, that property is not included in the chapter 7 estate. In a case of bad faith conversion, the Code provides that the "property of the estate in the converted case shall consist of property of the estate as of the date of conversion." *Id*. § 348(f)(2). Prior to confirmation, that simply serves to render all of the debtor's property, whether acquired prepetition or postpetition, property of the new chapter 7 estate. Post-confirmation, under the estate termination theory, however, there may be *no* property within the chapter 13 estate. It seems clear that Congress intended, in a case of bad faith conversion, that all of the debtor's property, whenever acquired, should be part of the new chapter 7 estate. Section 348(f) was added to the Bankruptcy Code in 1994, after at least some courts had adopted a practice of maintaining all property within the estate throughout the chapter 7 case. *See*, *e.g.*, Security Bank of Marshalltown v. Neiman, 1 F.3d 687, 690–91 (8th Cir. 1993). The anomaly created here, however, is not a grave one. Confirmation of a chapter 13 plan requires a determination from the bankruptcy court that the chapter 13 case has been proceeding in good faith. 11 U.S.C. § 1325(a)(3). It seems unlikely that a debtor who had previously proposed and been performing under a plan good faith will subsequently affect a bad faith conversion. And in any event, the bankruptcy court always retains the power to sanction a debtor for bad faith conduct by dismissing the case or denying the debtor a discharge. *Id.* §§ 707(3)(a), 727.

pursue the debtor's assets without first seeking court permission. For some of the debtor's new creditors, this will be of little effect. Ordinary unsecured creditors will likely need to invoke some other court process before they have any opportunity to force repayment of a debt—for example, by getting a judgment against the debtor in state court and securing a wage garnishment order. But a new secured creditor of the debtor will be able to exercise ordinary self-help remedies: for example, if the debtor who bought a truck post-confirmation and falls behind on his payments will find that the auto lender can repossess the truck just as it would have outside of bankruptcy.

Other creditors may have similar self-help remedies. The Seventh Circuit in its *Steenes* decisions was faced with the question of whether the city of Chicago, in cases in which it was a postpetition creditor of the debtor, could exercise its ordinary remedies of towing and impounding a city resident's vehicle based on unpaid traffic fines.[180] The Seventh Circuit found that the City should, in future cases, be free do to so because the chapter 13 estate should not extend to include the debtor's property post-confirmation.[181] Securing exactly this kind of protection, though, is central to many defenses of preservation of the estate; it is for that reason, in jurisdictions where the debtor may choose what theory of the estate to adopt, that debtors are routinely advised to keep property within the estate—a recommendation that has been echoed by one prominent former bankruptcy judge in his leading treatise on chapter 13.[182]

5. *A Defense of Estate Termination*

A defense of estate termination may proceed along two lines. First, even conceding that the broader policy goal animating this recommendation, of enhancing the success rate of chapter 13 or other debt adjustment bankruptcy cases, is a worthy one, preserving the estate is likely not as effective in securing that goal as many of its defenders suppose. The protection is at root more a procedural than a substantive one. There are likely to be other, better ways of promoting success in debt adjustment bankruptcy. Second, even that limited

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180 *See Steenes I*, 918 F.3d 554, 556–57 (7th Cir. 2019); *Steenes II*, 942 F.3d 834, 836 (7th Cir. 2019).

181 *Steenes I*, 918 F.3d at 558.

182 Former Judge Lundin noted:

> The debtor is best positioned to defend the problems created by § 1327(b) by always including in the plan a provision continuing the estate and overcoming the vesting effect of § 1327(b) until completion of payments under the plan. Coupled with the expanded definition of estate property in § 1306, this puts the debtor in the strongest position to argue that the stay continues to protect all property and income after confirmation.

Keith M. Lundin, LUNDIN ON CHAPTER 13 § 113.11, at ¶ 3 (2020).

protection, absent the exceptional facts that I describe in Section II.B.2 below, seems inconsistent with the logic and structure of debt adjustment bankruptcy law.

a. Stay Relief and Administrative Expenses

As to the first point, the protection against postpetition creditors provided by sheltering assets within the estate is not absolute. Unpaid postpetition creditors may seek a remedy from the bankruptcy court. Most clearly, those creditors have the right to seek relief from the automatic stay, which will free the creditor to take any actions that would be permissible under state law, just as if the estate had terminated at plan confirmation.[183] Stay relief may be granted for cause—a standard which is likely met in a case in which a debtor is using estate property in a way that generates obligations to postpetition creditors that she is not meeting.[184] Perhaps more controversially, the Seventh Circuit ruled in *Steenes II* that unpaid postpetition creditors may, at least in some circumstances, be entitled to an administrative expense, affording them the right not just to be paid in the bankruptcy case, but to receive priority treatment as against the debtor's prepetition general unsecured creditors.[185]

Here is how the administrative expense theory works. The Code entitles creditors who meet the actual and necessary costs and expenses of preserving the estate to receive a priority claim for reimbursement.[186] In a debt adjustment bankruptcy, such a priority claim is typically paid from the debtor's regular plan payments, diminishing the funds available to pay prepetition creditors. Administrative expenses must be paid in full before the debtor may be deemed to have completed the plan and receive a discharge.[187] In a traditional chapter 11 case, it has long been recognized that involuntary creditors of the bankruptcy estate are entitled to such administrative expenses.[188] Without this rule of

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[183] 11 U.S.C. § 362(d).

[184] Relief from the automatic stay, therefore, was the alternative remedy for postpetition creditors highlighted by the lower courts and by the chapter 13 trustee in the *Steenes* litigation as a better alternative to prohibiting debtors from preserving property within the estate or granting administrative expenses. City of Chicago v. Marshall, 281 F. Supp. 3d 702, 705 (N.D. Ill. 2017), *rev'd by Steenes II*, 942 F.3d 834 (7th Cir. 2019); Response Brief of Trustee-Appellee Marilyn O. Marshall at 20–23, *Steenes I*, No. 17-3630 (7th Cir. May 14, 2018). In cases in which the debtor has resorted to the protections of the automatic stay in bad faith, both the District Court and the trustee in *Steenes* suggested that the case might be dismissed entirely. *Id.*

[185] *Steenes II*, 942 F.3d at 839 (7th Cir. 2019).

[186] 11 U.S.C. §§ 503(b)(1)(A), 507(b).

[187] *Id.* § 1322(a)(2). Section 1328(b) allows for a hardship discharge where the debtor is unable to complete a plan "due to circumstances for which [she] should not justly be held accountable" and she has already paid to unsecured creditors at least as much as they would have received in a chapter 7 liquidation. *Id.* § 1328(b).

[188] *See* Reading Co. v. Brown, 391 U.S. 471, 482–83 (1968); *Steenes II*, 942 F.3d at 836.

traditional chapter 11, a debtor with a pending bankruptcy case that pollutes its surrounding neighborhood might resort to bankruptcy to avoid or defer liability for clean-up costs.[189] Tort creditors and other similar postpetition creditors of the estate would be turned into involuntary financiers of the bankruptcy case as the debtor used the bankruptcy to avoid meeting its obligations to them while resolving its liabilities to prepetition creditors. Intermittently, the same reasoning has been applied to chapter 13.[190] The logic of this analysis is hard to deny. If—and only if—a debtor's property remains within the bankruptcy estate, then the costs of maintaining that property become costs of preserving the bankruptcy estate. When such costs are necessary or are involuntarily imposed upon creditors—such as the unpaid traffic tickets in *Steenes II*—there is a fair argument that they should qualify as administrative expenses.

Exactly how persuasive this conclusion may be is not the focus of this Article. It is not essential that the *Steenes II* administrative expense ruling hold true to conclude that the potential protection of the expanded estate is qualified because creditors will always have the right to seek relief from stay. And there are perhaps textual reasons—and certainly policy reasons—to be wary of the administrative expense analysis. On a textual level, allowing postpetition creditors administrative expenses in chapter 13 cases (even if not in other forms of debt adjustment bankruptcy) sits uneasily with section 1305, which provides a less favorable mechanism by which some postpetition creditors may seek to participate in the bankruptcy case.[191] On a policy level, granting an administrative expense is a significantly more heavy-handed remedy than granting relief from stay. It does the very opposite of what this Article argues should be the norm in the post-confirmation world—it expands, rather than minimizes, the footprint of the bankruptcy court because the court becomes responsible for ensuring that the debtor's postpetition creditors are paid. Moreover, while estate termination refuses to allow the debtor ordinarily to use the bankruptcy case as a shield against postpetition creditors, it does not actually take sides in those disputes over payment between the debtor and creditors.[192] It

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[189] In *Reading*, an employee of the debtor started a fire that damaged a neighboring property. *Reading Co.*, 391 U.S. at 473.

[190] *Compare Steenes II*, 942 F.3d at 837–39 (concluding that *Reading* controls in chapter 13 just as in chapter 11), *with In re* Haynes, 569 B.R. 733, 739 (Bankr. N.D. Ill. 2017) *overruled by Steenes II*, 942 F.3d 834 (7th Cir. 2019) (rejecting the administrative expense argument arguing that Chicago "does not cite one opinion that applies *Reading v. Brown* in a Chapter 13 case.").

[191] *But see Steenes II*, 942 F.3d at 838. The best rejoinder to this argument may be that Congress did not anticipate that postpetition creditors would routinely hold administrative expense claims precisely because it did not anticipate that the estate would routinely outlast plan confirmation.

[192] The exception to this principle is when a postpetition creditor chooses to participate in the bankruptcy case pursuant to section 1305 of the Code, in which case it accepts payment on the same terms as other general

leaves all such disputes, and the legality of any actions creditors might take in connection therewith, to state law and ordinary non-bankruptcy processes. Allowing postpetition creditors administrative expense claims instead puts bankruptcy's thumb on the scales in favor of the postpetition creditor.

For purposes of this Article's analysis, the key insight is simply that the decision to keep property within the estate to protect against postpetition creditors is far from a sure one. Although my preference in cases in which property has been preserved within the estate and a postpetition creditor has gone unpaid would be to grant relief from stay rather than allow an administrative claim, the debtor is subject to attack along either pathway. Thus, the real effect of preserving property within the estate is a procedural rather than a substantive one. What the debtor really gains is an opportunity to have the validity of the postpetition creditor's claim tested in the bankruptcy court before any money or property is transferred to that creditor. As discussed below in Section III.B.2, there are some cases where this additional procedural hurdle may be justified. But in many cases, it is likely inconsistent with the structure of debt adjustment bankruptcy law.

b. The Place of Postpetition Expenses in Bankruptcy

The basic assumption of debt adjustment bankruptcy is that debtors can afford to pay current expenses as they come due. Debt adjustment bankruptcy commits only disposable income to the plan—what the debtor has left to repay creditors with after subtracting allowable expenses from income. A debtor who cannot afford to pay current expenses is not a good candidate for debt adjustment bankruptcy. Indeed, bankruptcy will necessarily fail to rehabilitate such a debtor financially, as new unpaid debts mount up even as old debts are paid under the plan. It is true that many debtors may face unexpected new expenses some way into a debt adjustment bankruptcy case. This problem is most keenly identifiable in chapter 13; commentators investigating the low success rate of chapter 13 plans have found that many chapter 13 cases fail for precisely this reason.[193] It is plausible that allowing the debtor to defer paying postpetition creditors might allow them more space to keep making plan payments and thus complete their cases. But this is inequitable to postpetition creditors who are by default excluded from the plan. And because, as discussed in the preceding Section, the key effect of preserving the estate is to erect a procedural hurdle rather than a

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unsecured creditors and, in exchange for this immediate partial payment, at least runs the risk that the unpaid balance of its claims will be discharged. *See* Keith M. Lundin, LUNDIN ON CHAPTER 13 § 158.6, at ¶ 2 (2020).

193 *See* Greene, Patel & Porter, *supra* note 2, at 1063–64.

substantive barrier in front of postpetition creditors, the greatest impact of estate preservation may be to discourage postpetition creditors from pursuing debts that are too small to justify the additional costs of enforcement.[194]

There are likely better ways to respond to this important problem. One possibility is to permit liberal modification of chapter 13 plans by debtors, allowing the debtor to reduce their monthly payment to prepetition creditors when faced with some new financial shock.[195] Concomitantly, reducing the trustee or creditor's ability to seek modification to increase plan payments may allow the debtor to build up additional financial resources.[196] Some bankruptcy courts, when calculating a debtor's monthly disposable income, recognize as one of the permissible expenses that chapter 13 debtors may deduct from their gross income a regular contribution to an emergency savings fund;[197] recent reform proposals have suggested standardizing that practice.[198] Under chapters 13 and 12, the bankruptcy court may approve a "hardship discharge" for debtors whose failure to complete the plan is due "to circumstances for which the debtor should not justly be held accountable. . . ."[199] As a result, bankruptcy courts should consider more frequently resorting to this rarely deployed safety valve.[200]

B. *The Life of the Bankruptcy Estate in Chapter 12 and Small Business Cases*

The estate termination theory also holds in chapter 12 and subchapter V. First, in chapter 12, the language of the statute is identical in all respects. Section 1227 of the Code, like section 1327, vests all property of the estate in the debtor at plan confirmation.[201] There is no reason to believe that vesting property of the estate means anything different in chapter 12 than in chapter 13—or the traditional understanding of chapter 11 which, in turn, informs the estate

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194 In oral argument in *Steenes I*, Judge Easterbrook suggested that one potential consequence of preserving the estate would be to make after-the-fact collection of de minimis expenses relating to operating a vehicle—such as a toll that is not paid at the time a car is driven on a toll road—practically uncollectable so long as the vehicle remains in a chapter 13 bankruptcy estate. Oral Argument at 32:33–34:59, *Steenes I*, 918 F.3d 554 (7th Cir. Sept. 12, 2018) (No. 17-3630), http://media.ca7.uscourts.gov/oralArguments/oar.jsp?caseyear=17&casenumber=3630&listCase=List+case%28s%29.

195 *See* 11 U.S.C. § 1329 (2019).

196 Indeed, subchapter V does precisely this for small business debtors; only the debtor, and not the trustee or creditors, may propose modifications to a confirmed plan. *Id.* § 1193(b).

197 AM. BANKR. INST., FINAL REPORT OF THE ABI COMMISSION ON CONSUMER BANKRUPTCY 173 (2019).

198 *Id.* at 171–72.

199 11 U.S.C. § 1328(b). The debtor must already have paid creditors at least as much as they would have received in a liquidation, and the bankruptcy court must also make a finding that the debtor's problems cannot be resolved by modification of the plan. *Id.*; *see id.* § 1228(b).

200 *See* Lawrence Ponoroff, *Rethinking Chapter 13*, 69 ARIZ. L. REV. 1, 43–44 (2017).

201 11 U.S.C. § 1227(b).

termination theory in chapter 13. For that reason, the few courts that have considered the lifespan of the bankruptcy estate specifically within the context of chapter 12 have stressed the influence of chapter 13 on their analysis.[202] Indeed, the Supreme Court has explained that "because chapter 12 was modeled on chapter 13, and because so many of the provisions are identical, chapter 13 cases construing provisions corresponding to chapter 12 provisions may be relied on as authority in chapter 12 cases."[203] Whatever conclusion is reached regarding the lifespan of the bankruptcy estate in chapter 13, it must hold for chapter 12 also.

Only in subchapter V are there any difficulties in reaching this conclusion. This is perhaps counterintuitive. The notion that property of the chapter 13 or 12 estate vests in the debtor upon confirmation, terminating the estate, is informed by the understanding of traditional chapter 11. Exactly the same statutory provision that prescribes vesting of the estate in the debtor in traditional chapter 11 cases applies in subchapter V.[204] At first glance, this same result should hold: for subchapter V cases, the bankruptcy estate will terminate at plan confirmation.

Section 1186 of subchapter V, however, obstructs this conclusion. In large part, this section tracks the sections of chapter 12 and 13 that explain that property of the estate comprises not just property that the debtor owns as of the bankruptcy filing, but also property acquired afterwards.[205] I have explained why the broad language of these sections does not justify the conclusion that the estate nevertheless remains in existence after confirmation of the plan.[206] Section 1186 adds an additional gloss to this language; it provides that "*[i]f a plan is confirmed under section 1191(b) of this title*," property of the estate shall include property acquired after the commencement of the case.[207] Because the extensive words regarding the scope of the bankruptcy estate are said to apply only "if a plan is confirmed," the most natural reading of the text appears to be that the expansive subchapter V estate must exist after confirmation—indeed, that it *only*

[202] *See, e.g.*, *In re* Knudsen, 356 B.R. 480, 490 (Bankr. N.D. Iowa 2006) (adopting the estate preservation theory in chapter 12, citing chapter 13 cases); *In re* LaRosa Greenhouse, LLP, 565 B.R. 304, 311–12 (Bankr. D.N.J. 2017) (same); *In re* Smith, 514 B.R. 464, 468–72 (Bankr. N.D. Tex. 2014) (adopting a hybrid view of the estate, citing chapter 13 cases); *In re* Daugherty, 117 B.R. 515, 518 (Bankr. D. Neb. 1990) (adopting estate termination, discussing chapters 12 and 13 together).

[203] Hall v. United States, 566 U.S. 506, 516 (2012) (internal citations omitted).

[204] 11 U.S.C. § 1141(b) ("Except as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor.").

[205] *Id.* §§ 1306, 1207.

[206] *See supra* Section II.A.1.

[207] 11 U.S.C. § 1186(a)(1) (emphasis added).

exists post-confirmation, rather than from the beginning of the bankruptcy case. In other words, of the various theories of the lifespan of the bankruptcy estate, section 1186 of subchapter V seems most compatible with an incomplete theory of estate preservation. Judge Paul Bonapfel, in one of the few extended commentaries on SBRA published to date, reaches exactly this conclusion.[208]

Yet it seems unlikely that this is what Congress intended. The legislative history of the SBRA is minimal. The relevant section of the House report simply repeats the statutory language.[209] Nothing suggests an intention to resolve a multi-decade circuit split over this question of statutory interpretation. Even less plausible is that Congress would resolve this split in a way that tracks no pre-existing rule. Section 1186 is different to its counterparts in chapters 12 and 13, because as drafted, it appears to speak only to the period after confirmation of the plan. No pre-existing theory of the estate in debt adjustment bankruptcies has argued that the expanded estate comes into being only following plan confirmation. It seems unlikely that Congress intended to create a new and different working model of the debt adjustment bankruptcy estate. What is more probable is that Congress intended simply to duplicate the law as it exists under chapters 12 and 13. In that case, the statement that the expanded estate applies "if a plan is confirmed" reflects the fact that small business debtors have a choice how to proceed within chapter 11. Small business debtors may elect to proceed under the rules for traditional chapter 11, confirming a plan that is subject to all the usual requirements for a corporate reorganization, or they may choose the more streamlined procedures created by subchapter V. Congress's likely intention, therefore, was to implement a separation among small business debtors, segregating those proceeding under the new subchapter V provisions from those proceeding under traditional chapter 11. I believe Congress sought to subject the former, but not the latter, to the same expanded bankruptcy estate that is applicable to chapter 12 and 13 debtors, without deciding the precise content of that estate.

It remains unclear how bankruptcy courts should implement section 1186. Taken literally, there is little to justify the statutory scheme that Judge Bonapfel describes, in which an expanded estate comes into being only at the moment that the debtor confirms a plan. That approach gets precisely backward the policy rationale discussed above: that close supervision of the debtor's affairs is justified immediately after the bankruptcy case has begun, and it is unclear what the debtor's obligations to its creditors will be, but that the debtor should be able

[208] Bonapfel, *supra* note 26, at 626–27.
[209] H.R. REP. NO. 116-171, at 6 (2019), *as reprinted in* 2019 WL 3401849.

to enjoy a fresh start once its plan is confirmed and has embarked upon repayments. And in contemplating that property will move into the estate while the case is ongoing, this approach imports the most serious problem that affects the estate reconciliation theory; it may be difficult for the debtor to know exactly what property it has the right to deal with freely at any given time.

Indeed, the policy arguments against preservation of the estate post-confirmation are even stronger for business debtors than for consumer debtors under chapter 13. Depending upon a debtor's business model, a requirement that a business debtor appears in court to seek permission before making any other than ordinary sale or purchase, or other use of estate property, may prove burdensome. A business may acquire or dispose of assets with substantial value—such as equipment or real property—with greater frequency than a consumer. In some chapter 12 cases, debtors have been required to litigate pursuant to section 363(b) whether they may sell land or other property post-confirmation.[210] Since the section 363 standard is typically deferential to a debtor's business judgment, requiring litigation over such decisions hardly seems like an efficient use of resources. In similar fashion, because the Code regulates the payment of attorneys' fees out of the bankruptcy estate, a small business debtor who becomes involved in litigation during its bankruptcy case on a matter entirely separate from the conduct of the bankruptcy may nonetheless be required to submit its attorneys' fees to the bankruptcy court for approval.[211] Nor is it a convincing argument that a business should enjoy enhanced protection from its postpetition creditors. I have argued that the Code should not shelter a consumer from a postpetition creditor that she cannot afford to pay in order to give her a chance to pay prepetition creditors and earn a discharge.[212] But there is certainly a plausible equity-based argument for assisting consumers in securing a fresh start in this way. A business, in contrast, should not be able to seek the aid of the bankruptcy courts in externalizing its financial problems upon postpetition creditors.

The better view, therefore, is that section 1186 should not be read to have committed Congress to any particular theory of the bankruptcy estate in subchapter V. The estate termination theory should prevail there, as elsewhere, because it is the theory that best accounts for the structure of debt adjustment bankruptcies and the policy considerations that underlie them. Bankruptcy

[210] *See In re* McLendon, 506 B.R. 243, 246 (Bankr. N.D. Miss. 2013).

[211] *See In re* LaRosa Greenhouse, 565 B.R. 304, 312 (Bankr. D.N.J. 2017) (bankruptcy court approval required for fees for post-confirmation services provided by attorney in chapter 12 case); *In re* Brandenburger, 145 B.R. 624, 629–30 (Bankr. D.S.D. 1992) (similar).

[212] *See supra* page 6.

courts may be able to reach this outcome by concluding that section 1186 must still be read together with the Code's mandate that, unless the plan states otherwise, confirmation vests property of the estate in the debtor. In a case in which the plan purports to preserve the estate, then section 1186 will tell the debtor what property is contained therein. The greatest certainty, though, would come from clarification from Congress. Perhaps more feasible is an amendment of section 1186 that does not tip the scales towards any one of the pre-existing theories of the estate.[213] Congress might also choose to resolve the dispute for all forms of debt adjustment bankruptcy. In either case, subchapter V would be best served by application of the estate termination theory.

III. EXTENDING THE LIFE OF THE BANKRUPTCY ESTATE

The conclusion that the estate termination theory is more persuasive than other theories of debt adjustment bankruptcy does not fully resolve questions regarding the fate of the bankruptcy estate upon confirmation of a debt adjustment plan. Rather, the estate termination theory sets forth a default rule. The Code contemplates, however, that there will be circumstances when courts or debtors may depart from the statutory default. Section 1327(b) of the Code provides that property revests in the debtor "[e]xcept as otherwise provided in the plan or in the order confirming the plan."[214] Section 1322(b)(9) provides that the plan shall provide for vesting of property of the estate in the debtor or another entity "on confirmation of the plan or at later time."[215] Chapter 12 and chapter 11 contain largely parallel provisions.[216]

Notwithstanding the disagreement regarding the default rule those provisions establish, courts and commentators, with a few exceptions, have presumed that these provisions grant a largely free choice—whether to debtors, to bankruptcy courts, or to both—to adopt a different vesting rule, if the default rule is not to their liking.[217] Thus bankruptcy courts routinely confirm plans that

213 Congress might delete the reference to plan confirmation in section 1186, and instead state that the expanded definition of property of the estate shall apply in any case in which the debtor elects to proceed under subchapter V. Since an expanded estate, with the closer supervision of the debtor that it brings, is most important at the beginning of a case, Congress could also require a small business debtor promptly to declare after commencing the case its intention to proceed either under subchapter V or traditional chapter 11, engaging as quickly as possible the expanded bankruptcy estate contemplated by section 1186.

214 11 U.S.C. § 1327(b) (2019).

215 *Id.* § 1322(b)(9)

216 *Id.* §§ 1227(b), 1222(b)(1), 1141(d). Subchapter V contains no analog to §1322(b)(9)'s direction that the plan shall explain in whom property of the estate shall vest.

217 Indeed, Carlson suggests that the text of the Code "specifically invites just this." Carlson, *supra* note 9, at 244–46.

provide that the bankruptcy estate shall not terminate upon confirmation. Instead, revesting property of the estate is delayed until a later time—typically, the end of the bankruptcy case. In essence, debtors and bankruptcy courts are thought to be empowered to adopt an entirely different theory of the estate and its purposes to suit individual cases.

The better view is that the presumption that all property of the estate revests upon plan confirmation cannot be so lightly dispensed with. Instead, the default rule is sticky. Before a plan providing for continuation of the estate may be approved, the bankruptcy court must find that preserving the estate serves a valid bankruptcy purpose. Typically, that will require a showing by the debtor that keeping property in the bankruptcy estate is necessary to the fulfilment of the plan. The pathbreaking decision suggesting such an approach is the Seventh Circuit's opinion in *In re Heath*.[218] As previously noted, *Heath* is somewhat unclear in its view of the default rule of revesting upon confirmation of a chapter 13 plan.[219] The Seventh Circuit's description of the chapter 13 estate as "return[ing] so much of that property to the debtor's control as is not necessary to the fulfillment of the plan" could be read either to adopt the estate transformation or the estate termination theories.[220] Regardless, *Heath* did clearly argue, albeit in brief dicta, that property necessary to the fulfillment of the plan represented an upper limit on the contents of the estate post-confirmation. *Heath* suggested that it would be an abuse of the bankruptcy court's discretion to confirm a plan or sculpt the terms of a confirmation order to provide that any additional property remained in the chapter 13 estate.[221]

The Seventh Circuit recently reiterated its conclusions from *Heath* in *Steenes I*.[222] At the time of the *Steenes I* decision, the form confirmation order used in every chapter 13 bankruptcy case in the Northern District of Illinois incorporated a delayed revesting provision even broader than that at issue in *Heath*. The *Steenes I* form confirmation order provided that all of the debtor's property should remain in the estate until the conclusion of the bankruptcy case.[223] In essence, the bankruptcy court adopted the estate preservation theory, not as a matter of statutory interpretation, but instead via local rule superimposed

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218 *In re* Heath, 115 F.3d 521, 522–24 (7th Cir. 1997).

219 *Id.*

220 *Id.* at 524.

221 *Id.* ("It would presumably be an abuse of discretion for the bankruptcy court to confirm a plan that retained more of the property in the hands of the trustee than was reasonably necessary to fulfill the plan, though we need not decide that in this case.").

222 *Steenes I*, 918 F.3d 554, 557 (7th Cir. 2019).

223 *Id.* at 556.

over the Code's ordinary default rules. The Seventh Circuit characterized this as a reversal of the Code's "presumptive[] return[] [of] the estate's property to the debtor."[224] But that kind of blanket reversal was illegitimate: "[i]t is hard to see how the court could justify routinely doing the opposite of what the statute provides."[225] Although it gave little explanation for the form such an order might take, or the reasons that might be required to support it, the Seventh Circuit made clear that "a case-specific order, supported by good case-specific reasons" would be necessary before property may be retained in the bankruptcy estate post-confirmation.[226]

This conclusion was subsequently reiterated in *In re Cherry*.[227] In *Cherry*, it was the debtor, rather than the bankruptcy court, that sought to include within the plan a provision preserving the estate.[228] Just as in *Steenes I*, however, the preservation of the estate was not supported by any explanation or any findings by the bankruptcy court; rather, the court asserted that it was the debtor's right to choose what theory of chapter 13 to implement.[229] The Seventh Circuit disagreed; any time the debtor (or the bankruptcy court) wants to depart from the default rule, the debtor has to provide adequate reasons to justify this choice.[230] The alternative allowed for the subversion of the ordinary statutory scheme without appropriate justification.[231]

The Seventh Circuit has it right. The Seventh Circuit's approach to plan or confirmation order provisions that deviate from the default rule of estate termination and preserve the bankruptcy estate states the correct rule of the bankruptcy estate in debt adjustment cases—although it requires further elucidation. This Section will explain that the power to propose a plan provision that delays revesting of property of the estate belongs to the debtor in a debt adjustment case, and not to the bankruptcy court. Consistent with bankruptcy law that is well-established in other contexts, a provision delaying revesting should be approved only when it serves some valid bankruptcy purpose. The principle that the broad and general powers of bankruptcy may only be exercised in service of a valid bankruptcy purpose is deeply rooted; indeed, it has been commented upon in positive fashion (although not expressly adopted) by the

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224 *Id.*
225 *Id.* at 557.
226 *Id.*
227 *In re* Cherry, 963 F.3d 717, 718 (7th Cir. 2020).
228 *See id.*
229 *Id.*
230 *Id.* at 719.
231 *Id.*

Supreme Court.[232] Ordinarily, establishing a valid bankruptcy purpose will require the debtor to meet the standard set forth in *Heath*: a showing that retention of property within the estate is necessary to fulfilment of the plan.

A. *The Holder of the Power to Delay Revesting*

There is considerable lack of clarity as to whether the power to propose departures from the default rule of revesting—whatever that default rule is assumed to be—belongs to the debtor or the bankruptcy court. One hint is found in chapter 13, which uses highly standardized forms. The new national model chapter 13 plan, effective as of December 2017,[233] but only adopted by roughly a dozen bankruptcy courts, appears on its face to grant that choice to debtors.[234] Part 7 of the model plan instructs the debtor to choose from three options: property of the estate will vest in the debtor upon plan confirmation; property of the estate will vest upon entry of the discharge; or some other alternative that the debtor specifies.[235] The relevant Committee Note, however, jettisons any clarity that might be provided by the text of the model plan by stating that the debtor's choice "is subject to a contrary court order under Code § 1327(b)."[236] Consistent with that approach, some bankruptcy courts in chapter 13 cases have used form plans or confirmation orders that make the revesting choice for debtors.[237] And when debtors have attempted to depart from a court's preferred choice,

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[232] Czyzewski v. Jevic Holding Corp., 137 S. Ct. 973, 985 (2017).

[233] U.S. COURTS, OFFICIAL FORM 113, available at http://www.uscourts.gov/forms/individual-debtors/chapter-13-plan.

[234] Bankruptcy courts that have not adopted the national model plan use their own standardized forms. Daniel Gill, *No Thanks: Most Districts Opt Out of National Chapter 13 Plan*, BLOOMBERG LAW (Dec. 1, 2017), https://www.bna.com/no-thanks-districts-n73014472651/.

[235] *See* U.S. COURTS, OFFICIAL FORM 113, available at http://www.uscourts.gov/forms/individual-debtors/chapter-13-plan.

[236] U.S. COURTS, COMMITTEE NOTES ON OFFICIAL FORM 113, Part 7, available at http://www.uscourts.gov/sites/default/files/b_113_cn_0.pdf.

[237] *See, e.g.*, *In re* Henneghan, 2009 Bankr. LEXIS 2553, at *4 n. 1 (Bankr. D.D.C. 2009) ("In this district, this vexing issue [of whether, by default, the estate terminates on confirmation] is largely moot because, since several years ago, the court's usual chapter 13 confirmation order routinely postpones vesting under § 1327(b) until the entry of the discharge order."); *In re* Boyd, 2020 Bankr. LEXIS 1954, at *33 (Bankr. D.S.C. 2020) (concluding that the Seventh Circuit correctly stated the default rule of estate termination in chapter 13, but that "[t]his District has opted out of the § 1327(b) and (c) vesting provisions", and explaining that neighboring bankruptcy courts in the Western and Middle Districts of North Carolina have done similarly); U.S. COURTS, LBF-M CHAPTER 13 PLAN, U.S. Bankruptcy Court for the District of Maryland ¶ 8, available at https://www.mdb.uscourts.gov/sites/default/files/LBF_M_1217_0.pdf, ("Title to the Debtor's property shall revest in the Debtor when the Debtor is granted a discharge pursuant to 11 U.S.C. § 1328 . . ."); U.S. COURTS, FORM BTXN222 – CHAPTER 13 PLAN, U.S. Bankruptcy Court for the Southern District of Texas at p. 11 (effective July 1, 2017), available at https://www.txnb.uscourts.gov/forms/btxn222-chapter-13-plan-new-form-effective-712017 ("Property of the estate shall not vest in the Debtor until such time as a discharge is granted or the Case is dismissed or closed without discharge.").

bankruptcy judges have not been slow to rein the debtor in. One bankruptcy court, therefore, observed that:

> the Bankruptcy Code provides [debtors] with no absolute right to vesting of property prior to discharge, and, if the Court orders otherwise, property of the estate does not vest in them upon confirmation. In the instant case, the Court ordered otherwise, consistent with practice in this jurisdiction for the past five years. The orders of confirmation were not inconsistent with their right to propose plan provisions, including vesting. The Court, however, is not required to confirm a plan which calls for vesting under the provisions of § 1327(b), particularly in view of the First Circuit's decision in *Barbosa v. Solomon*.[238]

Another bankruptcy court, relying on section 1327(b)'s provision, concluded that the Code "clearly reserves in the bankruptcy court the power to determine when property of the estate shall vest in the debtor, so the latter half of § 1327(b) works as a gap-filler for when the confirmation order or the plan does not treat this issue."[239]

It is hard to justify replacing the default rule of estate termination with their own different and preferred approach to revesting property of the estate, as some bankruptcy courts have.[240] To the extent that the Code provides any discretion to depart from that presumption of revesting, that discretion must belong to the debtor, not the bankruptcy court. Courts that make that decision for all debtors that come before them are making an essentially legislative judgment. In effect, chapter 13 is transmuted into a dramatically different statute on a district-by-district basis. It is certainly true that divergent local practices have been a persistent feature of the law of chapter 13 for many years.[241] But differences in varying mechanics of chapter 13—such as whether chapter 13 plans are funded by direct payments of the debtor or via wage garnishment orders,[242] or whether routine confirmation hearings are presided over by the bankruptcy judge or the

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238 *In re* Smith, 334 B.R. 26, 39 (Bankr. D. Mass. 2005). *Barbosa* adopted the estate reconciliation approach, but noted as to the debtor's prepetition property that "in spite of the 'vesting' provided by section 1327 of the Code, until all payments due under the plan are made, both the trustee and the unsecured creditors have an interest in the preservation of the debtor's financial situation." Barbosa v. Solomon, 235 F.3d 31, 36–37 (1st Cir. 2000).

239 *In re* Moore, 312 B.R. 902, 908 (Bankr. N.D. Ala. 2004).

240 *See In re Boyd*, 2020 Bankr. LEXIS 1954, at *35.

241 *See* Greene, Patel & Porter, *supra* note 2, at 1034–35 (describing scholarship on "local legal culture" and chapter 13, beginning with the 1994 article from Sullivan, Warren, and Westbrook) (citing to Teresa Sullivan, Elizabeth Warren & Jay Westbrook, *The Persistence of Local Legal Culture: Twenty Years of Evidence from the Federal Bankruptcy Courts*, 17 HARV. J.L. & PUB. POL'Y 801 (1994)).

242 *See* Greene, Patel & Porter, *supra* note 2, at 1036.

chapter 13 trustee[243]—should not provide a basis for varying basic structural principles of bankruptcy law. Nor, as debt adjustment bankruptcies are made available to new classes of debtors, is there reason to conclude that Congress intended such fundamental differences based solely on the debtor's location.

Even setting aside such structural concerns, I do not believe that bankruptcy courts should make the revesting choice for debtors. At root, those courts who do deviate from the norms of traditional chapter 11 do so for paternalistic reasons. Yet a debtor who commences a bankruptcy case should never be in doubt about whether he will recover full rights to all his property once he has struck his bargain with prepetition creditors, and thus has secured court approval for a plan. As Section II explains, adopting any different revesting rule may seriously constrains the debtor's ability to deal with his own property; regardless of how diligent he is in making his plan payments, he may still be precluded from buying a car, selling investment property, or even taking a vacation, without first securing trustee or court approval. The Seventh Circuit in *Heath* may have overstated the case in observing that the five-year guardianship effected by preserving the entire bankruptcy estate would reduce "[t]he legal situation of the debtor … to that of a child, a mental incompetent, or a married woman in the era of coverture."[244] But bankruptcy courts are nonetheless well aware that some debtors chafe at restrictions imposed upon their management of their own post-confirmation affairs.[245] The highly paternalistic view of courts that impose estate preservation upon chapter 13 debtors against their wishes implies that courts must be "gatekeepers" of chapter 13 debtors' affairs. This is unlikely to promote successful reorganizations in chapter 13. Chapter 13 is, after all, entirely voluntary, and over-intrusive management of individual debtors' lives may simply prompt the debtor to dismiss their bankruptcy case.[246] Any discretion provided to the bankruptcy court should not include the ability to impose such constraints upon a debtor against his wishes.[247]

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[243] Professor Melissa Jacoby has described this practice of some courts in past work. Melissa Jacoby, *Superdelegation and Gatekeeping in Bankruptcy Courts*, 87 TEMPLE L. REV. 875, 887–89 (2015).

[244] *In re* Heath, 115 F.3d 521, 523 (7th Cir. 1997).

[245] *See In re* Ward, 546 B.R. 667, 679 (Bankr. N.D. Tex. 2016) (ordering debtor to return vehicle she had purchased post-confirmation with post-confirming earnings and observing that "this court believes that the Chapter 13 trustee and court are required to be gatekeepers on post-confirmation activities, to some extent, such as a Chapter 13 debtor's desire to purchase a car during her case.").

[246] Thus, in the *Ward* bankruptcy, the court expected that the debtor would voluntarily dismiss her bankruptcy case in light of the court's ruling that the debtor was required to return a vehicle purchased with property of the estate. *Id.* at 681. Apparently viewing that outcome as unsatisfactory, the bankruptcy court ordered that, should the debtor do so, she would be subject to a 180-day bar before the case could be refiled. *Id.*

[247] Carlson similarly concludes that "the confirmation order must achieve what the debtor legitimately wants, free of coercion by the court or trustee." Carlson, *supra* note 9, at 246.

The argument against forcing a delay in revesting upon a debtor is even stronger in business cases outside the context of chapter 13. Requiring debtors frequently to resort to the bankruptcy court may impose costs that the debtor is not well placed to bear.[248] Each interaction with the bankruptcy court will cost both time, as it waits for court approval, and money, as it pays for attorneys to represent it before the court. The case for paternalistic oversight of its affairs is also weaker than with a consumer debtor. Small businesses are already subject to extensive regulatory oversight which does not need to be supplemented by long-term bankruptcy court scrutiny. Moreover, to the extent that a bankruptcy court believes a business's prospects to be so poor that it cannot survive unless its affairs are overseen by the court in this way, it is likely that the business is a poor candidate for reorganization in the first place. Rather than confirming a plan that holds the business's assets in the estate, the bankruptcy court should consider whether business's assets would be put to better use if they were transferred or sold and a new manager allowed to take over.[249]

B. The Scope of the Power to Delay Revesting

Any discretion created by the Code to delay revesting of property of the estate, properly understood, belongs to debtors, not judges. Next at issue is the extent of that discretion: Is it an unqualified discretion that permits the debtor to choose, in each individual case, the revesting rule that suits him best? Or may the default presumptive rule that property of the estate revests in the debtor upon plan confirmation be disturbed only under more limited circumstances?

1. Valid Bankruptcy Purpose

The discretion of the debtor must be limited. A debt adjustment plan may not retain property within the estate unless doing so serves some appropriate purpose consistent with the goals of bankruptcy. The notion that broad and general discretionary powers contained with the Code may be exercised only for an appropriate purpose is long rooted.[250] The bankruptcy process affords debtors

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248 *See In re* McLendon, 506 B.R. 243 (Bankr. N.D. Miss. 2013); *In re* LaRosa Greenhouse, 565 B.R. 304, 311 (Bankr. D.N.J. 2017) (bankruptcy court approval required for fees for post-confirmation services provided by attorney in chapter 12 case); *In re* Brandenburger, 145 B.R. 624 (Bankr. D.S.D. 1992) (similar).

249 The bankruptcy court should confirm a plan only if it is feasible—that is, it does not believe the plan will likely be followed by liquidation or a later reorganization. 11 U.S.C. § 1129(a)(11) (2019).

250 Nor is the principle that discretion conferred by the text of a statute comes with constraints and may be exercised only for appropriate purposes limited to bankruptcy. *See, e.g.*, Blanchard v. Bergeron, 489 U.S. 87, 89 n. 1, 95 (1989) (for statutes stating that court "may" allow attorneys' fees, "that discretion is not without limit" and fees ordinarily "should" be allowed to a prevailing party to give effect to the purposes behind the statute); United States v. Olano, 507 U.S. 725, 735–36 (1993) (FED. R. CRIM. P. 52(b), allowing for plain error review of

a great deal of flexibility, including the ability to craft plans or other schema incorporating a wide range of provisions crafted to suit a debtor's individual circumstances. Rather than conclude that discretion-conferring provisions allow the debtor unconstrained freedom to reorder their affairs, courts conclude that the Code's provisions may only be used in a manner consistent with the broader statutory scheme and that reflect a valid bankruptcy purpose. Most prominently, this principle was recently reaffirmed by the Supreme Court in *Jevic*.[251] The issue in *Jevic* was whether distributions to creditors on account of their prepetition claims deviated from the ordinary scheme of priorities applicable to a chapter 11 plan.[252] The Supreme Court tacitly approved some categories of such distributions—such as orders entered early in chapter 11 cases that permit the debtor to pay the prepetition wage claims of its employees, or claims of prepetition vendors whose continued business is vital to the company—on the theory that such distributions serve "significant Code-related objectives."[253] The priority-violating distributions at issue in *Jevic*, however, were impermissible because they did not serve a proper bankruptcy purpose.[254]

Lower court decisions have set forth similar principles. The Seventh Circuit's decision in *In re Sadler*—a decision cited approvingly by the Supreme Court in *Jevic*—interpreted the scope of the flexibility conferred upon debtors by section 349, the provision governing the effect of a dismissal of a bankruptcy case. [255] The debtors in *Sadler*, who ran a family farm, defaulted on a loan, causing a creditor to file suit and obtain a prejudgment attachment against their crops.[256] The debtors subsequently filed a chapter 13 bankruptcy case; during

a criminal judgment, "is permissive not mandatory" but exercise of discretion must be "guide[d]" and errors "should" be corrected if they seriously affect the fairness of a proceeding); Price v. Pelka, 690 F.3d 98, 101 ("The language of section 1988 is permissive, therefore, an award of attorneys' fees is discretionary. . . . Although the language of section 1977 is permissive, the court must exercise its discretion consistent with the congressional purpose underlying the statute."); Travelers Ins. Co. v. La. Farm Bur. Fed., Inc., 996 F.2d 774, 778 (5th Cir. 1993) (discretion to decide whether or not to dismiss a declaratory judgment action is "broad [but] not unfettered" and may not be exercised "on the basis of whim or personal disinclination" but must instead "address[] and balance[] the purposes of the Declaratory Judgment Act and the factors relevant to the abstention doctrine"); Serco Servs. Co. v. Kelley Co., 51 F.3d 1037, 1039 (Fed. Cir. 1995) (similar); Speed v. JMA Energy Co., 872 F.3d 1122, 1128 (10th Cir. 2017) (finding that the district court's discretion pursuant to Class Action Fairness Act to decline to exercise jurisdiction over a class action is not unfettered but must be guided by statutory factors).

[251] Czyzewski v. Jevic Holding Corp., 137 S. Ct. 973 (2017).

[252] *Id.* at 978.

[253] *Id.* at 985.

[254] *Id.* at 985–86 (violation of priority rules lacked "any significant offsetting bankruptcy-related justification").

[255] *In re* Sadler, 935 F.2d 918, 918–21 (1991); *Jevic*, 137 S. Ct. at 985 (quoting *In re Sadler*, 935 F.2d at 918–21).

[256] *In re Sadler*, 935 F.2d at 919.

that case, the bankruptcy court entered an order avoiding the prejudgment lien.[257] After the Sadler's bankruptcy case had been proceeding for some months, chapter 12 of the Code, which was specifically designed to promote the reorganization of family farms, went into effect.[258] The Sadlers believed they would be better off in chapter 12, but the Code—as it existed at that time—prohibited conversion from chapter 13 to chapter 12.[259] Instead the Sadlers dismissed their chapter 13 case and filed a new chapter 12 bankruptcy case. Concurrently, they successfully moved the bankruptcy court to enter an order keeping in effect the avoidance of the lien, even though dismissal would normally unwind such avoidance actions.[260] To be sure, the Code expressly contemplates flexibility in such circumstances: the ordinary effects of dismissal, including the vacatur of orders avoiding liens, may be modified "for cause."[261] But "'[c]ause' under § 349(b) means an acceptable reason. Desire to make an end run around a statute is not an adequate reason."[262] In short, the flexibility inherent in the Code may be exercised only to serve an appropriate purpose.

Nor, in this case, does the requirement for a valid bankruptcy purpose lack support from the text of the Code. Each form of debt adjustment bankruptcy provides a textual hook for this requirement in mandating that a plan must be proposed in good faith.[263] It has been established in chapter 11 that the good faith standard requires the showing of a valid bankruptcy purpose. Any chapter 11 case, for example, is subject to dismissal if not filed in good faith.[264] Again, leading decisions interpreting that requirement make clear that the core of that inquiry is whether the bankruptcy petition serves a valid bankruptcy purpose.[265] And chapter 11's parallel to section 1325(a)(3), section 1129(a)(3) (which governs both traditional chapter 11 plans and debt adjustment plans under subchapter V), has similarly been held to require that a proposed chapter 11 plan "will fairly achieve a result consistent with the objectives and purposes of the

257 *Id.*

258 *Id.*

259 *Id.* at 920.

260 *Id.* at 919.

261 11 U.S.C. § 349(b) (2019).

262 *In re Sadler*, 935 F.3d at 921.

263 11 U.S.C. §§ 1325(a)(3), 1225(a)(3), 1129(a)(3).

264 *In re* SGL Carbon Corp., 200 F.3d 154, 159–62 (3d Cir. 1999).

265 *Id.* at 165–66 (lack of good faith where "absence of a valid reorganizational purpose"); *see In re* 15375 Memorial Corp., 589 F.3d 605, 618–19 (3d Cir. 2009) (affirming dismissal of petitions because "Debtors were not seeking Chapter 11 protection of a valid bankruptcy purpose, but instead were using the filings as a litigation tactic"); *see also* Carolin Corp. v. Miller, 886 F.2d 693, 701 (4th Cir. 1989) ("overall aim" of good faith inquiry must be "to determine whether the purposes of the Code would be furthered by permitting the Chapter 11 petitioner to proceed").

Bankruptcy Code."[266] Courts will thus decline to confirm chapter 11 plans that contain provisions not appropriately directed toward a valid bankruptcy purpose.[267]

In addition to finding both deep roots in bankruptcy jurisprudence and an appropriate textual hook, there are good policy reasons for identifying a valid bankruptcy purpose requirement before property may be retained within the estate post-confirmation. The Code unambiguously provides for close supervision and protection of property of the estate in the pre-confirmation world.[268] Until the debtor confirms a debt adjustment plan, his assets are preserved within the bankruptcy estate for the benefit of creditors. The automatic stay serves to protect those assets, and bankruptcy court and trustee supervision prevents the debtor from dissipating them.[269] Meanwhile, disputes regarding those assets are funneled into the bankruptcy court for resolution. Once the debtor has confirmed a plan, a bargain has been struck with creditors.[270] Thus, in the post-confirmation world, bankruptcy court control over all of the debtor's assets is not required. The debtor's obligations to prepetition creditors extend only to meeting his obligations under the plan. The bankruptcy court's jurisdiction, in turn, is appropriately limited to supervising and enforcing the terms of the plan.[271]

To follow the principle of cases like *Jevic* and *Sadler*, the bankruptcy court must come up with some other valid bankruptcy purpose before it may conclude that property may be preserved within the bankruptcy estate. And it appears, given the limited jurisdiction of the bankruptcy court, that no such valid

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266 *In re* Combustion Eng'g, Inc., 391 F.3d 190, 247 (3d Cir. 2004); *see In re* Vill. at Camp Bowie I, L.P., 710 F.3d 239, 247 (5th Cir. 2013) (good faith requirement met where plan "proposed with the legitimate and honest purpose to reorganize").

267 *See, e.g.*, *In re* GAC Storage Lansing, LLC, 465 B.R. 174, 201–02 (Bankr. N.D. Ill. 2013) (plan's improper purpose to secure injunction protecting non-debtor guarantor rather than maximize debtor's value meant not proposed in good faith); *In re* Noll, 172 B.R. 122, 124 (Bankr. M.D. Fla. 1994) (plan not proposed in good faith based on inclusion of economically unjustifiable release of debtor's claims against creditor); *In re* UVAS Farming Corp., 91 B.R. 579, 581 (Bankr. D.N.M. 1988).

268 *See* 11 U.S.C. § 541 (2019).

269 *Id.* §§ 362, 363.

270 *See In re* Murphy, 474 F.3d 143, 148 (4th Cir. 2007) ("A confirmed Chapter 13 plan is 'a new and binding contract, sanctioned by the court, between the debtors and their pre-confirmation creditor[s].'") (quoting *In re* Penrod, 169 B.R. 910, 916 (Bankr. N.D. Ind.1994)); *In re* Harvey, 213 F.3d 318, 321 (7th Cir. 2000); *In re* Oparaji, 698 F.3d 231, 238 (5th Cir. 2012) (finding a chapter 13 plan is an "exchanged for bargain between the debtor and the debtor's creditors"); *In re* Forte, 341 B.R. 859, 869–70 (Bankr. N.D. Ill. 2005) (discussing "contract between a debtor and creditors formed by confirmation of the chapter 13 plan.").

271 *In re* Craig's Stores of Tex., Inc., 266 F.3d 388, 390 (5th Cir. 2001) (holding in chapter 11 case that "[a]fter a debtor's reorganization plan has been confirmed, the debtor's estate, and thus bankruptcy jurisdiction, ceases to exist, other than for matters pertaining to the implementation or execution of the plan.").

bankruptcy purpose is served by delaying the revesting of all estate property until the conclusion of the bankruptcy estate. Rather, the effects of such a delay in revesting are inconsistent with the proper working of bankruptcy law. On the one hand, as we have seen, delaying revesting vitiates the fresh start that the debtor would otherwise obtain upon plan confirmation by continuing to subject all of the debtor's financial affairs to bankruptcy court supervision until the completion of the debtor's plan payments. On the other hand, delaying the revesting of all property of the estate contravenes the Code by providing a debtor with unwarranted protection from postpetition creditors. When the revesting of property of the estate is delayed, that property continues to be subject to the automatic stay as provided for by section 362(a)(3) of the Code, prohibiting acts to exercise control over property of the estate. Indeed, debtors in chapter 13 cases have been recommended to delay revesting to engage this protection.[272] The *Steenes* and *Cherry* litigation concerned precisely this: debtors who sought to delay revesting of property of the estate to protect the city of Chicago from enforcing postpetition traffic penalties by towing the debtors' cars.[273]

Expanding the automatic stay in this manner is inconsistent with the structure of the Code. Although the Code carefully regulates the relationship between a debtor and his prepetition creditors throughout the bankruptcy case, it does not seek to protect debtors from their postpetition creditors. The

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[272] *See supra* notes 178–180, 220–229 and accompanying text.

[273] *Steenes I*, 918 F.3d 554, 558 (7th Cir. 2019); *In re* Cherry, 963 F.3d 717, 719 (7th Cir. 2020). Chicago's practices in enforcing its traffic enforcement laws have been harshly criticized. *See, e.g.*, Melissa Sanchez & Sandhya Kambhampati, *How Chicago Ticket Debt Sends Black Motorists into Bankruptcy*, PRO PUBLICA (Feb. 27, 2018), https://features.propublica.org/driven-into-debt/chicago-ticket-debt-bankruptcy/. I do not write this Article to defend the City's choices in enforcing its traffic laws; indeed, Chicago itself has recognized that many of its historic practices require reform. *See generally Driven into Debt: How Tickets Burden the Poor*, PRO PUBLICA, https://www.propublica.org/series/driven-into-debt (last accessed Nov. 1, 2020) (collecting articles describing reforms to Chicago's traffic laws and policies). Regarding the broader debate over Chicago's traffic debt, I make only one point in this Article: that debtors cannot, at least by default, use the automatic stay in a pending bankruptcy case to shield a car from actions the City wants to take to enforce a ticket issued after the commencement of the bankruptcy case. There may be special cases in which such protection is justified, but likely not every case will qualify, and the protection of the stay should not apply as a matter of course. *See In re* Heath, 115 F.3d 521, 524 (7th Cir. 1997); *In re Cherry*, 963 F.3d at 719; *Steenes I*, 918 F.3d at 558. To be sure, that may harm some individual debtors. As I have explained, my normative view of debt adjustment bankruptcy assumes that debtors must pay all their ordinary go-forward expenses while they remain in bankruptcy. *Supra* notes 191–192 and accompanying text. The moral force of that argument is diminished in cases in which debtors are subject to unjust debt collection efforts of any type. Thus, to the extent that debtors in Chicago—or elsewhere—seek relief from unfair or heavy-handed traffic enforcement, chapter 13 may seem like a lifeline that may save their cars. But using bankruptcy in this way has to be, at a minimum, a second-best solution to reform or regulation of the underlying debt collection practices. In addition to being legally questionable, for the reasons I have outlined, it is not clear that debtors actually end up better off; temporarily unenforceable postpetition traffic fines and penalties will continue to pile up during the bankruptcy case and will likely mean that the debtor loses her car as soon as the case is over. *See Steenes I*, 918 F.3d at 558.

automatic stay, for example, enjoins "any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case," but does not enjoin postpetition creditors from taking such actions.[274] Nor is the stay intended to insulate debtors from collection efforts made by postpetition creditors. Absent special circumstances, postpetition creditors are not provided for by a debt adjustment plan.[275] The debtor is expected to meet his obligations to postpetition creditors in the ordinary course throughout the period in which he is making his payments under the plan to repay prepetition creditors. That also is implicit in the Code's structure: the debtor commits only his projected disposable income to the plan (and may modify the plan if his disposable income changes post-confirmation). Calculation of a debtor's disposable income takes account of the debtor's expected postpetition expenses.[276] Preserving property within the bankruptcy estate, however, prevents postpetition creditors from actually seeking to collect on their claims and is in contravention to the statutory scheme.[277] Notably, Carlson has criticized theories of chapter 13 that preserve the chapter 13 estate by default precisely because they serve to expand the automatic stay and inhibit collection attempts by postpetition creditors.[278] For exactly the same reason, a debtor in a debt adjustment case should not be permitted to elect to preserve the estate, in an attempt to secure stay protection at the expense of his postpetition creditors.

There is a further troubling effect to permitting debtors to delay the revesting of property of the estate until discharge, dismissal, or conversion of the case. Because the extent of the bankruptcy court's jurisdiction is largely tied to the scope of the bankruptcy estate, preserving the estate for the life of the plan vastly expands bankruptcy court jurisdiction.[279] Courts have warned against this

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[274] 11 U.S.C. § 362(a)(6) (2019).

[275] Section 1305(a)(1) allows tax creditors to file proofs of claim, and thus be paid under the plan, for taxes that fall due while the case is pending. *Id.* § 1305(a)(1). Section 1305(a)(2) allows postpetition creditors to file proofs of claim if they hold consumer debts against the debtor personally for property or services necessary for the debtor's performance under the plan. *Id.* § 1305(a)(2). There is no analog in chapter 12 or subchapter V.

[276] *Id.* §§ 1325(b)(2), 1225(b)(2), 1191(d).

[277] The Bankruptcy Court for the Northern District of Alabama reached a similar conclusion:

> If postpetition creditors can reach only debtors individually, but not property and wages that remain vested in the estate, then these creditors have no meaningful remedy while the case is pending unless they first obtain relief from the stay to pursue property of the estate before commencing state law collection remedies. Such a two-step process gives debtors, who leave all their property in the bankruptcy estate, unwarranted stay protection, and it imposes additional collection expenses and delays on postpetition creditors.

In re Jemison, 2007 Bankr. LEXIS 3107, at *7–9 (Bankr. N.D. Ala. 2007).

[278] Carlson, *supra* note 9, at 247–48.

[279] *Supra* pages 15–16 (discussing how bankruptcy court jurisdiction and the scope of the estate are intertwined).

outcome in chapter 11. The alternative is to "funnel virtually all litigation affecting [reorganized debtors] into a single federal forum."[280] A chapter 11 debtor is expected, post-confirmation, to "go about its business without further supervision or approval. The firm also is without the protection of the bankruptcy court. It may not come running to the bankruptcy judge every time something unpleasant happens."[281]

There is no reason to treat debtors in debt adjustment cases differently from those proceeding under traditional chapter 11. It is as untenable for bankruptcy jurisdiction to extend to all of the debtor's property post-confirmation in a chapter 13, chapter 12, or subchapter V case as it is for bankruptcy jurisdiction to extend to a traditional chapter 11 debtor's post-confirmation affairs. As Judge Posner explained in *Heath*, that would render the bankruptcy court the arbiter of "the dispute with the corner grocer."[282] One bankruptcy court forcefully rejected this possibility:

> [T]he retention of all property in the estate during the life of a case is not practical, and . . . would confer jurisdiction on the bankruptcy court and entangle it in even the pettiest of controversies and immerse the court in the day-to-day lives of debtors. For example, do the debtors in these cases intend for the Court to hear a dispute with the neighborhood grocer if the debtor is overcharged for an apple?[283]

Debtors certainly possess a degree of flexibility to shape the post-confirmation estate in a debt adjustment bankruptcy. But flexibility provided by the Code is not the same thing as license. A debtor's powers and privileges in bankruptcy must be exercised in good faith. The meaning of the good faith requirement—an overarching principle of bankruptcy generally—is that provisions incorporated in the plan must serve a valid bankruptcy purpose. That requirement governs provisions purporting to delay revesting of the estate, just as it does any other provision of the plan. And that requirement will substantially limit the circumstances in which revesting may be delayed.

2. *Necessity to Fulfillment of the Plan*

As the Seventh Circuit in *Heath* proposed, demonstrating a valid bankruptcy purpose for preserving the estate post-confirmation requires a showing that

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280 *In re* Boston Reg'l Med. Ctr., 410 F.3d 100, 106 (1st Cir. 2005).

281 Pettibone Corp. v. Easley, 935 F.2d 120, 122 (7th Cir. 1991).

282 *In re* Heath, 115 F.3d 521, 523 (7th Cir. 1997).

283 *In re* Jemison, 2007 Bankr. LEXIS 3107, at *20–21 (Bankr. N.D. Ala. 2007) (striking from chapter 13 plan provision that delayed revesting of all property of the estate).

property to be retained within the estate is necessary to the fulfillment of the plan.[284] The plan is the central feature of the post-confirmation world, and the key source of the debtor's obligations while the case remains pending. To the extent the debtor wishes to secure for himself or his property additional protections beyond those ordinarily afforded by the Code, those protections must be justified by their effect upon the debtor's ability to meet his plan obligations.

On this issue, the Seventh Circuit's decisions in *Steenes I* and *Cherry* do not provide helpful guidance. They observe that property may only be preserved within the estate for a "good, case-specific reason" without suggesting what kind of justification might suffice.[285] Implicit in the decisions seems to be that invoking the protection of the automatic stay will not count as a good reason for keeping property in the estate; the opinions describe the plans at issue as "sheltering scofflaws."[286] But it cannot be that a plan drafted to keep some property within the estate fails simply because the debtor's reason for preserving the estate is to secure the stay's protection. From the debtor's perspective, gaining the benefit of the stay as against postpetition creditors is really the only substantial benefit of keeping property within the estate. The other chief effect of preserving the estate is to require the debtor to seek court permission to make other-than-ordinary dispositions of assets; few debtors are likely to want to preserve the bankruptcy estate in order to impose that burden upon themselves.[287] If a finding that a debtor sought to secure the stay's protection were enough to doom a plan, then the ability for debtors to depart from the default rule would be read out of the Code entirely. There would be little, if anything, the debtor could propose that would meet the necessary hurdle.

Courts considering this question must therefore figure out for themselves what counts as a valid reason to preserve property within the bankruptcy estate. My suggestion is that the analysis should consider how compelling the debtor's reasons are for seeking this kind of special protection and for resorting to the bankruptcy court as a shield against postpetition creditors. As I discussed in Section II.A.5 above, the key protection provided by preserving the stay is procedural, rather than substantive. It affects the timing and forum of litigation over postpetition creditors' enforcement actions. In most cases, the debtor cannot secure absolute protection, because a bankruptcy court may grant unpaid postpetition creditors relief from the automatic stay or an administrative

[284] *In re Heath*, 115 F.3d at 524.

[285] *In re* Cherry, 963 F.3d 717, 719 (7th Cir. 2020).

[286] *Steenes I*, 918 F.3d 554, 558 (7th Cir. 2019).

[287] *See supra* pages 14–15 (discussing the role of the bankruptcy court for debtor's use of property post-confirmation).

expense. Meanwhile, it is not true that the debtor is entirely unprotected even in the absence of the estate. A debtor always has the right to challenge the validity of some collection effort in state court; for example, a debtor might sue an auto lender in state court that repossessed her car, arguing that the lender had miscalculated the balance due and the debtor had not really defaulted on the loan. The effect of preserving the estate is to funnel all such disputes into the bankruptcy court, and to ensure that they are resolved before, rather than after, postpetition creditors have taken some action to collect on unpaid debts. The best justification for preserving the stay is likely to come in cases in which this kind of after-the-fact challenge is insufficient, and it is essential to the debtor that any collection efforts are scrutinized in advance. In other words, the debtor should argue that collection efforts are likely to result in the immediate failure of the plan, such that the justifiability of the postpetition creditor's actions must be litigated in advance, rather than challenged after the fact in the ordinary course.

Precisely when such circumstances exist is likely to be a fact-dependent question. The standard appears clearly to be met if a plan provides that a specific piece of property will be liquidated to repay creditors. Once the property is gone, the debtor's ability to repay creditors vanishes, and the plan will fail. Before a postpetition creditor pulls the rug out from underneath the plan in this way, its claim and rights over the property ought to be subjected to appropriate review by the bankruptcy court (and the filing of a motion in the bankruptcy court may additionally prompt the debtor quickly to take steps toward working out this obligation). Similarly, if the debtor's ability to complete all plan payments is predicated on a specific piece of income generating property (such as a house from which the debtor receives rental income), that asset could be kept in the estate to ensure that the plan is not disrupted without appropriate cause.

To be sure, there will be some hard calls in implementing this standard. Debtors who seek broad post-confirmation protection from their postpetition creditors may argue that many of their key assets are necessary for them to continue making plan payments. Necessity, of course, is likely to be more clearly established in some cases than others. In a consumer case, a debtor who earns a major portion of her income driving a car for a ride-sharing service is likely to have a compelling argument that they cannot complete the plan without the vehicle, and thus should be able to justify retaining the vehicle within the bankruptcy estate. Other debtors may wish for the same protection for their vehicle simply because they drive it to and from work. The intention of this Article is not to require bankruptcy courts to hear extended testimony on such issues, or to make detailed findings of fact regarding, for example, how feasible it would be for a debtor who ordinarily drives to work instead to rely on public transit. Inquiries of this nature would be inconsistent with the "light touch" model of bankruptcy that I describe below, which seeks to minimize the debtor's encounters with the bankruptcy court.[288]

Rather, I expect that a proposed plan will pass muster if it identifies a specific asset that is to remain in the estate and recites some reason, compelling on its face, why the loss of that asset could immediately jeopardize the bankruptcy. That claim would be supported by a sworn declaration or some other attestation by the debtor—the kind of minimal evidentiary showing that is already extremely common in bankruptcy practice. In most cases, creditors are unlikely to object to these plan provisions and no litigation of any kind will ensure. After all, extending the stay chiefly impacts the enforceability of debts that do not yet exist at the time of plan confirmation. In some cases, there will be creditors who are already present at the time of plan confirmation and thus able to object to a plan provision keeping an asset within the estate. That may occur when a debtor has incurred an obligation between the time of filing a bankruptcy case and the confirmation of a plan, or is a repeat obligor of a specific creditor, such that the likelihood of some new debt arising during the plan period gives the creditor standing to object the plan. In these few cases, the creditor may challenge the debtor's recited reasons as to why keeping property in the estate is essential and, if it can supply evidence sufficient to controvert the debtor's testimony, that objection may be resolved by the bankruptcy court at the confirmation hearing.

The key advantages of this approach are certainty and predictability. For the debtor whose property needs the additional protection provided by the automatic stay, or whose affairs for some reason require greater supervision, the estate may remain open post-confirmation. But that will be the case only where specific language in the plan so provides. Because the retention of property within the estate is not self-executing, as with the estate transformation theory, the plan and confirmation order may provide guidance to the debtor and creditors as to precisely what assets are in the estate, and permit all parties to the bankruptcy case to understand their rights in respect of those assets. The plan will also articulate the basis for retention of property within the estate. Creditors who have grounds to challenge the debtor's decision in that respect will have the opportunity to raise that challenge at the time of plan confirmation and to force the debtor to justify his decision to depart from the default rule of revesting.

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[288] *See infra* Section IV.

IV. LIGHT-TOUCH BANKRUPTCY

To conclude, I will attempt to situate my view of the limited lifespan of the bankruptcy estate in a broader model of debt adjustment bankruptcy that I will call "light-touch bankruptcy." Light-touch bankruptcy law seeks to make bankruptcy cases as minimally burdensome for the debtor as possible. It assumes that the debtor will undertake the task of managing her own affairs, and thus seeks to afford her a financial "fresh start" at the earliest possible date. In so doing, the light-touch bankruptcy approach also attempts to make bankruptcy as simple and cheap as possible. One likely positive effect of this approach is to make bankruptcy cases easier to administer—a timely change given the expected waves of both business and consumer filings expected to follow the COVID-19 pandemic. From the perspective of the debtor, though, light-touch bankruptcy is very much conscious that debt adjustment bankruptcy exists as an alternative to a simple, speedy liquidation bankruptcy under chapter 7.[289] Debtors may emerge from chapter 7 proceedings after only a few short weeks or months immediately able to start a new financial life, freed of any restrictions attend to a bankruptcy filing, and unprotected by the bankruptcy court (save for the discharge of prepetition debt).[290] Debt adjustment bankruptcies, necessarily, take longer. But I posit that there is little need for them to be more intrusive for the debtor, or to presume that the debtor requires greater ongoing scrutiny or shielding from the bankruptcy court, than chapter 7 does. Light-touch bankruptcy, therefore, disagrees emphatically with bankruptcy courts that argue that their role is to be "gatekeepers on post-confirmation activities."[291]

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[289] Some chapter 13 debtors, of course, do not have the option of filing for bankruptcy under chapter 7. The means test created by Congress's 2005 bankruptcy reform legislation presumptively requires some above-median income debtors, who Congress believes to be most capable of repaying debts over time, to seek relief under chapter 13 rather than chapter 7. 11 U.S.C. § 707(b) (2019). I join with the many critics of the means test who have argued that it has largely failed to achieve what Congress wanted. *See* John Pottow et al., *Did Bankruptcy Reform Fail? An Empirical Study of Consumer Debtors*, 82 AM. BANKR. L.J. 349, 353 (2008). Perhaps more significantly, and certainly less justifiably, chapter 7 remains out of reach for many low income consumers that might benefit most from a speedy liquidation because consumer debtors' attorneys will typically require an upfront fee to file a chapter 7 case that is beyond the consumer debtor's means (while chapter 13 cases are often filed for no money down). *See* Pamela Foohey et al., *"No Money Down" Bankruptcy*, 90 S. CAL. L. REV. 1055 (2017); Pamela Foohey, *Access to Consumer Bankruptcy*, 34 EMORY BANKR. DEV. J. 341, 360–63 (2018).

[290] A small business that files a chapter 7 or other liquidation proceeding, of course, does not emerge from bankruptcy with a fresh start. But the entrepreneur owner of the small business is nonetheless freed by the speedy windup of her old business immediately to start a new one—as many choose to do. *See* Douglas G. Baird & Edward R. Morrison, *Serial Entrepreneurs and Small Business Bankruptcies*, 105 COLUM. L. REV. 2310, 2310–18, 2328–30 (2005).

[291] *In re* Ward, 546 B.R. 667, 679 (Bankr. N.D. Tex. 2016); *see supra* notes 243–244 and accompanying text.

Limiting the lifespan of the bankruptcy estate moves closer to a model of light-touch bankruptcy because it reduces the number of interactions between the debtor and the bankruptcy court. The shadow of the bankruptcy proceeding is reduced. Although it allows for exceptions, it assumes that once the debtor's plan is confirmed and his repayment obligations are crystallized, he will have no further recourse to the bankruptcy court. As this Article has explained, the debtor is not required to pay for an attorney to go into court on his behalf to seek permission to sell assets or make purchases, which the bankruptcy court may grant based on its view of whether the proposed transactions are financially wise or involve advantageous terms.[292] Even in cases in which the bankruptcy court approves the proposed transactions, the need for motions practice in such cases may cost a debtor hundreds of dollars on each occasion.[293] This Article proposes simply to do away with those costs in the post-confirmation world. Nor may the debtor ordinarily seek the aid of the bankruptcy court in disputes with new creditors that arise after the financial fresh start of plan confirmation. Although my view of the limited lifespan of the bankruptcy estate permits exceptions, presumptively the debtor must deal with those outside bankruptcy on the same terms as a consumer with no pending bankruptcy case, or a debtor already granted a chapter 7 discharge.

Light-touch bankruptcy, though, is broader than just the scope of the bankruptcy estate. Congress and the bankruptcy courts should be attentive to other ways that debt adjustment bankruptcy may be streamlined for debtors. To take a number of examples of what light-touch bankruptcy should mean: on an operational level, debt adjustment bankruptcy should continue the trend towards use of standardized forms that allow for cheaply prepared, off-the-shelf reorganization proceedings, and should, where possible, simplify filings that the debtor makes or receives after the earliest period of the bankruptcy case; bankruptcy courts should be skeptical of plan provisions, such as conduit mortgage payment plans, that take control of the debtor's ordinary financial affairs away from her;[294] and Congress should rigorously scrutinize mandates

[292] *See In re Ward*, 546 B.R. at 680 (declining to approve debtor's purchase of a car because proposed financing terms were "onerous and unfavorable" notwithstanding "some anecdotal evidence that [the terms] might be customary in the industry for individuals in financial distress.").

[293] *See id.* (describing typical fees in the Northern District of Texas).

[294] These are plan provisions or local rules that provide that the debtor's ongoing monthly mortgage payment during the plan period is to be paid by the chapter 13 trustee (who may receive the funds, along with the remainder of the debtor's plan payments, either via a wage garnishment order or a direct payment from the debtor), rather than directly by the debtor herself to the mortgage holder.) Although relatively common and endorsed as a best practice by many bankruptcy judges and professionals, AM. BANKR. INST., FINAL REPORT OF THE ABI COMMISSION ON CONSUMER BANKRUPTCY 184–87 (2019), one recent study suggested that they have no statistically significant impact one way or the other on plan completion rates. Greene, Patel & Porter, *supra*

such as the requirement in chapter 13 for credit counselling (before a bankruptcy case is commenced)[295] and personal financial management (before a discharge is granted)[296] to ensure these programs provide a sufficient benefit for debtors to justify the financial and time cost imposed upon debtors.[297] One welcome substantive change would be to amend the Code to change the rules for modification of confirmed plans in chapters 12 and 13 cases. Under current law, chapter 12 or 13 debtors may be brought back into bankruptcy court by a motion of the trustee or a creditor to modify the confirmed plan to increase the debtor's payments on the basis that her disposable income has increased in the period following plan confirmation.[298] Subchapter V has eliminated this possibility for small business debtors, permitting only the debtor to seek modification in order to reduce its plan payments.[299] Adopting that rule in chapters 12 and 13 not only permits the debtor to benefit from good fortune during the pendency of the case but also makes the plan period administratively more simple for both the debtor and trustee.[300]

Finally, while I do not claim that my model of bankruptcy follows necessarily from the insights that are at the heart of most recent bankruptcy scholarship, I note that light-touch bankruptcy is at least consistent with its most significant conclusions. Light-touch bankruptcy is normatively predicated on the notion that the substantial majority of debtors do not end up in bankruptcy because they are bad actors, or because they are unduly or unusually irresponsible in the management of their finances. Research beginning in the 1980s with the pathbreaking empirical work of Professors Elizabeth Warren, Jay Westbrook, and Theresa Sullivan has argued instead that bankruptcy is most

note 2, at 1076.

295 11 U.S.C. § 109(h) (2019).

296 *Id.* §§ 111, 727(a)(11), 1328(g)(1).

297 Most debtors do not appear to find these courses helpful. *See generally* Michael D. Sousa, *Just Punch My Bankruptcy Ticket: A Qualitative Study of Mandatory Debtor Financial Education*, 97 MARQ. L. REV. 391 (2013) ("only four out of the fifty-eight participants (6.90%) [] interviewed for this study found the mandated education courses helpful"); AM. BANKR. INST., FINAL REPORT OF THE ABI COMMISSION ON CONSUMER BANKRUPTCY 121–25 (2019) (noting widespread criticism of the utility of the pre-bankruptcy credit counseling requirement and proposing its elimination); *id.* at 125–26 (describing track record of debtor financial management course as "mixed at best," but not proposing repeal).

298 *See* 11 U.S.C. §§ 1229(a)(1), 1329(a)(1).

299 *Id.* § 1193.

300 Many of my suggestions for a new light-touch framework for debt-adjustment bankruptcy are consistent in theme with recent reform proposals, such as now-Senator Warren's bankruptcy reform plan to replace current chapter 7 and chapter 13 filing rules with a single, streamlined consumer bankruptcy filing process intended to make bankruptcy "simple, cheap, fast, and flexible." *Fixing our Bankruptcy System to Give People a Second Chance*, ELIZABETH WARREN, https://elizabethwarren.com/plans/bankruptcy-reform (last accessed Nov. 19, 2020).

frequently the product of unpredictable and frequently unavoidable financial setbacks, whether income shocks such as job losses or family separation, or expense shocks, such as medical treatment.[301] This research emphasizes that consumer bankruptcy in the United States frequently plays the role of social insurance, providing relief for financially distressed debtors that supplements that provided by more formal social insurance programs such as unemployment insurance or health insurance.[302] Bankruptcy law is not the resort for spendthrifts seeking to avoid paying too casually incurred debt; rather, it continues to carry very substantial social stigma, and many consumer debtors will suffer considerable financial hardship for long periods of time before turning to bankruptcy to address their problems.[303]

With this understanding of both of the purposes that bankruptcy law serves and of the types of debtors that most frequently end up in bankruptcy, a light-touch model of debt adjustment bankruptcy seems justifiable. Among consumer bankruptcy's gravest challenges today are barriers to access that prevent debtors from gaining effective relief. These are deep-rooted problems that do not admit of any easy solution. Even if the effect is felt only at the margins, simplifying and streamlining the bankruptcy process—and thus, potentially, making it cheaper—may do something to help promote wide access to bankruptcy. Meanwhile, given the profile of the typical chapter 13 debtor, it is at best questionable whether the potentially costly additional procedures that I have described add much value for debtors. There is little reason to believe that close scrutiny of consumer debtors by the bankruptcy courts is warranted as the price for admission to bankruptcy—and even less reason to suppose that to be the case for business debtors under other chapters of the Code.

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[301] TERESA A. SULLIVAN, ELIZABETH WARREN & JAY LAWRENCE WESTBROOK, THE FRAGILE MIDDLE CLASS: AMERICANS IN DEBT 6 (Yale University Press 2020).

> The debtors in our sample include accountants and computer engineers, doctors and dentists, clerks and executives, salesclerks and librarians, teachers and entrepreneurs. They are middle class folks . . . the first to succumb to difficulties that also face many of their fellow citizens. . . They are a silent reminder that even the most secure family may be a job loss, a medical problem, or an out-of-control credit card away from financial catastrophe.

Id. at 6; *see also id.* at 75–107 (discussing job loss as a cause of bankruptcy); 141–71 (discussing medical expenses as a cause of bankruptcy); 172–98 (discussing divorce as a cause of bankruptcy).

[302] *See* Adam Feibelman, *Defining the Social Insurance Function of Consumer Bankruptcy*, 13 AM. BANKR. INST. L. REV. 129, 129–31 (2005) (describing various forms of the claim that bankruptcy law functions as social insurance).

[303] *See* Pamela Foohey, *Access to Consumer Bankruptcy*, 34 EMORY BANKR. DEV. J. 341, 347–57 (2018).

CONCLUSION

Since the first years of the modern Code, courts have been divided on the scope of the post-confirmation estate in chapter 13. A four-way fracture among courts and commentators has developed, with each theory reflecting radically different understandings of the structure of chapter 13. As Congress has expanded the availability of debt adjustment bankruptcy, the dispute over the fate of the bankruptcy estate has reached beyond chapter 13. Most recently, it has become of pressing concern to bankruptcy courts who must preside over new small business cases under subchapter V of chapter 11. As a matter of text, structure, and purpose, the estate termination theory is the most persuasive of the various accounts of the lifespan of the bankruptcy estate. The estate termination theory aligns debt adjustment bankruptcy with traditional chapter 11 and gives full and appropriate effect to the Code's direction that property of the estate vest in the debtor upon confirmation of the plan.

Having established that the estate presumptively terminates upon confirmation of a debt adjustment plan, it is necessary to consider under what circumstances the plan or confirmation order may deviate from the default rule and preserve the estate. The power to propose a delay in the revesting of property of the estate after confirmation belongs to the debtor, rather than to the bankruptcy court. But it is a limited power. A debtor must be able to point to some valid bankruptcy law purpose before property can be retained within the estate. The usual justifications for preserving the estate post-confirmation—in particular, securing the protection of the automatic stay against postpetition creditors—do not suffice. Instead, such property must be necessary to the fulfillment of the plan, the landmark of the post-confirmation world. This approach appropriately preserves the debtor's post-confirmation freedom of action, ensures that postpetition creditors have an avenue to enforce their own rights outside of the bankruptcy case, and prevents the bankruptcy court from exercising unlimited jurisdiction over the debtor's post-confirmation affairs. Adopting this theory of the estate in debt adjustment bankruptcy cases will help shift bankruptcy law toward a light-touch approach will minimize the need for the debtor to interact with the bankruptcy court, and finally, will make the bankruptcy process as a whole cheaper and less burdensome for debtors.

By Hon. Elizabeth L. Gunn and Shelby Kostolni

Post-Petition Appreciation: Whose Line (Item) Is It, Anyway?

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Fluctuations in the value of real estate and personal property items occur often, resulting in the prediction of future value feeling like seeking the answer from a Magic 8 Ball. The fluid nature of real estate values is not solely an issue for real estate agents, homebuyers or homeowners; it also frequently arises in bankruptcy cases, especially consumer cases. Courts continue to struggle with and deepen a split of authority as to who has the right to the post-petition appreciation of a consumer debtor's real property: the debtor or the debtor's estate (and, thus, creditors). In considering the question, bankruptcy courts struggle with the intersection of two sections under chapter 13: 1306 (additions to § 541 property of the estate in chapter 13) and 1327 (effect of confirmation). Even considering the same sections, the answers continue to differ.

As eloquently stated in a recent case on the issue, "harmonizing the inharmonious is a tall order."[1] Most courts considering the issue have found that §§ 1306 and 1327 do not seamlessly fit together. Over time, four general approaches to reconcile §§ 1306 and 1327, and when and where property vests, have developed: (1) estate termination; (2) estate transformation/conditional vesting; (3) estate preservation; and (4) estate replenishment.[2] In addition, depending on the terms of any local form chapter 13 plan, some of these options may not be applicable in all jurisdictions. Before examining recent decisions from the Ninth Circuit and the U.S. Bankruptcy Court for the Eastern District of Michigan, it is helpful to understand each category.

Court Approaches to Vesting

Estate Termination

As generally accepted, the estate-termination approach results in all property vesting in the debtor at plan confirmation and the estate ceasing to exist.[3] This view is based on a reading of § 1327(b) that results in all property vesting in the debtor at confirmation.[4] The estate-termination approach attempts to harmonize § 1306(b)'s giving debtors possession of the property of the estate and § 1327(b)'s vesting of title and ownership by finding § 1327(b) to be the more specific, and thus controlling, section as to the ownership of appreciation of property in the estate.[5] However, in jurisdictions where the required local form plan provides for vesting only at discharge, this approach is inapplicable.

Estate Preservation/Conditional Vesting

In these substantially similar approaches, all property is deemed estate property until entry of discharge.[6] The theory of estate preservation is based on an interpretation of § 1327(b) finding that confirmation does not disturb the existence of the estate, only the debtor's responsibilities toward the property of the estate.[7]

Similarly, conditional vesting gives the debtor the right to use the property of the estate, but it is not a final right until the plan is complete and the debtor obtains a discharge.[8] These approaches rely on the premise that § 1327(b) does not remove property from the estate, but only places control of the property in the debtor pending the completion of the chapter 13 case.[9]

Estate Transformation

The estate-transformation approach is seen as a compromise between the extreme estate-termination and estate-preservation/conditional-vesting approaches.[10] It holds that at plan confirmation there is an estate transformation where all property of the estate becomes property of the debtor, except for post-petition income and property considered essential to the performance of the plan.[11] (However, this raises a new issue on how you define whether property is "essential" to performance of the plan, but that question is outside the scope of this article.)

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1 *In re Elassal*, 2023 WL 5537061, *4 (Bankr. E.D. Mich. 2023) (citing *City of Chicago v. Fulton*, 141 S. Ct. 585, 591 (2021)).
2 These approaches are very succinctly defined in *In re Baker*, 620 B.R. 655, 663-64 (Bankr. D. Colo. 2020).
3 *Baker*, 620 B.R. at 663.
4 *Calif. Franchise Tax Bd. v. Jones (In re Jones)*, 420 B.R. 506, 514 (B.A.P. 9th Cir. 2009) (citing *In re Petruccelli*, 113 B.R. 5, 15 (Bankr. S.D. Cal. 1990)).
5 *Petruccelli*, 113 B.R. at 15. *See also Oliver v. Toth (In re Toth)*, 193 B.R. 992, 996 (Bankr. N.D. Ga. 1996) (finding *Petruccelli* analysis most persuasive; policy reasons (being able to obtain credit and use property after confirmation) support concluding that vesting at confirmation ends the estate); *In re Dagen*, 386 B.R. 777, 782 (Bankr. D. Colo. 2008) (stating that "only the estate termination approach gives effect to the literal terms of § 1327(b)").
6 *Baker*, 620 B.R. at 664.
7 *Id.* at 663-64.
8 *Id.* at 664.
9 *In re Brensing*, 337 B.R. 376, 383 (Bankr. D. Kan. 2006) (citing *Sec. Bank of Marshalltown, Iowa v. Neiman*, 1 F.3d 687, 690 (8th Cir. 1993)).
10 *Telfair v. First Union Mortg. Corp.*, 216 F.3d 1333, 1340 (11th Cir. 2000) (citing *In re Heath*, 115 F.3d 521, 524 (7th Cir. 1997); *In re McKnight*, 136 B.R. 891, 894 (Bankr. S.D. Ga. 1992)).

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Estate Replenishment

Finally, the estate-replenishment approach results in all property of the estate becoming property of the debtor on confirmation, but the estate continues to exist and "refills" with property defined in § 1306 acquired by the debtor after confirmation.[12] The vesting in the estate of post-petition property is without regard to whether the property is necessary to the plan's performance.[13]

Recent Cases, Opposite Results

Two recent cases each faced the question of whether appreciated value of the debtor's real property was property of the estate or property of the debtor. In *In re Castleman*, the Ninth Circuit considered an appeal where the question was whether pre-conversion real estate appreciation belongs to the estate or the debtors who converted from a chapter 13 reorganization to a chapter 7 liquidation.[14] When the Castlemans originally filed for chapter 13, they listed their residence in their schedules with a value of $500,000 and a secured lien of $375,077, and claimed a homestead exemption in the $124,923 balance based on Washington's state exemptions.[15]

The Castlemans successfully made chapter 13 plan payments for 20 months, but after a job loss, the pandemic-deferred payments and a serious health diagnosis for John Castleman, they decided that they could no longer make their payments and converted to chapter 7.[16] The problem was that during the 20 months it took the Castlemans to make this determination, their home value had appreciated to approximately $700,000, leaving $200,000 of equity unprotected by their original homestead exemption.[17]

After conversion, the chapter 7 trustee moved to sell the home to recover the appreciated/unprotected value for the estate. The Castlemans objected to the sale on the basis that the post-petition appreciation value (*i.e.*, the "new" equity) was property of the debtor — not property of the estate.[18] In the Ninth Circuit, there is long-standing authority that even if a debtor amends the homestead exemption post-petition,[19] post-petition appreciation inures to the bankruptcy estate, not the debtor.[20] In other words, the Castlemans could not simply have increased their claimed homestead exemption (to the extent available) to exempt the new equity.

In its analysis, the court noted the potential benefits to debtors and creditors of a chapter 13 case: The ability for debtors to retain property while creditors receive a higher return than in chapter 7. The court noted that post-confirmation property of the estate is defined not by § 1306 (titled "Property of the Estate"), but rather by § 348(f) (titled, "Effect of Conversion," which explains converting from chapter 13 to another chapter). Under § 348(f), property of the estate after a good-faith conversion includes property that was part of the estate as of the petition date that remains in the possession or control of the debtor upon conversion.

Only in cases of bad-faith conversion does all property, whether acquired pre- or post-petition, become property of the chapter 7 estate. Because the appreciation was not "property" acquired post-petition, merely a change in valuation for pre-petition property, the court concluded that the appreciation was not a separate asset, and because it was part of pre-petition property, the appreciation belonged to the chapter 7 estate.[21]

Following closely on the heels of *Castleman*, in *In re Elassal* the U.S. Bankruptcy Court for the Eastern District of Michigan found that post-petition, nonexempted appreciation of real property belongs to the debtor in a chapter 13 case.[22] Wendy Elassal filed a chapter 13 petition in March 2021 in which she valued her home at $250,000, which was encumbered by $228,000 of liens.[23] She claimed a homestead exemption in the remaining $22,000 of value. Her ownership of the property was subject to three conditions arising from her pre-petition divorce: (1) her former spouse would make 24 monthly mortgage payments in lieu of child and spousal support; (2) she would sell or refinance the property on or before Dec. 31, 2022 (21 months after the petition date), to pay the former spouse's equity position; and (3) she would be responsible for any mortgage payments after Jan. 1, 2023.[24]

The debtor's chapter 13 plan, which provided for the sale of the home and included the exempt value in the liquidation analysis, was confirmed at the end of July 2021.[25] In February 2023, Elassal moved to sell the property for $435,000 and use all proceeds (the $22,000 exempted, plus approximately $171,000 of post-confirmation appreciation) to purchase a new residence without modifying her plan.[26] The chapter 13 trustee objected, arguing that Elassal should only be entitled to keep proceeds after payment in full of all her creditors.

The court described the situation as one that no party to the case could have predicted at confirmation — not the debtor, nor the trustee or the unsecured creditors. At confirmation, the debtor agreed to make a payment to creditors based on the liquidation analysis of whether her home appreciated or depreciated over the life of the plan. In considering whether the proceeds were property of the chapter 13 estate, the court compared the protections of chapter 7 vs. chapter 13. The court noted that while chapter 7 estates generally encapsulate appreciation, the standard is different in chapter 13.[27]

Next, the court recognized that many courts (including *Castleman*) have found that appreciation is property of the estate when a case is converted from chapter 13 to chap-

11 *Baker*, 620 B.R. at 664.
12 *Id.* at 663.
13 *Id.*
14 *In re Castleman*, 75 F.4th 1052, 1054 (9th Cir. 2023).
15 *Id.*
16 *Id.*
17 *Id.*
18 *Id.*
19 *See generally Wilson v. Rigby*, 909 F.3d 306 (9th Cir. 2018).
20 *Schwaber v. Reed (In re Reed)*, 940 F.2d 1317, 1323 (9th Cir. 1991).
21 *Castleman*, 75 F.4th at 1055-56.
22 *Elassal*, 2023 WL 5537061 at *1.
23 *Id.*
24 *Id.* at *2.
25 *Id.* at *10.
26 *Id.* at *2.

ter 7.[28] However, the court noted that chapter 13 cases "still present ... the best avenue for debtors to retain property in bankruptcy, and the unqualified right to dismiss their chapter 13 proceedings protects them from any adverse consequences of conversion to chapter 7."[29] The court further held that in chapter 13, "disposable income does not include prepetition property or its proceeds."[30] Ultimately, the *Elassal* court determined that the proceeds were not newly acquired property, thus they did not fall under the definition of property of the estate under § 1306, and Elassal could retain all sale proceeds while continuing to pay the dividend to creditors over the term of her originally confirmed plan.[31]

27 *Id.* at *6.
28 *Id.* (citing *In re Adams*, 641 B.R 147 (Bankr. W.D. Mich. 2022); *Coslow v. Reisz*, 811 Fed. App'x 980 (6th Cir. 2020)).
29 *Id.* at *6 (quoting *In re Adams*, 641 B.R. at 156).
30 *Id.* at *10 (citing *In re Burgie*, 239 B.R. 406, 410 (B.A.P. 9th Cir. 1999)).
31 *Id.* at *11.

Is Conversion the Key Factor?

On their face, the results in *Elassal* and *Castleman* appear to be in direct contradiction. However, at their core, these cases highlight the different results that may arise depending on the procedural history and current chapter of a debtor's case. The question of estate property is much clearer in unconverted cases. However, these definitions are complicated in converted cases, which does not mean that a party who is subject to a chapter 13 plan that they cannot afford to complete is without options.

As noted by the *Elassal* court, such debtors can seek to dismiss (or take actions that result in the dismissal of) the chapter 13 case and refile a chapter 7 petition. In that situation, it eliminates the question of whether the appreciation is or is not property of the estate. *Elassal* and *Castleman* highlight the fact that debtors need to consider the value of the property at all points during their case, particularly when considering whether to convert or dismiss. abi

SO ORDERED

SIGNED this 27 day of November, 2023.

Pamela W. McAfee
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF NORTH CAROLINA
FAYETTEVILLE DIVISION

IN RE:

DANIEL JAMES MAYNOR,

DEBTOR

CASE NO.
23-00958-5-PWM
CHAPTER 13

MEMORANDUM OPINION DENYING CONFIRMATION OF CHAPTER 13 PLAN

The matter before the court is the chapter 13 trustee's objection to confirmation of the debtor's second amended plan. A hearing took place in Fayetteville, North Carolina on September 7, 2023, at the conclusion of which the court denied confirmation from the bench. This memorandum opinion sets forth the reasons for the court's decision.

BACKGROUND

Daniel James Maynor filed a voluntary petition for relief under chapter 13 of the Bankruptcy Code on April 5, 2023. Joseph A. Bledsoe, III (the Trustee) is the standing trustee assigned to the case. Mr. Maynor filed his Schedules and Statements, D.E. 11, and his chapter 13 plan, D.E. 12, on April 13, 2023. The Trustee objected to the plan and sought dismissal of the case on May 12, 2023, based on the failure of Mr. Maynor to file tax returns for tax years 2021 and 2022. D.E. 14, 15. The initial hearing on confirmation and the motion to dismiss was continued from June 8, 2023 to July 11, 2023. Mr. Maynor filed an amended plan on June 19, 2023, D.E. 21 (the First Amended Plan), to which the Trustee objected on June 30, 2023, D.E. 22, based on failure to make plan payments, failure to file prepetition tax returns, and the inclusion of certain "nonstandard provisions" in Section 8.1 of the First Amended Plan, as follows:

> The liquidation test of 11 USC 1325(a)(4) assumes a 6% cost of sale for real property and a 10% cost of sale for personal property.
>
> Plan provision 7.2 shall not apply.
>
> EDNC LBR 4002-1(g)(4) shall not apply post-confirmation.
>
> Paragraph 10 of the Order and Notice to Chapter 13 Debtor issued on April 7, 2023 shall not apply.
>
> Upon confirmation, the Debtor's interest in 8016 Lane Road in Linden, NC shall no longer be property of the bankruptcy estate pursuant to 11 USC 1329(b)(9), 11 USC 1327(b) and plan provision 7.1.
>
> The Debtor shall not [be] required to file a notice pursuant to 11 USC 363(b) prior to selling any vested property.
>
> The debtor shall not be required to obtain a court order prior to selling any vested property.

D.E. 22 at ¶ 19 (citing the First Amended Plan, D.E. 21 at ¶ 8.1). As discussed more thoroughly below, the nonstandard provisions generally seek to excuse Mr. Maynor from the requirement that the debtor obtain court authority to sell a residence postconfirmation. The Trustee's objection noted that the mortgage lien and debtor's exemption on the real property identified in the nonstandard provisions, when compared to the scheduled fair market value of the property, resulted in no net equity in the real property for the estate.

The July 11, 2023 hearing on confirmation was continued to August 10, 2023, D.E. 24, and an interim consent order was entered on the Trustee's motion to dismiss, D.E. 27, with the motion to dismiss also continued to August 10, 2023. At that hearing, the parties agreed to continue both the motion to dismiss and the Trustee's objection to confirmation to September 7, 2023, in order to resolve the issues regarding the outstanding tax returns. At that same hearing, the court forecast to counsel that it would be willing to consider excusing Mr. Maynor from the requirements to seek court authority to sell his residence based on the specific facts of the case (namely, the lack of net equity for the estate), but would not excuse compliance based on Mr. Maynor's inclusion of the nonstandard provisions in the First Amended Plan, nor based on the debtor's election to have his property "vest" at confirmation. The parties indicated they could likely agree to some plan language to accomplish this.

Two days later, Mr. Maynor filed another amended plan, D.E. 32 (the Second Amended Plan), in which the original nonstandard provisions were not only retained, but significantly expanded. This plan contains the following revised nonstandard provisions, with changes from the First to the Second Amended Plan highlighted in italics, and redactions shown by strikethrough:

> a. The liquidation test of 11 USC 1325(a)(4) assumes a 6% cost of sale for real property and a 10% cost of sale for personal property.
>
> b. Plan provision 7.2 shall not apply. *This is a deviation from the EDNC Local Form Plan in order to avoid conflict with the Debtor's rights pursuant to 11 USC 1321, 11 USC 1322(b)(9), and 11 USC 1327(b).*
>
> c. EDNC LBR 4002-1(g)(4) shall not apply post-confirmation *to the real property located at 8016 Lane Road, Linden, NC 28356 because the property is not non-exempt and post-confirmation it will not be property of the bankruptcy estate*.
>
> d. Paragraph 10 of the Order and Notice to Chapter 13 Debtor issued on April 7, 2023 shall not apply *to the real property located at 8016 Lane Road, Linden, NC 28356 because the property is not non-exempt and post-confirmation it will not be property of the bankruptcy estate*.
>
> *e. The Debtor must notify his attorney and the trustee of any change of address or if he experiences a substantial change in his property ownership.*
>
> f. Upon confirmation, the Debtor's interest in 8016 Lane Road in Linden, NC shall no longer be property of the bankruptcy estate pursuant to 11 USC 1329(b)(9), 11 USC 1327(b) and plan provision 7.1.
>
> g. The Debtor shall not [be] required to file a notice pursuant to 11 USC 363(b) *or Federal Bankruptcy Rule 6004(a)* prior to selling ~~any~~ vested property.

> h. The debtor shall not be required to obtain a court order prior to selling any vested property.
>
> *i. If the Debtor seeks to sell, lease or use estate property outside the ordinary course during the pendency of the case (e.g. property of the kind described in 11 USC 541(a)(5)), then he shall comply with the requirements of 11 USC 363(b), 11 USC 1303 and Fed Bankr Rule 6004 but shall not be required to comply with EDNC LBR 4002-1(g)(4). This provision is intended to identify the proper procedural mechanism that is applicable and avoid neglect and/or duplication with regard to any substantive or procedural requirement.*

D.E. 32 at ¶ 8.1. The Trustee again objected to confirmation based on the inclusion of the nonstandard provisions,[1] D.E. 33. Mr. Maynor submitted a memorandum of law in support of confirmation in which he addressed the meaning of the terms "vested" and "exempt," and represented that his inclusion of the nonstandard provisions was "intended to bring clarity and to avoid having [Mr. Maynor's] rights inappropriately infringed by a form plan which cannot abridge or modify his substantive rights." D.E. 35 at 4. The Second Amended Plan and the Trustee's objection to confirmation of that plan were the matters before the court at the September 7, 2023 hearing. Because the court agreed with the Trustee in all respects, and because Mr. Maynor presented no acceptable basis on which the court could approve the Second Amended Plan, confirmation was denied, with the court indicating to all counsel that it would enter this subsequent opinion stating the bases for denial in more detail. The court notes that as of the date of this opinion, Mr. Maynor's plan has yet to be amended.

JURISDICTION

This bankruptcy court has jurisdiction over the parties and the subject matter of this proceeding pursuant to 28 U.S.C. § 1334, and this is a statutorily core proceeding under 28 U.S.C. § 157(b)(1) that this court is authorized to hear and determine. The United States District Court

[1] The Trustee does not object to the first nonstandard provision regarding the calculation of the liquidation value of the debtor's assets.

for the Eastern District of North Carolina has referred this case and this proceeding to this court under 28 U.S.C. § 157(a) by its General Order of Reference entered on August 3, 1984. This proceeding is constitutionally core, and this court may enter final orders herein. Venue is proper pursuant to 28 U.S.C. §§ 1408 and 1409.

DISCUSSION

The nonstandard provisions in the Second Amended Plan implicate a number of rules and procedures in this district and in the Bankruptcy Code, which include the following: First, the form chapter 13 plan adopted by this district provides, as relevant here:

> **7.1 Vesting of Property of the Bankruptcy Estate:** *(Check one.)*
> Property of the estate will vest in the Debtor(s) upon:
> □ plan confirmation.
> □ discharge
> □ other
>
> **7.2 Possession and Use of Property of the Bankruptcy Estate:** The use of property by the Debtor(s) remains subject to the requirements of 11 U.S.C. § 363, all other provisions of the Bankruptcy Code, Bankruptcy Rules, and Local Rules.

Mr. Maynor checked the "plan confirmation" box in section 7.1. Second, Local Rule 4002-1(g)(4), which applies to chapter 13 debtors, provides:

> (4) DISPOSITION OF PROPERTY. After the filing of the petition and until the plan is completed, the debtor shall not dispose of any non-exempt property having a fair market value of more than $10,000 by sale or otherwise without prior approval of the trustee and an order of the court.

E.D.N.C. LBR 4002-1(g)(4). Finally, the Notice and Order to the Debtor, which is issued upon the filing of a chapter 13 case, provides, as is relevant here:

> (4) <u>Financial/Address Changes</u>: You must notify your attorney and the trustee of any change of mailing address or employment. You must notify the court of any change in mailing address. You must also promptly notify your attorney and the trustee of any substantial changes in your financial circumstances, including substantial changes in your income, expenses, or property Ownership. . . .
>
> * * *

(10) Disposition of Property: You must not dispose of any non-exempt property having a fair market value of more than $10,000.00 by sale or otherwise without prior approval of the trustee and an order of this court.

D.E. 8.

The Trustee's objection contends that Mr. Maynor's nonstandard provisions seek to circumvent this court's Local Form Plan (E.D.N.C. Local Form 113A), the Local Rules, the Order and Notice, and certain provisions of the Bankruptcy Code and Federal Rules of Bankruptcy Procedure, all without any justification or sufficient explanation, and that these provisions are inappropriate and do not comply with the Bankruptcy Code.[2] The Trustee further contends that Mr. Maynor's attempt to abrogate Local Rule 4002-1(g)(4) based on a distinction between exempt and non-exempt property is an improper interpretation of how exemptions operate, and that two of the nonstandard provisions are duplicative of requirements to which the debtor is already subject. Taking all things together, the Trustee also raised the over-arching and troubling question of whether nonstandard provision (e) was "to limit the debtor's obligations under the Order and Notice, or to obfuscate and confuse the trustee as to his intention with respect to this or any of the other nonstandard provisions of the Plan." D.E. 33 at ¶ 31. Finally, the Trustee notes that the issues raised by these nonstandard provisions may be new to Mr. Maynor but certainly are not new to the court, having been raised by Mr. Maynor's counsel in other cases and resolved against his position multiple times within this district.[3]

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[2] *See In re Mank*, No. 19-04199-5-SWH, 2020 WL 1228671 at *3-4 (Bankr. E.D.N.C. March 10, 2020), for a comprehensive discussion of the Official Form Plan, the Local Form Plan, and appropriate use of nonstandard provisions.

[3] At the September 7 hearing, the Trustee observed, "I don't think it's appropriate to say that on all of these issues so far in the bankruptcy court, and I think there's a handful of district court opinions too, where [debtor's counsel] has made these arguments and lost—I don't think it's appropriate to say 'even though I lost . . . I'm hoping that the Fourth Circuit changes their mind so based on that you should confirm the plan.'"

This court addressed the use of nonstandard provisions in chapter 13 plans in *In re Skilling*, where, like here,

> [t]he Nonstandard Provisions at issue largely involve whether [the debtor] may sell property without court approval, which is required in this district whether or not the property vests with the debtor at confirmation. Through his Nonstandard Provisions, [the debtor] wants the applicable local form plan provisions, Local Rules, and Order and Notice to the Debtor to be deemed inapplicable. In support of the Nonstandard Provisions, he argues that the district's local form plan and Local Rules are inappropriate and inconsistent with the Bankruptcy Code.

In re Skilling, No. 22-01085-5-PWM (Bankr. E.D.N.C. Oct. 10, 2022), D.E. 25 at 7.[4] There, the court noted that

> [t]he propriety of subsections of Local Rule 4002-1(g) and provisions of the Order and Notice to Debtor has been the subject of numerous arguments and opinions in this district dating back to 2018, and the two standing chapter 13 trustees and counsel for Mr. Skilling[5] have been involved in most, if not all, of these arguments. While coming before the court in a variety of procedural postures, the issues related to the court's authority to impose requirements on chapter 13 debtors related to the sale of assets postconfirmation has been addressed on multiple occasions by courts in this district at both the bankruptcy and district court level.

Id. Relying on *In re Mank,* No. 19-04199-5-SWH, 2020 WL 122867 (Bankr. E.D.N.C. March 10, 2020) (Humrickhouse, C.J.), the court rejected the nonstandard provisions included in the *Skilling* plan but held that "[t]he court will address a motion for a variance from the Local Rules, or, for

[4] Notably, the nonstandard provisions in *Skilling* are virtually identical in purpose, though somewhat less problematic in text, to those included in the instant case. In *Skilling*, the court denied confirmation of the debtor's plan based on inclusion of these nonstandard provisions:

- Plan provision 7.2 shall not apply.
- EDNC LBR 4002-1(g)(4) shall not apply.
- Paragraph 10 of the ORDER AND NOTICE TO DEBTOR issued by the court on May 24, 2022 (DE 9) shall not apply.
- It shall not be necessary for the court to approve the sale of any vested property.
- 11 USC 363(b) and BR 6004 shall not apply to property that has vested in the Debtor on account of the plan being confirmed.

Skilling, No. 22-1085-5-PWM, D.E. 25 at 3, 10.

[5] Counsel for Mr. Maynor also was counsel for Mr. Skilling.

example, whether 11 U.S.C. § 363(b) and Federal Rule of Bankruptcy Procedure 6004 apply after confirmation, *when relevant to a particular debtor's circumstances*." *Skilling*, No. 22-01085-5-PWM, D.E. 25 at 9 (emphasis added). In fact, this case in its present posture is virtually indistinguishable from *Skilling* and multiple other prior cases in which the court has denied confirmation based on the inappropriate and/or unsupported use of nonstandard provisions.[6]

Here, despite the guidance from this court in *Skilling*, and notwithstanding the specifically expressed readiness of both the court and Trustee to excuse Mr. Maynor's compliance with some requirements based purely upon his articulation of an appropriate factual basis on which to do so, Mr. Maynor still seeks a variance from the rules and procedures that apply throughout this district based on his insistence first that "vesting" insulates him from further interaction with the court, and second that the rules and procedures are fundamentally invalid and abridge his substantive rights. Specifically, Mr. Maynor seeks exemption from standard language in all chapter 13 plans in this district (provision 7.2, which specifies the continuing applicability of 11 U.S.C. 363); this district's Local Rule LBR 4002-1(g)(4); and the standard order issued to a chapter 13 debtor (the Order and Notice), based on his legal interpretation of the terms "vesting" and "non-exempt" property – but with no indication that Mr. Maynor intends to sell his property during the life of the case. Practically speaking, Mr. Maynor's overall goal here has two parts, with the second taking apparent precedence: Part One is to not have to request and obtain permission to sell property valued at $10,000 or above, which could have been accomplished by way of a requested variance. Part Two is to accomplish that goal specifically on this basis: "because the property is not non-

[6] A provision under consideration by the *Mank* court states: "Pursuant to 11 U.S.C. 1322(b)(9), all property owned by the Debtor at the time of the filing of the bankruptcy case shall vest in the Debtor upon confirmation of the plan. 'Vest' means for the property to be removed from the bankruptcy estate therefore obviating the need for the Debtor to file a Notice or Motion with the court pursuant to 11 U.S.C. 363(b) when using, selling or leasing property outside the ordinary course." *Mank*, 2020 WL 1228671, at *5. In both cases, the Trustee objected and the debtors' use of that language precluded confirmation by the court.

exempt and post-confirmation it will not be property of the bankruptcy estate," due to having vested, as Mr. Maynor defines that term. D.E. 32. Mr. Maynor insists that through his use of nonstandard plan provisions, he is seeking to "bring clarity" while avoiding any infringement of his rights. Presumably, he is also seeking a court order agreeing with these principles that may be used by other debtors to insulate themselves from the rules and procedures simply by checking the box indicating that property vests "at plan confirmation" on their plan and/or by claiming an exemption in the property, regardless of the other applicable facts.

For the reasons that follow, the mechanism used by Mr. Maynor – that being the inclusion of nonstandard provisions containing purported statements of law, all of which are misplaced in a chapter 13 plan, many of which are contested, and some of which are inaccurate – will not be approved by this court in this case, or in cases to follow. The court concludes that the notice and approval of sale requirements Mr. Maynor seeks to avoid are not only appropriate, but essential to the straightforward and efficient administration of bankruptcy cases in this district, and to the transparency and candor that are so crucial to the workings of the court – while acknowledging that under the appropriate factual circumstances those requirements may be waived.[7]

This conclusion breaks no new ground, deriving as it does from one of the most basic precepts of bankruptcy law. "Chapter 13 proceedings provide debtors with significant benefits: For example, debtors may retain encumbered assets and have their defaults cured, while secured creditors have long-term payment plans imposed upon them and unsecured creditors may receive payment on only a fraction of their claims." *Carroll v. Logan*, 735 F.3d 147, 151 (4th Cir. 2013) (citing 11 U.S.C. §§ 1322, 1325). In exchange for these benefits, which also include the presence

[7] For example, variance may be appropriate where a plan provides that general unsecured creditors will be paid in full with interest, as there would be no possible effect on the administration of the chapter 13 case if property were to be sold postconfirmation.

of the automatic stay for three to five years and the discharge of sometimes hundreds of thousands of dollars of debt, it is reasonable for the court to overlay disclosure requirements upon the major financial transactions conducted by debtors over the course of the case, including requiring court authority to sell assets and compliance with a handful of other rules that may, as an additional advantage, facilitate successful completion of a plan and entry of discharge. *See In re Murphy*, 327 B.R. 760, 772 (Bankr. E.D. Va. 2005) ("[R]egardless of whether property revesting in the debtor is technically property of the estate, 'until all payments due under the plan are made, both the trustee and the unsecured creditors have an interest in the preservation of the debtor's financial situation . . ..'") (quoting *Barbosa v. Soloman*, 235 F.3d 31, 37 (1st Cir. 2000)), *aff'd*, *Murphy v. O'Donnell* (*In re Murphy*), 474 F.3d 143, 153 (4th Cir. 2007).

In part because of that continuing interest in "the preservation of the debtor's financial situation," the bankruptcy process is dependent upon disclosure and transparency. The Bankruptcy Code, as well as this court's procedures and local rules, are designed, in some measure, to keep the stage light shining on the debtor's financial transactions throughout the course of the bankruptcy case. Through his nonstandard provisions, Mr. Maynor seeks to have this court adopt, through plan confirmation, his legal conclusions that the Bankruptcy Code as a matter of law allows him to pull the stage curtain closed at confirmation, and, further, that this court's local rules and procedures abridge those rights. Numerous cases, including *Murphy*, demonstrate that this is not correct.

Because these same nonstandard provisions have been presented to the court so many times before, consistently resulting in denial of confirmation for the same reasons present in this case, the court reasonably could base this opinion on simply that: Repetition alone, with no new binding law and no unique factual circumstances, is now and will remain insufficient to accomplish Mr.

Maynor's goal. Indeed, to engage in further discussion comes uncomfortably close to issuing an advisory opinion on the legal arguments embedded in Mr. Maynor's nonstandard provisions, which the court is loath to do. What the court emphatically *does* intend to do, however, is to articulate the bases upon which it will not confirm plans that include provisions that are identical in substance, form, or intent to those present in Mr. Maynor's Second Amended Plan. For the reasons that follow, the court specifically rejects Mr. Maynor's arguments on the appropriate definition and treatment of exempt, non-exempt, and "not non-exempt" property, his arguments on the meaning and significance of vesting, and his contentions that this court's local form plan and local rules abridge rights given to the debtor under the Bankruptcy Code.

A. Limited Significance of Whether Property is "Not Non-Exempt"

In North Carolina, debtors who seek relief under the Bankruptcy Code are required to use the North Carolina statutory and constitutional exemptions. *See* N.C. Gen. Stat. § 1C-1601(f). Subject to some variations not relevant here, the statutory exemption for real or personal property used as a residence (known colloquially as the "homestead exemption") is "the debtor's aggregate interest, not to exceed thirty-five thousand dollars ($35,000) in value." N.C. Gen. Stat. § 1C-1601(a)(1). The amount of the claimed homestead exemption may be impacted by any exemption claimed under § 1C-1601(a)(2) (the "wildcard exemption"), and as a result of claiming some items under his wildcard exemption, Mr. Maynor claimed a homestead exemption in the amount of $34,513.24. Schedule C-1, D.E. 11 at 10. Mr. Maynor scheduled the value of the residence as $150,000, and indicated that it is encumbered by a mortgage lien of $132,287. *Id.* Mr. Maynor contends that his claim of exemption "renders that property exempt based on the definition used by the [North Carolina] Administrative Office of the Courts," as follows:

> **Exempt property** – Property, or the value of a portion of it, that the law allows you to keep for your use rather than surrender it for the payment of your debts, provided that you follow the correct procedure to claim the exemption.

D.E. 35 at 3.

In his memorandum, Mr. Maynor states that nonstandard provision (c)[8] is not seeking to determine that the claim of exemption removes the real property from the bankruptcy estate, but that because the property is "exempt property, it is not non-exempt property and E.D.N.C. LBR 4002-1(g)(4) does not apply." D.E. 35 at 3-4. Presumably, then, the portion of nonstandard provision (c) stating that post-confirmation the property "will not be property of the estate" relates to vesting (as discussed below), and not the claimed exemption. The assertion that the property is "not non-exempt" is a misstatement of the law and a misinterpretation of the language of the Local Rule and Order and Notice.

[8] Mr. Maynor's included nonstandard provisions asserting as a matter of law that certain rules and orders do not apply because his residence is "not non-exempt" include the following:

> c. EDNC LBR 4002-1(g)(4) shall not apply post-confirmation to the real property located at 8016 Lane Road, Linden, NC 28356 because the property is not non-exempt and post-confirmation it will not be property of the bankruptcy estate.
>
> d. Paragraph 10 of the Order and Notice to Chapter 13 Debtor issued on April 7, 2023 shall not apply to the real property located at 8016 Lane Road, Linden, NC 28356 because the property is not non-exempt and post-confirmation it will not be property of the bankruptcy estate.

As noted above, Local Rule 4002-1(g)(4) provides:

> DISPOSITION OF PROPERTY. After the filing of the petition and until the plan is completed, the debtor shall not dispose of any non-exempt property having a fair market value of more than $10,000 by sale or otherwise without prior approval of the trustee and an order of the court.

Paragraph 10 of the Order and Notice reads, "<u>Disposition of Property</u>: You must not dispose of any non-exempt property having a fair market value of more than $10,000.00 by sale or otherwise without prior approval of the trustee and an order of this court."

The issue is whether the property itself, *or only a specified value*, is exempt. The statute contains a limitation on the value that a debtor may claim as exempt. Even the language cited by Mr. Maynor from the North Carolina Administrative Office of the Courts references "the value of a portion of" the property, not the entire property. The varying arguments that have been made by Mr. Maynor's counsel on this issue have been thoroughly examined and rejected in *In re Sugar*, No. 19-04279-5-DMW, 2023 WL 1931078, at *7 (Bankr. E.D.N.C. Feb. 10, 2023) (Warren, C.J.), *appeal pending*, No. 5:23-cv-00082-FL (E.D.N.C.); *see also Reeves v. Callaway*, 546 Fed. Appx. 235, 241 (4th Cir. 2013) (under North Carolina's exemption laws, property of a debtor which is not subject to an unlimited or in-kind exemption, such as a debtor's residence, remains property of the bankruptcy estate notwithstanding a debtor's claim of exemption in it).

Mr. Maynor contends that Judge Callaway of this district's interpretation of the term "non-exempt" is consistent with his, citing *In re Robinson*, No. 20-02747-5-JNC, 2020 Bankr. LEXIS 3769 (Bankr. E.D.N.C. Dec. 14, 2020), and *In re Nigro*, No. 21-01123-5-JNC, D.E. 25 (Bankr. E.D.N.C. Sept. 7, 2021). D.E. 35 at 4. Having reviewed those opinions, this court cannot agree with that conclusion. In *Robinson*, the court simply found that there was no equity in the property at issue and ***excused the debtor from compliance with Local Rule 4002-1(g)(4)***. *Robinson*, 2020 Bankr. LEXIS 3769 at *5-6 ("A nonstandard chapter 13 plan provision removing the Residence . . . from Local Rule 4002-1(g)(4) compliance is permitted and will be approved in an amended plan.") (emphasis added). That is precisely what this court indicated it would do had Mr. Maynor not included language in his nonstandard provisions purporting to set forth the legal implications of vesting and exemptions. Put more bluntly, Judge Callaway did not find that the Local Rule by its terms does not apply. And in *Nigro*, the court found there was substantial nonexempt equity in the debtor's residence and refused to excuse the debtor from compliance with the Local Rule even where the debtor's plan provided for a 100% payment to unsecured creditors. *In re Nigro*, No. 21-01123-5-JNC, D.E. 25. The court did not address the definition of "non-exempt."

The court acknowledges that there is more than one way to read Local Rule 4002-1(g)(4), but none of those readings support the debtor's interpretation. The plain meaning of the local rule is that if the fair market value exceeds $10,000 over the debtor's claimed exemption, regardless of encumbrances, then court authority is required to sell the property. The more practical reading is that if the fair market value exceeds $10,000 over liens plus the claimed exemption, then court authority is required to sell the property. *See Sugar*, 2023 WL 1931078, at *8 ("The debtor's interest in the property is nonexempt for any value exceeding the liens and allowed exemption."). However, the determination of value must be made at the time the property is sold, not as of the petition date or the confirmation date.[9] Accordingly, the court cannot determine at confirmation whether property is "not non-exempt" for purposes of Local Rule 4002-1(g)(4) because it is dependent upon a valuation to be determined on a date in the future. Including a statement of "not non-exempt" in a nonstandard provision seeks an advisory opinion of what the value will be on the

[9] Mr. Maynor's counsel recently raised the timing of valuation for purposes of Local Rule 4002-1(g)(4) in another case before the court. Determining value at the time of sale is consistent with how North Carolina applies its exemptions at judgment execution. A judgment lasts ten years, but an execution terminates 90 days after issuance. N.C. Gen. Stat. § 1-47; § 1-310. A judgment debtor is entitled to claim exemptions each time a new execution is to be issued. *See Household Finance Corp. v. Ellis*, 419 S.E.2d 592, 593-94, 107 N.C. App. 262 (N.C. App. 1992). Along with each claim of exemptions is a new determination of the value of property. N.C. Gen. Stat. § 1C-1603. Further, "[w]here the order designating exemptions indicates excess value in exempt property, the clerk, in an execution, may order the sale of property having excess value and appropriate distribution of the proceeds." N.C. Gen. Stat. § 1C-1603(e)(10). And, the debtor's exemptions may be modified upon a change of circumstances, which may include a "substantial change in value." N.C. Gen. Stat. § 1C-1603(g). Thus, a judgment creditor is not limited to collection of the value of property as of the date of its judgment, but can take advantage of appreciated value if it delays execution. This is also consistent with re-evaluating the liquidation value of a chapter 13 estate at the time of plan modification. *See In re Adams*, No 21-80425, 2023 WL 7320858, at *6 (Bankr. M.D.N.C. Nov. 3, 2023). Regardless, using an earlier date—whether the petition date or initial confirmation date—is irreconcilable with the holding in *Murphy*, which required the debtor to pay the appreciated value of the debtor's property interest to the creditors after sale.

date of a hypothetical future sale.[10] Because the Second Amended Plan contains nonstandard provisions concluding that Mr. Maynor's residence is "not non-exempt" such that Local Rule 4002-1(g)(4) and the Order and Notice do not apply, confirmation is denied.

B. Legal Effect of Vesting at Confirmation

Before turning to Mr. Maynor's interpretation of "vesting" and what he contends that entails, the court reviews the basics. First, § 1327(b) provides that "[e]xcept as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor." 11 U.S.C. § 1327(b). Section 1327(c) states that "[e]xcept as otherwise provided in the plan or in the order confirming the plan, the property vesting in the debtor under subsection (b) of this section is free and clear of any claim or interest of any creditor provided for by the plan." 11 U.S.C. § 1327(c). Section 1306(a) of the Bankruptcy Code provides that in a chapter 13 bankruptcy case,

> (a) Property of the estate includes, in addition to the property specified in section 541 of this title—
>
> (1) all property of the kind specified in such section 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, 11, or 12 of this title, 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, 11, or 12 of this title, whichever occurs first.

11 U.S.C. § 1306(a). "By providing that the bankruptcy estate continues to be replenished by post-petition property until the case is closed, dismissed, or converted under Chapter 7, 11, or 12 of the Bankruptcy Code, § 1306(a) provides for the continued existence of the bankruptcy estate until the earliest of any of the above-mentioned events occur." *Murphy v. O'Donnell* (*In re Murphy*),

[10] Notwithstanding that some degree of prescience is required, the court has indicated that with the agreement of the Trustee, it would excuse the debtor from application of this rule where it seems unlikely there will ever be value above liens and the claimed exemption, as Judge Callaway did in *Robinson*.

474 F.3d 143, 153 (4th Cir. 2007). There is a statutory dissonance between having property of the estate "vest" in the debtor at confirmation under § 1327, and the estate continuing to refill with postconfirmation property under §1306.

The interplay of these two sections has confounded courts, leading to five different approaches to the concept of "vesting" in chapter 13. *See In re Baker*, 620 B.R. 655, 663-64 (Bankr. D. Colo. 2020). As described in *Baker*, those approaches are:

> Estate termination. At confirmation, the estate ceases to exist and all property of the estate, whether acquired before or after confirmation, becomes property of the debtor.
>
> Estate transformation. At confirmation, all property of the estate becomes property of the debtor except property essential to the debtor's performance of the plan. The chapter 13 estate continues to exist, but it contains only property necessary to performance of the plan, whether acquired before or after confirmation.
>
> Estate replenishment. At confirmation, all property of the estate becomes property of the debtor. The chapter 13 estate continues to exist and "refills" with property defined in section 1306 that is acquired by the debtor after confirmation, without regard to whether that property is necessary to performance of the plan.
>
> Estate preservation. The vesting of property in the debtor under section 1327(b) does not remove any property from the chapter 13 estate, whether acquired before or after confirmation. Property remains in the estate until the case is closed, dismissed, or converted. The debtor's rights and responsibilities with respect to property of the estate may change somewhat at confirmation, but the existence and composition of the estate are not disturbed by section 1327(b).
>
> Conditional vesting. At confirmation, vesting gives the debtor an immediate and fixed right to use estate property, but that right is not final until the debtor completes the plan and obtains a discharge.

Id.

The cases analyzing vesting primarily arise in the context of whether postconfirmation sale proceeds of vested property belong to the debtor or should be paid to creditors through plan modification; none address the more narrow issue before this court, which is what authority the court has, and the means by which that authority may be exercised, over an asset that has vested.

But the two issues go hand in hand, because if the court has *no* authority over an asset, it could not order a plan to be modified for the proceeds of that asset to be paid to creditors. And, the opposite is true: if the court *has* authority to allow a plan modification for sale proceeds to be paid to creditors, it must also have some authority over that asset prior to its sale. This precise conclusion was recently articulated in this district in *Sugar:*

> If vesting does not preclude the court from modifying a plan to account for the receipt of proceeds from vested property, then similarly, vesting would not strip the court of jurisdiction over the disposition of vested property before it is converted into cash proceeds. *See also Taylor v. Logan*, No. 5:20-CV-663-BO, 2021 U.S. Dist. LEXIS 103282, at *11 (E.D.N.C. June 2, 2021) ("[B]ased on the applicable language and rules, the bankruptcy court may, through an order, exercise oversight of non-exempt property, whether termed estate property or property of the Debtor, after confirmation of the Chapter 13 plan.").

Sugar, 2023 WL 1931078, at *6, n.4.

The Court of Appeals for the Fourth Circuit has not adopted a specific approach to vesting, but it has discussed the issue in the context of plan modification. In *Murphy*, 474 F.3d at 143, the appellate court considered whether to require modification of a confirmed plan to provide for the payment to creditors of postconfirmation sale proceeds of the debtor's residence. The court considered the debtor's argument that "the bankruptcy court was not at liberty to modify his confirmed plan because his plan, in accordance with § 1327(b), vested all property of the estate in him at the time of confirmation. According to [the debtor], once his plan was confirmed, the Chapter 13 trustee forfeited any claim to the proceeds of the sale." *Id.* at 153. The lower court had rejected that argument, determining that "[t]he debtor's revesting argument, taken to its logical conclusion, would effectively read § 1329 out of existence, and is inconsistent with the holding in *Arnold v. Weast (In re Arnold)*, 869 F.2d 240 (4th Cir. 1989)." *Murphy*, 327 B.R. at 772. On review, and after discussing the various theories of vesting, the circuit court concluded that it "need not discuss these varying interpretations or select one as the most preferable," but instead held that "***a debtor cannot use plan confirmation as a license to shield himself from the reach of his creditors when he experiences a substantial and unanticipated change in his income***." *Murphy*, 474 F.3d at 154 (citation omitted) (emphasis added); *see also Croniser v. Logan*, No. 5:22-cv-00352-D, 2023 U.S. Dist. LEXIS 102067, at *14 (E.D.N.C. Jun. 12, 2023) (adhering to Fourth Circuit precedent and applying *Murphy* standards).

In short, while the *Murphy* court declined to adopt a specific approach to vesting, *Murphy* absolutely stands for the proposition that the sale proceeds of a vested asset are still available for payment to creditors. Notwithstanding any larger discussion about the apparent statutory dissonance, *Murphy* remains binding on this court, and its conclusion gives this court some guidance and insight – albeit through a process of elimination – as to what approaches to vesting are and are not available in this circuit.[11] This court cannot reconcile *any* approach to vesting that allows the debtor to retain postconfirmation sale proceeds with *Murphy*, and thus must conclude that those approaches are not the current law in the Fourth Circuit.

With that background in mind, the court turns to Mr. Maynor's arguments. Several of the nonstandard provisions assert that the court's rules and procedures, and sections of the Bankruptcy Code and Federal Rules of Bankruptcy Procedure, are inapplicable specifically because Mr. Maynor chose for his property to vest at confirmation pursuant to § 1327(b). According to Mr.

[11] This court undertook an analysis of what other bankruptcy courts within the Fourth Circuit – similarly bound by *Murphy* – have said about their approach to "vesting." The majority of districts within this circuit have adopted provisions either in their form plans, form orders, or local rules that provide that property vests at discharge, not at confirmation. Accordingly, it appears that no bankruptcy court has identified the approach to vesting that best aligns with *Murphy*, but instead most have avoided the issue by prohibiting vesting at confirmation. The extent to which courts may require vesting at discharge in their local form plan is currently before the Fourth Circuit in *Trantham v. Tate,* No. 22-2263 (appeal from No. 1:22-cv-00076-MOC, 2022 WL 17091982 (W.D.N.C. Nov. 21, 2022)), with oral argument tentatively scheduled for late January 2024. Whether to amend this district's form plan and order may be considered by the court and Local Rules Committee upon further guidance from the circuit court.

Maynor, that means that the property is no longer property of the estate.[12] When asked how the court could reconcile this argument with *Murphy*, and further how this argument could be consistent with any theory of vesting other than the "estate termination approach," which is clearly contrary to *Murphy*, Mr. Maynor referred the court to the analysis in a recent opinion issued from the bankruptcy court in the Eastern District of Michigan, *In re Elassal*, 654 B.R. 434 (Bankr. E.D. Mich. 2023).

The *Elassal* court adopted the "estate replenishment" approach, and concluded that because the sale proceeds of a residence that vested in the debtor at confirmation were not newly-acquired property, the debtor could not be compelled to turn over the proceeds to be paid to creditors. *Id.* at 437. In doing so, however, it noted the diverging positions on vesting across the courts. *See id.* at 437, n.2. Significantly, the *Elassal* court was unconstrained by Fourth Circuit precedent requiring post-confirmation appreciation to be paid to creditors upon the sale of an asset despite the vesting of that asset at confirmation, as were the other courts cited by *Elassal* that reached a similar conclusion.

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[12] Mr. Maynor included the following nonstandard provisions implicating vesting:

> c. EDNC LBR 4002-1(g)(4) shall not apply post-confirmation . . . because . . . post-confirmation [the debtor's residence] will not be property of the bankruptcy estate;
> d. Paragraph 10 of the Order and Notice . . . shall not apply . . . because . . . post-confirmation [the debtor's residence] will not be property of the bankruptcy estate;
> f. Upon confirmation, the Debtor's interest in [his residence] shall no longer be property of the bankruptcy estate pursuant to 11 USC 1329(b)(9), 11 USC 1327(b) and plan provision 7.1;
> g. The Debtor shall not [be] required to file a notice pursuant to 11 USC 363(b) or Federal Bankruptcy Rule 6004(a) prior to selling vested property;
> h. The debtor shall not be required to obtain a court order prior to selling any vested property.

D.E. 32 at 4.

Further, it appears that courts adopting the same "estate replenishment" approach to vesting have reached opposite conclusions with respect to whether the debtor or creditors receive the benefit of postconfirmation appreciation when the property is sold. *Compare Elassal,* 654 B.R. 434 (adopting the estate replenishment approach and authorizing debtor to use proceeds to purchase a new home, but reserving the question of what happens to any proceeds in excess of the amount needed for that purchase), *and In re Larzelere*, 633 B.R. 677, 682 (Bankr. D.N.J. 2021) (adopting the estate replenishment approach and finding proceeds are property of the debtor) *with Barbosa v. Solomon (In re Barbosa)*, 235 F.3d 31 (1st Cir. 2000) (adopting the estate replenishment approach and finding sale proceeds attributable to appreciation in value must be paid to creditors), *and In re Marsh*, 647 B.R. 725 (Bankr. W.D. Mo. 2023) (same).[13]

With courts unable to agree as to how a specific approach to vesting is to be applied postconfirmation, this court is left, through the process of elimination, with the certainty that absent revisiting its conclusion in *Murphy*, the Fourth Circuit would adopt the estate preservation or conditional vesting approaches, or the estate replenishment approach as applied by *Barbosa* and *Marsh*, but *not* the estate termination, estate transformation, or estate replenishment approach as applied by *Elassal* and *Larzelere*. Again, the conundrum is that the *Murphy* court essentially gave us its answer without showing us the specific methodology by which it got there, so, while this court can deduce from that answer the approaches that *could not* have been used to arrive at it, this court cannot be sure of which approach the *Murphy* court *did* take. That said, this much is certain: none of the approaches possibly employed by the *Murphy* court could support Mr. Maynor's asserted conclusions in his nonstandard provisions that his residence is no longer subject to court oversight due to vesting.

[13] The court notes that in all four of these cases, the debtor first sought and obtained court authority to sell the property, notwithstanding that the property "vested" at confirmation.

The court acknowledges that this discussion strays a bit from the issue actually before it, which is not whether postconfirmation sale proceeds of vested property are property of the estate, but whether vesting at confirmation removes an asset from the estate such that no notice or authority to sell that asset is necessary as a matter of law, as asserted in Mr. Maynor's nonstandard provision. Given that the four cases adopting the estate replenishment approach discussed in this opinion did so ***after court approval*** of a sale of vested property, the court finds no authority to support Mr. Maynor's position under any theory of vesting available in this circuit.

Finally, the Bankruptcy Code explicitly allows bankruptcy courts to require property to vest at a time other than at confirmation (such as at discharge), and to provide that vesting is *not* free and clear of claims or interests of creditors. 11 U.S.C. §§ 1327(b), (c). By inference, courts have the authority to impose some oversight and restraint on what it means for property to vest or how vested property may be used or transferred, which by definition is an exercise of authority less restrictive than disallowing vesting at confirmation entirely. In sum, the court cannot agree with Mr. Maynor's theory that "vesting" entirely removes property from the estate and from court oversight, and does not agree that the rules and procedures applicable to the sale of property no longer apply as a legal consequence of vesting at confirmation. Accordingly, the inclusion of nonstandard provisions asserting that the procedures for postconfirmation sale of property do not apply due to vesting is a basis for denial of confirmation.

C. Other Nonstandard Provisions

Finally, Mr. Maynor included three other nonstandard provisions that do not relate solely to his arguments about property being "not non-exempt" or "vested," but simply state the debtor's interpretation of the Bankruptcy Code, the Federal Rules of Bankruptcy Procedure, the court's local rules and orders, and the court's local form plan. Like those addressed above, these nonstandard provisions also are inappropriate and support denial of confirmation. Those provisions are:

> b. Plan provision 7.2 shall not apply. This is a deviation from the EDNC Local Form Plan in order to avoid conflict with the Debtor's rights pursuant to 11 USC 1321, 11 USC 1322(b)(9), and 11 USC 1327(b).
>
> e. The Debtor must notify his attorney and the trustee of any change of address or if he experiences a substantial change in his property ownership.
>
> i. If the Debtor seeks to sell, lease or use estate property outside the ordinary course during the pendency of the case (e.g. property of the kind described in 11 USC 541(a)(5)), then he shall comply with the requirements of 11 USC 363(b), 11 USC 1303 and Fed Bankr Rule 6004 but shall not be required to comply with EDNC LBR 4002-1(g)(4). This provision is intended to identify the proper procedural mechanism that is applicable and avoid neglect and/or duplication with regard to any substantive or procedural requirement.

D.E. 32 at § 8.1. The court will address each in turn.

1. Nonstandard Provision (b)

With respect to nonstandard provision (b), as noted above, plan provision 7.2 provides generally that § 363 of the Bankruptcy Code, as well as all other provisions of the Bankruptcy Code, Bankruptcy Rules, and Local Rules, remain in effect postconfirmation. Mr. Maynor contends that this provision conflicts with or abridges rights given to him by the Bankruptcy Code and thus it should not apply where property vests in the debtor at confirmation. In essence, through this nonstandard provision, Mr. Maynor seeks a determination by this court that this district's local form plan is invalid. To the extent this argument overlaps with Mr. Maynor's argument that this court simply has no authority to require anything with respect to vested property postconfirmation, the court incorporates its discussion of "vesting" from above and rejects this provision. To the extent this provision seeks to have the court, through confirmation, agree with him that plan provision 7.2 (and thus the requirements of the Bankruptcy Code, Bankruptcy Rules, and Local Rules) conflicts with the debtor's rights under the Bankruptcy Code, that, too is rejected.

In essence, Mr. Maynor contends that because the Bankruptcy Code imposes certain requirements, it necessarily means that other requirements are not allowed. For example, Mr. Maynor contends that because § 363(b) only requires *notice* of a potential sale of property of the estate outside of the ordinary course of business, courts may not require *court approval* of a proposed sale, nor may the court extend its authority to consider such a sale if property has vested in the debtor because, according to Mr. Maynor, that property is no longer property of the estate. Of course, if a party were to object to the notice provided under § 363(b), then court approval (overruling any objection) would be necessary for the debtor to sell the property.

As the Trustee points out, however, the Bankruptcy Code does not give debtors an unfettered right to do what they please with their property while the case is pending.[14] The Code clearly authorizes the court to require vesting at discharge, 11 U.S.C. § 1327, and continued oversight of certain assets, whether vested or not, is less intrusive than requiring vesting at discharge. This oversight falls within the court's authority. Chapter 13 debtors are given relatively few obligations with which to comply postconfirmation in exchange for the significant benefits of the automatic stay, a discharge upon completion of a plan that may require ***no*** repayment to unsecured creditors, and, as in Mr. Maynor's case, the ability to force a secured creditor to accept a repayment plan after default that extends over five years. More generally, chapter 13 is a voluntary process: if Mr. Maynor does not wish to comply with these minimal requirements, he may dismiss his case.

[14] In addition, Local Rule 4002-1(g)(4) does not *prohibit* the debtor from selling property during the chapter 13 case; instead, it specifies the process through which a debtor may sell property. *Cf. Higgins v. Logan*, 635 B.R. 776, 779-82 (E.D.N.C. 2021) (holding Local Rule 4002-1(g)(5), which sets forth the procedure for a debtor to seek court authority to incur debt over $10,000 during the pendency of a chapter 13 case, is procedural and not substantive, as it "does not prohibit the debtor from incurring post-petition debt of $10,000.00 or more. Rather, it specifies the process by which a debtor may seek to incur such debt.").

In sum, the court will not confirm a plan with a provision stating that the court's form plan – which requires compliance with the Bankruptcy Code, Bankruptcy Rules, and Local Rules – conflicts with the debtor's rights under the Bankruptcy Code. This is a misstatement of the law and an inappropriate use of nonstandard provisions.

2. Nonstandard Provision (e)

Nonstandard provision (e) is both duplicative and an incomplete recitation of one provision of the Order and Notice. As noted above, that provision requires:

> (4) Financial/Address Changes: You must notify your attorney and the trustee of any change of mailing address or employment. You must notify the court of any change in mailing address. You must also promptly notify your attorney and the trustee of any substantial changes in your financial circumstances, including substantial changes in your income, expenses, or property Ownership. . . .

D.E. 8. Nonstandard provision (e) rewrites this paragraph to limit the debtor's notice requirements only to any change of address or a substantial change in his property ownership, omitting any other substantial change in financial circumstances. The Trustee's objection raised the question of whether nonstandard provision (e) was "to limit the debtor's obligations under the Order and Notice, or to obfuscate and confuse the trustee as to his intention with respect to this or any of the other nonstandard provisions of the Plan." D.E. 33 at ¶ 31. The court is equally flummoxed by what is intended by this nonstandard provision. The debtor already is required to notify his attorney and the Trustee of a change of address and any change in property ownership, and there is no need to repeat that obligation in a nonstandard provision – it is, by inclusion in the Order and Notice, already "standard."

Accordingly, the inclusion of this language in section 8.1 of the Second Amended Plan suggests that Mr. Maynor intends to override the obligations delineated in the Order and Notice and to eliminate the requirement to notify his counsel and the Trustee of other substantial changes in financial circumstances, such as a change in income or expenses. As with the other nonstandard provisions, there is no factual explanation of why Mr. Maynor should be excused from the requirements imposed on all debtors in this district, nor can the court imagine any basis on which a debtor would be excused from notifying his counsel and the Trustee of a substantial change in income or expenses.[15]

3. Nonstandard Provision (i)

Nonstandard provision (i) seems to have two goals: first, to limit all procedural requirements regarding the sale of property *only* to property of the estate (which Mr. Maynor contends will not include his residence postconfirmation due to vesting), and second, to the extent any rule must be followed, to have a declaration through his nonstandard provision that the local rule governing the sale of property is not the "proper procedural mechanism." Mr. Maynor contends instead that the debtor is only required to provide notice under § 363(b) and Federal Rule of Bankruptcy Procedure 6004. The court has already addressed the issue of vesting, and concludes that any nonstandard provision seeking to exempt the debtor from the procedures related to sale of property during the pendency of the plan based on his legal interpretation of the meaning of "vesting" is inappropriate and a basis upon which to deny confirmation.

With respect to the second apparent goal, this court has authority to establish procedures to exercise oversight of the debtor's major financial transactions during the course of the case, including its requirements under Local Rule 4002-1(g)(4). Local Rule 4002-1(g)(4) ***is*** the "proper

[15] To the extent this provision was intended to, in the context of the other nonstandard provisions, acknowledge that Mr. Maynor still must notify his counsel and the Trustee of any sale of property notwithstanding the asserted inapplicability of the requirements to give notice or seek court authority in advance of a sale, the court agrees that if Mr. Maynor is to be excused from those requirements, notice after a sale is appropriate. However, it is unclear whether that is the meaning or intent of this nonstandard provision, and in light of the court's denial of the remaining nonstandard provisions, this provision is unnecessary.

procedural mechanism" and full, transparent compliance with that rule necessarily includes compliance with the plain requirements of § 363(b). "While local rules are tied to the Federal Rules of Bankruptcy Procedure, courts are authorized to implement local rules that are necessary for the administration of cases filed in their districts, especially rules like Local Rule 4002-1(g)(4), that provide structure for a successful Chapter 13 plan and eventual discharge. Nothing in the Local Rule conflicts with § 363 and Rule 6004." *Sugar*, 2023 WL 1931078, at *7. Mr. Maynor's effort to deem the court's Local Rules improper through a nonstandard plan provision is rejected and constitutes a basis upon which to deny confirmation.

CONCLUSION

This court has emphasized that it would allow prospective relief from certain provisions of the court's rules and procedures where that relief is warranted by the specific facts before it, and that while a separate motion seeking that relief is preferable, the court also would consider providing that relief through a debtor's *appropriate* use of nonstandard provisions. The court offered to do exactly that at the August 10 hearing. What the court will *not* do is excuse debtors from compliance with the local rules and procedures based upon the debtors' inclusion in their plan of nonstandard provisions that purport to set out statements or interpretations of law, or to assert that the rules and procedures are invalid or contrary to law. Based on the foregoing, confirmation is **DENIED**. The debtor may file an amended plan within 14 days of the date of this order.

END OF DOCUMENT

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION (DETROIT)

In re:	Chapter 13
Wendy Elassal,	Case Number 21-42801
Debtor.	Hon. Mark A. Randon

_______________________________/

OPINION AND ORDER OVERRULING TRUSTEE'S OBJECTION AND DENYING PLAN MODIFICATION

I. INTRODUCTION

Housing prices fluctuate over time, as do the relative financial risks and benefits of home ownership. Ideally, home values appreciate. Yet history cautions, there are no guarantees. Reliably predicting the real estate market's ebbs and flows ranges from difficult to a fool's errand.

In 2021, Wendy Elassal ("Debtor") filed chapter 13 bankruptcy, committing three years of disposable income to keep her assets—including a $250,000 home—with $228,000 of liens. Although unsecured creditors would have received nothing in a hypothetical Chapter 7 liquidation (Debtor could have exempted the remaining home equity), Debtor's Second Amended Plan proposed to pay a minimum of $1,277.16 towards $93,805.83 in general unsecured claims. This plan was confirmed without objection.

Who could have predicted, in less than two years, Debtor's home would sell for $435,000, netting $177,695.13 in proceeds after full payment of the liens? Not the Trustee, who consented to confirmation; nor the unsecured creditors, who could reasonably have decided something was better than nothing at the time. Likely not even Debtor, who agreed to the modest payment to unsecured creditors, whether her home appreciated or *depreciated*.

Through either her uncanny real estate market expertise or good fortune, Debtor's decision to file and remain in Chapter 13 has "paid off."[1] But for whom? Debtor wants to keep the money: Having now paid her secured creditors, she seeks Court approval to use all of the sale proceeds to buy a new home—for cash—while making her promised dividend to unsecured creditors over the remainder of her plan. The Trustee's objection and proposed plan modification urge a different outcome: Debtor may only keep what remains *after* unsecured claimants receive full payment—anything less would be inconsistent with the code and evidence Debtor's lack of good faith. The Court disagrees. Superior discernment or luck is neither gamesmanship nor an absence of good faith. Because the Court determines: (1) the estate replenishment theory best harmonizes 11 U.S.C. §§ 1306 and 1327, Debtor's home vested in her at confirmation; (2) the sale proceeds, derived from post-confirmation appreciation of Debtor's pre-petition real property, cannot be untethered from the real property itself, and do not refill the estate; and (3) the sale proceeds, particularly when escrowed for direct rollover into a new home purchase, are not "disposable income"—Debtor may use the sale proceeds to buy a new residence. The Trustee's objection is **OVERRULED**, and her plan modification is **DENIED**.

[1]Many chapter 13 cases end unsuccessfully: without a discharge, debtors face the resumption of accumulated interest on their debts, which has compounded during their bankruptcies and, having paid a fee to their attorneys and trustees, often find themselves in worse financial shape than before they filed. *See Harris v. Viegelahn*, 575 U.S. 510, 514, 135 S. Ct. 1829 (citing Porter, *The Pretend Solution: An Empirical Study of Bankruptcy Outcomes*, 90 TEXAS L. REV., 103, 107–11 (2011)).

II. JURISDICTION

The Court has jurisdiction over this matter under 28 U.S.C. §§ 1334(b) and 157(a) and (b), and is authorized, by standing reference from the United States District Court, to resolve the contested matter as a core proceeding under 28 U.S.C. § 157(b)(2)(A) and (O).

III. PROCEDURAL AND FACTUAL BACKGROUND

Debtor filed Chapter 13 bankruptcy on March 31, 2021. A Judgment of Divorce provided Debtor's former spouse an interest in the marital home in Van Buren Township, Michigan (the "Van Buren Property"). Debtor listed her interest on Schedule A/B and valued the Van Buren Property at $250,000, which was unchallenged. She also disclosed three outstanding liens in favor of: (1) Independent Mortgage in the amount of $180,000; (2) Debtor's divorce attorney for $3,597.40; and (3) her former spouse in the amount of $48,000. Debtor listed the remaining $22,000 equity as subject to her federal homestead exemption.

The Judgment of Divorce awarded Debtor the Van Buren Property with three conditions: (1) Debtor's former spouse would make 24 monthly mortgage payments in lieu of child and spousal support; (2) Debtor would sell or refinance the Van Buren Property by December 31, 2022, to pay the former spouse's equity position; and (3) Debtor would be responsible for any mortgage payments after January 1, 2023.

On July 31, 2021, the Court entered an Order Confirming Debtor's Plan. On February 2, 2023, after the deadline to sell or refinance, Debtor filed a motion to sell the Van Buren Property. The Trustee objected to the proposed sale to Debtor's friend for $275,000; Debtor filed an amended motion to sell the Van Buren Property. This time, she sought approval to sell it for $435,000 through an arms length transaction and to use all of the proceeds from the sale, $173,655.93 (the "Sale Proceeds"), to purchase a new residence. The Trustee objected. She argued Debtor was first required to use $94,000 of the Sale Proceeds to pay her unsecured creditors in full. Debtor and Trustee stipulated to the entry of an order approving the sale, requiring Debtor's attorney to retain the Sale Proceeds in attorney's client trust ("IOLTA") account until further order of the Court. On May 8, 2023, Debtor filed a motion to use the Sale Proceeds to purchase a new residence. The Trustee objected and filed a plan modification, again proposing Debtor use $94,000 of the Sale Proceeds to pay unsecured creditors in full.

After hearing the motions, the Court ordered supplemental briefing. On July 21, 2023, Debtor filed her Post-Hearing Response Brief ("Debtor's Brief"), and the Trustee filed her Supplemental Brief in Support of Trustee's Proposed Post-Confirmation Plan Modification ("Trustee's Brief" and collectively, the "Briefs").

IV. APPLICABLE LAW AND ANALYSIS

The Court recognizes that the Briefs cite to competing persuasive–but not controlling–authority to support their respective positions. The Court first adopts a common position that appears in both Briefs—implementation of the Estate Replenishment approach to harmonize 11 U.S.C. §§ 1306 and 1327. *See In re Marsh*, 647 B.R. 725 (Bankr. W.D. Mo. 2023) (relied upon in Trustee's Brief); *see also In re Larzelere*, 633 B.R. 677 (Bankr. D. N.J. 2021) (relied upon in Debtor's Brief). The Court then leans into Debtor's argument, finding the post-confirmation Sale Proceeds belong to Debtor. *See e.g., McDonald v. Burgie (In re Burgie)*, 239 B.R. 406 (B.A.P. 9th Cir. 1999); *In re Euler*, 251 B.R. 740 (Bankr. M.D. Fla. 2000); *In re Larzelere*, 633 B.R. 677 (Bankr. D. N.J. 2021); *In re Mobley*, No. 11-49079, 2011 WL 6812551 (Bankr. E.D.

Mich. Dec. 1, 2011); *In re Ash'shadi*, No. 04-55924, 2005 WL 1105039 (Bankr. E.D. Mich. May 6, 2005).

A. *Reconciliation of 11 U.S.C. §§ 1306 and 1327 is Best Accomplished Though the Estate Replenishment Approach*

This Court is not the first to grapple with fashioning an approach which harmonizes the competing statutory directives of sections 1306 and 1327. *See e.g., In re Tarby*, 2012 WL 1390201 (Bankr. D. N.J. Apr. 20, 2012); *In re Scholl*, 605 B.R. 163 (Bankr. S.D. Ohio 2019); *In re Baker*, 620 B.R. 655 (Bankr. D. Colo. 2020); *In re Clouse*, 446 B.R. 690 (Bankr. E.D. Pa. 2010).[2] This Court finds the Estate Replenishment approach best reconciles these code sections.

Sections 541 and 1306 primarily govern property of the chapter 13 bankruptcy estate. 11 U.S.C. §§ 541 and 1306. Section 541 defines estate property as "all legal or equitable interests of the debtor in property as of the commencement of the case" and "[p]roceeds, product, offspring, rents, or profits of or from property of the estate[.]" 11 U.S.C. § 541(a)(1), (6). Section 1306 incorporates section 541 and captures additional property in chapter 13 cases:

> (a) Property of the estate includes, in addition to the property specified in section 541 of this title—

[2] *In re Larzalere*, 633 B.R. at 681-82 (Bankr. D. N.J. 2021) ("The Circuit Courts of Appeals that have addressed the issue are not in agreement. *See In re Jones*, 420 B.R. 506, 515 (B.A.P. 9th Cir. 2009) *aff'd on other grounds*, 657 F.3d 921 (9th Cir. 2011) (following estate termination approach); *Telfair v. First Union Mortg. Corp*., 216 F.3d 1333, 1339-40 (11th Cir. 2000) (estate transformation); *In re Barbosa*, 236 B.R. 540, 550 (Bankr. D. Mass. 1999) *aff'd sub nom*, *Barbosa v. Solomon*, 243 B.R. 562 (D. Mass. 2000) *aff'd*, 235 F.3d 31 (1st Cir. 2000) (following estate replenishment approach); *In re Talbot*, 124 F.3d 1201, 1208 (10th Cir. 1997) (stating without discussion that house revested in debtors at confirmation pursuant to section 1327(b)); *Black v. United States. Postal Serv. (In re Heath)*, 115 F.3d 521, 524 (7th Cir. 1997) (estate transformation). *See also In re Goldston,* 627 B.R. 841, 864 (Bankr. D.S.C. 2021) (stating that 'The Fourth Circuit has expressly avoided reconciling the interplay between §§ 1306(a) and 1327(b).'); *Sec. Bank of Marshalltown v. Neiman*, 1 F.3d 687, 690 (8th Cir. 1993) (holding that estate exists after confirmation even if it holds no property")).

> (1) all property of the kind specified in such section 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, 11, or 12 of this title, 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, 11, or 12 of this title, whichever occurs first.

Read together, sections 541 and 1306 appear to encompass all property of the estate that a debtor owns as of the petition date and any property acquired during the pendency of a chapter 13 case before closure or conversion. In contrast to sections 541 and 1306, section 1327 vests all estate property in the debtor at confirmation and creates the crux of the issue here.

Section 1327, in pertinent part, states:

> (b) Except as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor.
>
> (c) Except as otherwise provided in the plan or in the order confirming the plan, the property vesting in the debtor under subsection (b) of this section is free and clear of any claim or interest of any creditor provided for by the plan.[3]

But given these competing code sections, what if any, property remains part of the bankruptcy estate post-confirmation? According to section 1327, "confirmation of a plan vests *all of the property of the estate in the debtor*" and "property vesting in the debtor under [section 1327] is free and clear of any claim or interest of any creditor provided for by the plan." 11 U.S.C. § 1327(b), (c) (emphasis added). However, section 1306 seemingly stands in direct conflict with section 1327 posing "estate property includes . . . property of the kind specified in

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[3]Under section 1327(b), the Plan or Order Confirming the Plan could have included a provision excluding any property appreciation from revesting in Debtor. *See e.g., In re Euler*, 251 B.R. 740, 747 (Bankr. M.D. Fla 2000).

section 541 [and] *all property of the kind specified in such section 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, 11, or 12 of this title, whichever occurs first." 11 U.S.C. § 1306(a) (emphasis added).

A reading of the plain language of section 1306(a) appears to render all property until "the case is closed, dismissed, or converted," property of the estate. On the other hand, a reading of the plain language of section 1327(b) appears to vest all property with the debtor post-confirmation. Moreover, section 1327(c) provides that this property is free and clear of any claims. Harmonizing the inharmonious is a tall order. And courts must do so in light of a Supreme Court's recent reminder that "'[t]he canon against surplusage is strongest when an interpretation would render superfluous another part of the same statutory scheme.'" *City of Chicago v. Fulton*, 141 S. Ct. 585, 591 (2021) (citing *Yates v. United States*, 574 U.S. 528, 543 (2015)). Faced with this task, "several courts [] suggest [sections 1306 and 1327] . . . may even be 'impossible to reconcile.'" *In re Scholl*, 605 B.R. at 173 (citing *In re Rangel*, 233 B.R. 191, 194 (Bankr. D. Mass. 1999); *see also In re Barbosa*, 236 B.R. 540, 545 (Bankr. D. Mass. 1999)). The Court believes reconciliation, while difficult, is not impossible, and will add another opinion to the growing discord.

Courts have utilized at least five different theories or "approaches" in their attempts to reconcile sections 1306 and 1327: the Estate Termination approach;[4] the Estate Transformation

[4] *In re Baker*, 620 B.R. 655, 663 (Bankr. D. Colo. 2020) ("At confirmation, the estate ceases to exist and all property of the estate, whether acquired before or after confirmation, becomes property of the debtor.").

approach;[5] the Conditional Vesting approach;[6] the Estate Preservation approach;[7] and the Estate Replenishment approach.[8] *In re Marsh*, 647 B.R. at 730–34; *In re Baker*, 620 B.R. at 663–64 (listing all five approaches).

Many courts have determined—and this Court agrees—that both the Estate Termination and Estate Preservation approaches "render another part of the statutory scheme superfluous." *City of Chicago*, 141 S. Ct. at 591. The Estate Termination approach draws a sharp line at confirmation, vesting all property with debtor, and the "estate ceases to exist." *In re Baker*, 620 B.R. at 663 (citing KEITH M. LUNDIN, LUNDIN ON CHAPTER 13 § 120.3, ¶ [9] (citations omitted); *see also In re Rangel*, 233 B.R. 191 (Bankr. D. Mass. 1999). This approach allows section 1327 to swallow up section 1306. The Estate Preservation approach proposes the opposite–section 1306 engulfing 1327.

> The vesting of property in the debtor under § 1327(b) does not remove any property from the chapter 13 estate, whether acquired before or after confirmation; property remains in the estate until the case is closed,

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[5] *Id*. ("At confirmation, all property of the estate becomes property of the debtor except property essential to the debtor's performance of the plan; the Chapter 13 estate continues to exist, but it contains only property necessary to performance of the plan, whether acquired before or after confirmation.").

[6] *Id*. at 664 ("At confirmation, vesting gives the debtor an immediate and fixed right to use estate property, but that right is not final until the debtor completes the plan and obtains a discharge.").

[7] *Id*. at 663–64 ("The vesting of property in the debtor under § 1327(b) does not remove any property from the chapter 13 estate, whether acquired before or after confirmation; property remains in the estate until the case is closed, dismissed, or converted. The debtor's rights and responsibilities with respect to property of the estate may change somewhat at confirmation, but the existence and composition of the estate are not disturbed by § 1327(b).").

[8] *Id*. at 663 ("At confirmation, all property of the estate becomes property of the debtor; the Chapter 13 estate continues to exist and 'refills' with property defined in § 1306 that is acquired by the debtor after confirmation, without regard to whether that property is necessary to performance of the plan.").

> dismissed, or converted. The debtor's rights and responsibilities with respect to property of the estate may change somewhat at confirmation, but the existence and composition of the estate are not disturbed by § 1327(b).

In re Baker, 620 B.R. at 663–64 (citing LUNDIN at § 120.3¶ [9]).

Because the Estate Termination and Preservation approaches effectively render the competing code section superfluous, this Court adopts a moderate approach, recently favored by other courts faced with this issue–the Estate Replenishment approach. *See e.g., City of Chicago v. Fisher (In re Fisher)*, 203 B.R. 958, 962–63 (Bankr. N.D. Ill. 1997); *Fritz Fire Protect. Co. v. Wei-Fung Chang (In re Chang)*, 438 B.R. 77, 83 (Bankr. M.D. Pa. 2010); *see also In re Marsh*, 647 B.R. 725 (Bankr. W.D. Mo. 2023); *In re Larzelere*, 633 B.R. 677 (Bankr. D. N.J. 2021; *In re Willard*, 2023 WL 2601769 (S.D.N.Y. Mar. 22, 2023)).

The Estate Replenishment approach provides "[a]t confirmation, all property of the estate becomes property of the debtor; the Chapter 13 estate continues to exist and 'refills' with property defined in § 1306 that is acquired by the debtor after confirmation, without regard to whether that property is necessary to performance of the plan." *In re Baker*, 620 B.R. at 663 (citing LUNDIN).

These facts are undisputed. Debtor listed the Van Buren Property on her Schedule A/B at $250,000. Her plan was confirmed on July 31, 2021; following confirmation, the Van Buren Property significantly appreciated in value—selling for $435,000. With the Trustee's consent, the Court approved the sale, Debtor sold the Van Buren Property, and the Sale Proceeds are being held in the Debtor's attorney's IOLTA account. Application of the Estate Replenishment approach vests the Van Buren Property in the Debtor at confirmation.

The Court finds the Van Buren Property was property of the estate until it confirmed Debtor's Plan. Following confirmation, the Van Buren Property vested in Debtor. The estate continues to exist and will "refill" with any property acquired post-confirmation. The Court now pivots to whether the Sale Proceeds are newly acquired post-confirmation property that refill the estate.

B. Post-Confirmation Sale Proceeds Cannot Be Separated from the Debtor's Pre-Confirmation Property from Which They Were Derived

Sale Proceeds must fall into either one of two categories to be considered post-confirmation estate property: (1) under the Estate Replenishment approach, the Sale Proceeds refill the bankruptcy estate post-confirmation because they are newly acquired property of the Debtor; or (2) the Sale Proceeds are disposable income encompassed by 11 U.S.C. § 1325. Neither categorization is persuasive.

1. The Sale Proceeds do not refill the estate

Several courts have addressed whether proceeds from the sale of prepetition property derived from post-confirmation appreciation are newly acquired property of a debtor. Unsurprisingly, courts have come down on both sides of the issue. The Court adopts what it believes is the better-reasoned line of cases and holds the Sale Proceeds cannot be untethered from the underlying Van Buren Property and therefore, are not a newly acquired asset of Debtor.

Courts have determined chapter 7 bankruptcy estates capture appreciation of prepetition property as property of the estate, despite proceeds being attributable to post-petition appreciation. *See e.g., Coslow v. Reisz,* 811 Fed. App'x 980 (6th Cir. 2020); *In re Lents*, 644 B.R. 479 (Bankr. D. S.C. 2022). The Court finds it unnecessary to look to Code provisions governing chapter 7 estate property when Debtor received the protections of the chapter 13 bargain. The Court looks to sections 1306, 1335, and 1327, and the chapter 13 case law relying on these sections, to guide its decision.

Even when a chapter 13 case is converted to a chapter 7, courts have found appreciation of prepetition property is property of the estate. *See In re Adams,* 641 B.R 147 (Bankr. W.D. Mich. 2022).[9] The Trustee's Brief relies on the *Adams* holding to suggest a chapter 13 debtor's post-confirmation sale proceeds from prepetition real estate are property of the bankruptcy estate. *See id*. But the *Adams* holding does not extend to the circumstances here because, unlike in *Adams*, Debtor did not convert to a chapter 7.

In *Adams*, the debtors converted their chapter 13 case to a chapter 7 and attempted to retain post-confirmation appreciation of real property, post-conversion. *In re Adams*, 641 B.R. 147 (Bankr. W.D. Mich. 2022). The court never contemplated sections 1306 and 1327, but relied mainly on 11 U.S.C. § 348(f) to determine whether property belonged to the debtor or to the estate. *Id*. Section 348—Effect of Conversion—is not applicable here as Debtor did not convert to a chapter 7. However, a chapter 13 debtor who converts to a 7, does lose the benefit of the bargain given to a chapter 13 debtor. The *Adams* court drove this point home, stating "chapter 13 still presents the best avenue for debtors to retain property in bankruptcy, and the unqualified right to dismiss their chapter 13 proceedings protects them from any adverse consequences of conversion to chapter 7." *In re Adams*, 641 B.R. at 156. Debtor retains the benefit of her bargain struck at confirmation.

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[9]The *Adams* court relied on the Sixth Circuit's reasoning in *Coslow v. Reisz*, where a chapter 7 debtor brought an adversary proceeding to compel the trustee to abandon his residential property. The debtor in *Coslow* filed under chapter 7, and the Sixth Circuit's reasoning as to property of the chapter 7 estate is not binding when resolving estate property issues in a chapter 13 case. *See Coslow v. Reisz,* 811 Fed. App'x 980 (6th Cir. 2020).

Moreover, a debtor's chapter 13 protections are distinguished from that of a debtor's chapter 7 protections. The Supreme Court framed this distinction clearly in *Hamilton v. Lanning*:

> Chapter 13 of the Bankruptcy Code provides bankruptcy protection to "individual[s] with regular income" whose debts fall within statutory limits. 11 U.S.C. §§ 101(30), 109(e). Unlike debtors who file under Chapter 7 and must liquidate their nonexempt assets in order to pay creditors, see §§ 704(a)(1), 726, Chapter 13 debtors *are permitted to keep their property*, but they must agree to a court-approved plan under which they pay creditors out of their future income.

Hamilton v. Lanning, 560 U.S. 505, 508 (2010) (emphasis added).

The Supreme Court in *Bullard v. Blue Hills Bank*, clarified its stance with respect to section 1327's vesting language stating "[s]ubject to certain exceptions, confirmation 'vests all of the property of the [bankruptcy] estate in the debtor' and renders that property 'free and clear of any claim or interest of any creditor provided for by the plan."' 575 U.S. 496, 502 (2015) (citing 11 U.S.C. § 1327(b), (c)).

Many decisions, nationwide, align with this Court's finding. *See e.g., In re Euler*, 251 B.R. 740, 747–48 (Bankr. M.D. Fla. 2000) ("As stated by Judge Jennemann in *In re Meeks,* 237 B.R. 856, 861, 'A debtor who decides to retain collateral at a confirmation hearing is entitled to any later appreciation in value but also must suffer any resulting depreciation or loss."' (citations omitted)); *In re Burgie*, 239 B.R. at 410 ("The chapter 13 deal permits a debtor to retain all prepetition property, including earnings, assets, money in the bank and real estate."); *In re Mobley*, 2011 WL 6812551, at *2 ("'Under a chapter 13 plan, the debtor is entitled to keep all of the debtor's prepetition property' and includes prepetition proceeds…" (quoting *In re Burgie*, 239 B.R. at 410–11)); *In re Ash'shadi*, 2005 WL 1105039, at *3 ("As explained above, the proceeds from the sale of a prepetition asset do not become property of the chapter 13 estate. . .").

The court in *Burgie* laid the framework for a line of cases, which have followed the *Burgie* court's analysis of chapter 13's protections—including two cases decided in the Eastern District of Michigan. *See e.g., In re Burgie*, 239 B.R. 406 (B.A.P. 9th Cir. 1999); *In re Euler*, 251 B.R. 740 (Bankr. M.D. Fla. 2000); *Black v. Leavitt (In re Black*), 609 B.R. 518 (B.A.P. 9th Cir. 2019); *Willard v. Preuss (In re Willard)*, No. 21 Civ 10220, 2023 WL 2601769 (S.D.N.Y. March 22, 2023); *see also In re Ash'shadi*, No. 04-55924, 2005 WL 1105039 (Bankr. E.D. Mich. May 6, 2005) and *In re Mobley*, No. 11-49079, 2011 WL 6812551 (Bankr. E.D. Mich. Dec. 1, 2011).

In *Burgie*, chapter 13 debtors sold their prepetition homestead five days post-confirmation. *In re Burgie*, 239 B.R. at 408. The debtors proposed to use the $63,000 in sale proceeds to purchase a new residence. *Id*. The trustee did not object to debtors' original proposal to dedicate *all* of the post-confirmation sale proceeds to the purchase of a new residence. *Id*. The trustee only objected to debtors' subsequent proposal to use $43,000 of the sale proceeds as a down payment on a new residence, and retain $20,000 "to support themselves and help complete their plan." *Id*. The trustee moved to modify the debtors' plan to require any sale proceeds *not* utilized in the purchase of a new residence to be turned over to the trustee to "provide 100% distribution" to unsecured creditors. *Id*.

The Bankruptcy Appellate Panel for the Ninth Circuit affirmed the bankruptcy court's decision denying the trustee's motion. *Id*. at 412. The court held "debtors cannot be compelled to use the proceeds from the sale of prepetition real estate to pay creditors under a confirmed chapter 13 plan." *Id*. at 410. And despite debtors retaining $20,000 of the sale proceeds, the court further stated "[w]hile a debtor may voluntarily use such proceeds to make payments to creditors under a chapter 13 plan, a debtor cannot be compelled to use the proceeds for this purpose." *Id.* at 409. The Court finds this reasoning persuasive, but does not expand its finding to the extent of the *Burgie* court.

The circumstances here are well within the scope of what the *Burgie* court saw fit for a chapter 13 debtor's post-confirmation sale proceeds. Debtor sold her homestead not five days, but over 20 months after confirmation.[10] Furthermore, the trustee in *Burgie* did not object to the debtors' use of the sale proceeds to purchase a new residence. Only when debtors proposed to retain $20,000 of the proceeds did the trustee object. Therefore, the Court limits its holding to Debtor's specific request: she may use the Sale Proceeds solely to purchase a new residence.[11] The Sale Proceeds must remain in the IOLTA account until transferred directly to close on a new residence. And Debtor must close on said residence *on or before December 31, 2023*—unless the Court extends this deadline, for cause.

Widening the scope on chapter 13 protections, the Southern District Court of New York recently addressed the sale proceeds issue on appeal from the Bankruptcy Court stating "'[a]n examination of the basic structure of chapter 13 makes it clear that the debtors cannot be compelled to' turn over their prepetition property, whether post-confirmation as in *Burgie*, or

[10] The Court entered an Order Confirming Plan on July 31, 2021 [Docket # 35] and the Order Approving Sale of Debtor's Real Property was entered on March 30, 2023 [Docket # 49].

[11] If the cost of the Debtor's new residence is less than the value of the Sale Proceeds, the fate of the excess Sale Proceeds can be addressed by the Trustee at that time. The Court does not contemplate the possibility herein.

pre-confirmation, as here." *In re Willard*, 2023 WL 2601769, at *3 (citing *In re Burgie*, 239 B.R. at 410). The chapter 13 debtor in *Willard* sought to retain sale proceeds of his prepetition property in the amount of $354,333.77, and the trustee objected. *In re Willard*, 2023 WL 2601769. The sale of the debtor's property occurred pre-confirmation and the trustee argued that the sale proceeds were property of the estate, not the debtor's property. *Id*. The district court disagreed with the trustee and Bankruptcy Court, finding the bankruptcy court had abused its discretion in requiring the debtor to turn over the sale proceeds to the trustee. *Id*. at *3.

The court explained that "[c]ompelling a debtor to submit a pre-petition asset to the trustee, and thereby exposing such pre-petition asset to the creditors, runs counter to the congressional design evidenced by Chapter 13's language and structure." *In re Willard*, 2023 WL 2601769, at *3. The Debtor's Sale Proceeds here, arise from a post-confirmation sale and are derived from post-confirmation appreciation. If a debtor cannot be compelled to turnover pre-confirmation sale proceeds derived from pre-confirmation appreciation because "chapter 13 makes it clear that debtors cannot be compelled to turn over their prepetition property," then certainly the protections of chapter 13 further fortified with the post-confirmation protections of section 1327 shield the Debtor's Sale Proceeds here.

The Sale Proceeds are the Debtor's property pursuant to 1327, cannot be separated from the underlying real estate, and according to the Supreme Court "[c]hapter 13 debtors are permitted to keep their property." *Hamilton*, 560 U.S. at 508. Not only does Debtor receive the benefit the bargain struck with her creditors—without the benefit of foresight—but she also receives the fortified protections of section 1327 because the appreciation generating the Sale

Proceeds arose post-confirmation. Consequently, the Sale Proceeds will not refill the bankruptcy estate.

2. The Sale Proceeds are not Disposable Income within the Purview of 11 U.S.C. § 1325

Alternatively, the Sale Proceeds could be categorized as disposable income. If the Sale Proceeds were considered disposable income under 11 U.S.C. § 1325(b), Debtor could be compelled to contribute them to the plan. Because the Court finds the Sale Proceeds are not disposable income, Debtor cannot be compelled to turn them over to her creditors. The Trustee's proposed plan modification is denied as moot.

Section 1325(b)(1) states:

> If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the court may not approve the plan unless, as of the effective date of the plan—
>
> (A) the value of the property to be distributed under the plan on account of such claim is not less than the amount of such claim; or
>
> (B) the plan provides that all of the debtor's projected disposable income to be received in the three-year period beginning on the date that the first payment is due under the plan will be applied to make payments under the plan.

Section 1325(b)(2) defines "disposable income" for the purpose of section 1325(b)(1) and provides in pertinent part:

> For the purposes of this subsection, "disposable income" means current monthly income which is received by the debtor and which is not reasonably necessary to be expended—
>
> (A) for the maintenance or support of the debtor or a dependent of the debtor....

11 U.S.C. § 1325(b)(2).

The Trustee suggests that Debtor must propose a post-confirmation plan modification as required by 11 U.S.C. § 1329, because the Sale Proceeds are disposable income not accounted for in her plan. Further, the Trustee asserts that because Debtor failed to propose a modification, the Trustee, pursuant to 11 U.S.C. § 1329(b)(1), proposed a post-confirmation plan modification to account for the Sale Proceeds. *Id.* The Court disagrees that (1) Debtor is required to propose a modification; and (2) that—under the particular circumstances here—the Trustee may propose a modification, as the Sale Proceeds are not disposable income. Debtor cannot be compelled to turn over any property that vested in her at confirmation.

a. Trustee's Reliance on Sixth Circuit Cases Misses the Mark

The Trustee presents two Sixth Circuit Court of Appeals cases in attempt to drive home her argument that the Sale Proceeds are disposable income. These decisions would be binding if on point, however, their holdings do not apply here. *In re Freeman* involved a post-confirmation plan modification where the court required the debtor to turn over an unexpected surplus in a tax refund derived from prepetition wages. *Freeman v. Schulman (In re Freeman)*, 86 F.3d 478 (6th Cir. 1996). The tax refunds were for prepetition wages, and the Trustee purports that the *Freeman* decision reaches the circumstances in here—but it does not.

The debtor in *Freeman*, upon the realization her tax refund would be in excess of what the plan projected, attempted to exempt the excess under state law. *In re Freeman*, 86 F.3d at 479. In addition, the debtor "specifically identified that tax refunds should go to the plan and made no argument that the funds were needed for 'maintenance and support' of the debtor or her dependents." *Id.* at 481. The court held that the tax refund qualified as disposable income under section 1325. *Id.* However, the court also stated that "[s]ituations may arise where a debtor did not specifically list tax refunds for inclusion in the plan and those situations would need to be examined on a case-by-case basis to decide whether a tax refund arising from pre-petition income qualified as 'projected disposable income."' *Id*.

Debtor neither seeks to exempt the Sale Proceeds under state law nor purports use of projected proceeds from the sale of the Van Buren Property for "maintenance and support" of herself and her children. In fact, at confirmation, the projected sale of the Van Buren Property would have yielded nothing to unsecured creditors after paying secured creditors and Debtor's exemption. And although the Court does not need to look to *Freeman*, it does agree with the recognition that circumstances require "a case-by-case" analysis to determine what constitutes disposable income.

The Trustee also cited *In re Harchar*, which relied on *Freeman* to reach its decision also surrounding tax refunds. *Harchar v. United States (In re Harchar)*, 694 F.3d 639 (6th Cir. 2012). There, the Sixth Circuit held that the IRS was permitted to seek modification of debtor's plan to compel turnover of a post-confirmation tax refund for prepetition wages. *See id*. Appreciation of prepetition real estate that arose post-confirmation, generated the Sale Proceeds here—not prepetition wages. Real property sale proceeds are categorically different than tax refunds. While this Court agrees with the holdings in both *Freeman* and *Harchar*, neither applies under the facts of this case.

b. Anticipated Stream of Payments

Instead of relying on *Freeman* and *Harchar*, this Court adopts the position that "disposable income does not include prepetition property or its proceeds." *In re Burgie*, 239 B.R. at 410. The test in *Burgie* is "whether the asset in question is an anticipated stream of payments.

If it is a stream of payments, the payments must be included in projected income. If the asset is not a stream of payments, it is not included." *Id*. (internal citations omitted).

The court goes on to distinguish a debtor's primary residence from income:

> The sale of a capital asset does not create "disposable income" pursuant to § 1325. Disposable income under § 1325 is postpetition income received by the debtor that is not reasonably necessary for the maintenance or support of the debtor or a dependant of the debtor. *See* § 1325(b)(2). A debtor's prepetition homestead is a capital asset, not postpetition income.

Id.

The court further states "[t]he proceeds of the sale of a debtors real estate in a chapter 13 case never become disposable income for the purposes of chapter 13." *Id*. at 409. The sale of a "capital asset" or a debtor's primary residence generates only a lump-sum payment; it is not an anticipated stream of payments. Although Debtor here planned from the outset to sell her property, not only would the sale generate a lump sum rather than a stream of payments, but the Sale Proceeds were certainly not anticipated. Again, the projected sale—based on the liquidation analysis—was expected to generate only $22,000 in proceeds. Therefore, the Sale Proceeds are not in the anticipated stream of payments for the "maintenance and support" of Debtor's family.

Moreover, as discussed above, the debtors in *Burgie* were not only allowed to use their sale proceeds as a down payment on a new residence, but were permitted to keep $20,000 "to support themselves." *In re Burgie*, 239 B.R. at 408. Despite the debtors actually realizing some of the sale proceeds rather than rolling over all them into a new residence, the court stated "a debtor's homestead is a capital asset" and "[t]he sale of a capital asset does not create disposable income pursuant to § 1325." *Id*. at 410. Debtor proposes to use the Sale Proceeds, in their entirety, to purchase a new residence. The Debtor does not realize any income as defined in section 1325, but is merely rolling over the Sale Proceeds directly into a new (replacement) homestead. The Court holds that the Sale Proceeds are not disposable income insofar they are used solely to purchase Debtor's new homestead. The Court does not make a determination as to the fate of any excess Sale Proceeds above and beyond the new-residence purchase price.

The Court also acknowledges, as the Trustee points out, that the facts of *Mobley* and *Ash'shadi* are different from those here. However, the Court looks to cases in this district not for factual identity but for its application of the stream of income test in a chapter 13 case. Both *Mobley* and *Ash'shadi* apply the stream of income test in a chapter 13 case, and this Court does the same. *See In re Mobley*, 2011 WL 6812551, at *2 ("Chapter 13 contemplates making available an ongoing stream of regularly anticipated income out of which plan payments are to be calculated and made."); *see also In re Ash'shadi*, 2005 WL 1105039, at *3 ("The cases cited by the Trustee in his brief do not control the disposition of the instant case because they all involve a stream of income, or a payment which replaces income, rather than the post-confirmation sale of a pre-petition asset. Specifically, *In re Freeman,* 86 F.3d 478 (6th Cir.1996) involved a post-petition tax refund related to pre-petition income."). The *Ash'shadi* court offered the same argument this Court presented above distinguishing *Freeman*: post-petition tax refunds derived from prepetition income are drastically different from proceeds from the sale of a chapter 13 debtor's primary residence. *See id*. The Court finds that the Sale Proceeds are not disposable income.

C. The Trustee's Proposed Post-Confirmation Plan Modification

The Court does not reach this issue as Debtor cannot be compelled to turn over the Sale Proceeds to the be distributed to general unsecured creditors. The Plan Modification is denied as moot.

V. CONCLUSION

More than 20 years ago, the Sixth Circuit determined it would be an "unlikely congressional intent" to give Chapter 13 debtors–post-confirmation—"the option to shift the burden of depreciation to a secured creditor by reclassifying the claim and surrendering the collateral when the debtor no longer has any use for the devalued asset." *Chrysler Fin. Corp. v. Nolan (In re Nolan)*, 232 F.3d 528, 533 (6th Cir. 2000). In other words, Chapter 13 debtors assume the risk of depreciation in their revested assets. It stands to reason they should also enjoy the benefit of any post-confirmation appreciation of revested property when sold.

The Court finds the Estate Replenishment approach best reconciles the disparities between 11 U.S.C.§§ 1306 and 1327, and that—at confirmation—all property of Debtor's chapter 13 bankruptcy estate vested in her. The bankruptcy estate continues to exist and can be refilled with a debtor's newly acquired post-confirmation property.

The Sale Proceeds are not newly acquired property as they cannot be untethered from the underlying Van Buren Property. The appreciation of the Van Buren Property occurred post-confirmation, which vested with the Debtor at confirmation. *See* 11 U.S.C. § 1327. Thus, the Debtor "cannot be compelled to turn over prepetition property." Furthermore, the Sale Proceeds are not disposable income as they are not in the anticipated steam of payments. Accordingly, Debtor may use all of the Sale Proceeds to purchase a new residence *on or before December 31, 2023*, unless the Court extends this deadline, for cause. The Trustee's Objection is **OVERRULED**, and her Plan Modification is **DENIED** as moot.

IT IS ORDERED.

Signed on August 28, 2023

/s/ Mark A. Randon

Mark A. Randon
United States Bankruptcy Judge

FOR PUBLICATION

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

In the Matter of: JOHN FELIX CASTLEMAN, Sr.; KIMBERLY KAY CASTLEMAN, *Debtors,*	No. 22-35604
------------------------------	D.C. No. 2:21-cv-00829-JHC
JOHN FELIX CASTLEMAN, Sr.; KIMBERLY KAY CASTLEMAN, *Appellants,*	OPINION
v.	
DENNIS LEE BURMAN, Chapter 7 Trustee, *Appellee.*	

Appeal from the United States District Court
for the Western District of Washington
John H. Chun, District Judge, Presiding

Argued and Submitted May 9, 2023
Seattle, Washington

Filed July 28, 2023

Before: Michael Daly Hawkins, Richard C. Tallman, and Sandra S. Ikuta, Circuit Judges.

Opinion by Judge Hawkins;
Dissent by Judge Tallman.

SUMMARY*

Bankruptcy

Affirming the district court's order, which affirmed the bankruptcy court's order, the panel held that post-petition, pre-conversion increases in the equity of an asset belong to the bankruptcy estate, rather than to debtors who, in good faith, convert their Chapter 13 reorganization petition into a Chapter 7 liquidation.

When debtors filed for bankruptcy, they listed their home among their assets. When they later converted to Chapter 7, the home had risen in value. Debtors argued that the home's increased equity belonged to them and not the bankruptcy estate under 11 U.S.C. § 348(f)(1)(A), which provides that "property of the estate in the converted case shall consist of property of the estate, as of the date of filing of the petition, that remains in the possession of or is under the control of the debtor on the date of conversion."

* This summary constitutes no part of the opinion of the court. It has been prepared by court staff for the convenience of the reader.

On de novo review, the panel held that the plain language of § 348(f)(1)(A), coupled with the Ninth Circuit's previous interpretation of 11 U.S.C. § 541(a), compelled the conclusion that any appreciation in the property value and corresponding increase in equity belonged to the estate upon conversion. The panel looked to the definition of "property of the estate" in § 541(a), which addresses the contents of the bankruptcy estate upon filing under either Chapter 7 or Chapter 13, and the court's prior opinions holding that the broad scope of § 541(a) means that post-petition appreciation inures to the bankruptcy estate, not the debtor.

Dissenting, Judge Tallman wrote that the Bankruptcy Code as a whole established that post-petition, pre-conversion appreciation belonged to the debtors. He wrote that the majority's reading of § 348(f)(1)(A) created a circuit split and was inconsistent with the statute's structure, object, policies, and legislative history.

COUNSEL

Steven Hathaway (argued), Law Office of Steven C. Hathaway, Bellingham, Washington, for Appellants.

Peter H. Arkison (argued), Bellingham, Washington, for Appellee.

Russell D. Garrett, Jordan Ramis PC, Portland, Oregon, for Amicus Curiae National Association of Bankruptcy Trustees.

OPINION

HAWKINS, Circuit Judge:

We must decide whether post-petition, pre-conversion increases in the equity of an asset—i.e., the difference between a home's value and how much is owed on the mortgage, whether a result of market appreciation, payment of secured debt, improvements or otherwise—belong to the bankruptcy estate or to debtors who, in good faith, convert their Chapter 13 reorganization petition into a Chapter 7 liquidation.

Debtors John Felix Castleman, Sr. and Kimberly Kay Castleman (the "Castlemans") filed for Chapter 13 bankruptcy. They listed their home among their assets with a value of $500,000, a mortgage with an outstanding balance of $375,077, and a homestead exemption of $124,923. The bankruptcy court confirmed a Chapter 13 plan, but after roughly twenty months, which included a temporary job loss and deferral of mortgage payments due to the pandemic, Mr. Castleman contracted Parkinson's Disease, and the couple could no longer make their required payments. The Castlemans exercised their right to convert to Chapter 7. In the interim, their home had risen in value an estimated $200,000.[1] Dennis Burman, the Chapter 7 trustee ("Trustee"), filed a motion to sell the Castlemans' home to recover the value for creditors. The Castlemans objected and argued that the home's increased equity belongs to them and

[1] In this case, it appears the increase in equity was attributable primarily, if not exclusively, to market appreciation. Due to the deferral of mortgage payments during the pandemic, the Castlemans actually owed more at the time of filing for conversion ($390,763) than they did at the time of their initial filing.

not the bankruptcy estate under 11 U.S.C. § 348(f)(1)(A).[2]

Although courts are heavily divided on this question,[3] we conclude on de novo review, *Simpson v. Burkart (In re Simpson)*, 557 F.3d 1010, 1014 (9th Cir. 2009), that the plain language of § 348(f)(1)(A), coupled with this circuit's previous interpretation of § 541(a), compel the conclusion that any appreciation in the property value and corresponding increase in equity belongs to the estate upon conversion. We therefore affirm the decisions of the bankruptcy and district courts.

The purpose of the Bankruptcy Code is to grant a "fresh start to the honest but unfortunate debtor." *Marrama v. Citizens Bank of Mass.*, 549 U.S. 365, 367 (2007) (internal quotation marks and citation omitted). Individual debtors may petition for bankruptcy under Chapter 7 (liquidation) or Chapter 13 (reorganization). *Harris v. Viegelahn*, 575 U.S. 510, 513–14 (2015). Chapter 13 "allows a debtor to retain his property if he proposes, and gains court confirmation of, a plan to repay his debts over a three-to-five-year period." *Id.* at 514 (citing §§ 1306(b), 1322, 1327(b)). Chapter 13 can benefit the debtor and creditors: the former keeps his assets, and the latter "usually collect more under a Chapter 13 plan than they would have received

[2] Unless otherwise noted, all statutory references are to the Bankruptcy Code, 11 U.S.C. §101 et seq.

[3] *Compare In re Goins*, 539 B.R. 510, 515–16 (Bankr. E.D. Va. 2015), *In re Goetz*, 647 B.R. 412, 416–17 (Bankr. W.D. Mo. 2022), *In re Peter*, 309 B.R. 792, 794–95 (Bankr. D. Or. 2004), and *Potter v. Drewes* (*In re Potter*), 228 B.R. 422, 424 (B.A.P. 8th Cir. 1999), *with In re Barrera*, 22 F.4th 1217 (10th Cir. 2022), *In re Cofer*, 625 B.R. 194, 202 (Bankr. D. Idaho 2021), *In re Hodges*, 518 B.R. 445, 451 (E.D. Tenn. 2014), and *In re Niles*, 342 B.R. 72, 75 (Bankr. D. Ariz. 2006).

under a Chapter 7 liquidation." *Id.*

However, most debtors fail to successfully complete a Chapter 13 repayment plan, which is why "Congress accorded debtors a nonwaivable right to convert a Chapter 13 case to one under Chapter 7 'at any time.'" *Id*. (quoting § 1307(a)). The property of this converted Chapter 7 estate is defined by § 348(f), which provides in relevant part:

> (1) Except as provided in paragraph (2), when a case under chapter 13 of this title is converted to a case under another chapter under this title-
>
> (A) property of the estate in the converted case shall consist of **property of the estate, as of the date of filing of the petition, that remains in the possession of or is under the control of the debtor on the date of conversion**;
>
> [. . .]
>
> (2) If the debtor converts a case under chapter 13 of this title to a case under another chapter under this title in bad faith, the property of the estate in the converted case shall consist of the property of the estate as of the date of conversion.

(emphasis added). The Trustee does not assert that the Castlemans converted in bad faith, and the Castlemans retained possession of the home on the date of conversion.

In interpreting the Bankruptcy Code, "the first step . . . is to determine whether the language [of a statute] has a plain and unambiguous meaning with regard to the particular dispute." *Hawkins v. Franchise Tax Bd. of Cal.*, 769 F.3d 662, 666 (9th Cir. 2014). If the plain meaning is unambiguous, it controls. *Id.*; *Puerto Rico v. Franklin Cal. Tax-Free Tr.*, 579 U.S. 115, 125 (2016).

Section 348(f) does not define the word "property" or the phrase "property of the estate." However, "property of the estate" is a term of art which appears throughout the Bankruptcy Code. *See, e.g.*, §§ 541, 554(a), 726(a), 1306(a); *see also* Keith M. Lundin, *Lundin On Chapter 13* § 46.1 (2023) ("'Property of the estate' is a phrase of art that is fundamental to almost everything that happens in Chapter 13 practice."); 4 William L. Norton III, *Norton Bankruptcy Law and Practice* § 61:1 (3d ed. 2023) ("[F]or more than two centuries 'property of the estate' has become a term of art unique to bankruptcy law.").

"Statutory construction . . . is a holistic endeavor. A provision that may seem ambiguous in isolation is often clarified by the remainder of the statutory scheme." *United Sav. Ass'n of Tex. v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 371 (1988). We therefore look to the definitions of "property of the estate" set forth in other provisions of the Code itself. *See Robinson v. Shell Oil Co.*, 519 U.S. 337, 340 (1997) ("The plainness or ambiguity of statutory language is determined by reference to the language itself, the specific context in which that language is used, and the broader context of the statute as a whole.").

Under § 541(a)(1), filing for bankruptcy creates an estate which includes "all legal or equitable interests of the debtor in property as of the commencement of the case." The estate also includes all "[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." § 541(a)(6).

In *In re Goins*, the court found the trustee was entitled to any post-petition appreciation in assets of the estate, explaining: "[T]he equity attributable to the post-petition appreciation of the property is not separate, after-acquired property . . . The equity is inseparable from the real estate, which was always property of the estate under Section 541(a)." 539 B.R. at 516; *see also In re Goetz*, 647 B.R. at 416 (the broad definition of "property of the estate" in § 541(a) "captures the debtor's entire ownership interest in each asset that exists on the petition date without fixing the estate's interest to the precise characteristics the asset has on that date"). Other courts have held that any post-petition increase in the property's equity is the "proceeds, product, offspring, rents or profits" of the estate's original property under § 541(a)(6), and so became part of the estate when the case commenced. *See In re Potter*, 228 B.R. at 424; *In re Peter*, 309 B.R. at 794–95.

In this circuit, we have likewise concluded that the broad scope of § 541(a), and especially § 541(a)(6), means that post-petition "appreciation [i]nures to the bankruptcy estate, not the debtor." *Schwaber v. Reed* (*In re Reed*), 940 F.2d 1317, 1323 (9th Cir. 1991). We recently re-affirmed this in *Wilson v. Rigby*, noting that when a debtor files for bankruptcy, the "proceeds, product, offspring, rents, or profits" which become part of the estate under § 541(a)(6) "include[] the appreciation in value of a debtor's home." 909 F.3d 306, 309 (9th Cir. 2018). The Castlemans point out that *Wilson* was originally filed as a Chapter 7 case, but the definition of property of the estate in § 541(a) applies equally to Chapter 13. There is no textual support for concluding that § 541(a) has a different meaning upon conversion from Chapter 13. As the district court in this case aptly summarized the significance of these prior Ninth Circuit decisions:

> It is well settled that in a Chapter 7 case, all property that the debtor acquires post-petition is excluded from the estate. *See, e.g., Harris*, 575 U.S. at 514 (citing § 541(a)(1)). Therefore, if appreciation were a separate, after-acquired property interest, it would have to inure to the debtor. The Ninth Circuit, in finding that appreciation inures to the estate under § 541(a)(6), has necessarily found that increased equity in a pre-petition asset cannot be a separate, after-acquired property interest. This logic applies with equal force in a conversion case.

Many of the courts who have reached a different conclusion regarding post-petition changes in equity have relied on various statements or examples in the legislative history surrounding § 348(f), which was enacted to clarify whether new property acquired during the course of Chapter 13 proceedings becomes property of the converted estate (under § 348(f)(2), this occurs only if the debtor was acting in bad faith). *See, e.g., In re Cofer*, 625 B.R. at 200–02; *In re Nichols*, 319 B.R. at 856. However, because we conclude the language of § 348(f), when read in conjunction with the remainder of the Bankruptcy Code, is not ambiguous, we do not look to legislative history for guidance. *Robinson*, 519

U.S. at 340 ("Our inquiry must cease if the statutory language is unambiguous.").[4]

Some courts have also relied on the implicit operation of § 1327(b), which provides: "Except as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor." Under this reasoning, equity increases from the time of the initial filing up until plan confirmation would inure to the estate, then from time of confirmation until conversion would vest in the debtor, and finally upon conversion, any additional post-conversion changes would benefit the estate. *See, e.g., In re Barrera*, 22 F.4th at 1223–24. However, we find it difficult to believe Congress envisioned this valuation and accounting process without making any explicit cross-reference to § 1327(b), and because in other instances where Congress wanted to exclude assets or certain interests of the debtor from the bankruptcy estate, it has done so with specificity. *See, e.g.,*

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[4] We recognize that some courts have found § 348(f) to be ambiguous. However, the existence of a division of judicial authority does not itself establish ambiguity in the text. *See, e.g., Roberts v. Sea-Land Servs., Inc.*, 132 S. Ct. 1350 (2012) (holding provision of Longshore and Harbor Workers' Compensation Act is unambiguous despite disagreement between Fifth, Ninth and Eleventh Circuits); *Mohamad v. Palestinian Auth.*, 132 S. Ct. 1702 (holding term used in Torture Victim Protection Act was unambiguous despite disagreement among several circuits); *Reno v. Koray*, 515 U.S. 50, 64–65 (1995) ("A statute is not ambiguous for purposes of lenity merely because there is a division of judicial authority over its proper construction.") (internal quotation and citation omitted). As we have explained, even if § 348(f) in isolation might be ambiguous, when read in connection with the remainder of the bankruptcy statute as already interpreted by this circuit, its meaning becomes clear. *See United Sav. Ass'n of Tex.*, 484 U.S. at 371 ("A provision that may seem ambiguous in isolation is often clarified by the remainder of the statutory scheme.").

§ 541(a)(6) (excluding post-petition earnings by an individual in a Chapter 7 case) and § 541(b) (excluding various specific items from the estate, such as funds used to purchase a 529 education plan). If, as the dissent suggests, Congress actually intended to exclude from the revived estate any increase in equity of an estate asset that may have occurred from the time of plan confirmation to conversion, it could have amended § 348(f) further to make this result clear. As written, § 348(f) only clarified that newly-acquired, post-petition property would not become part of the converted estate if the debtor had been acting in good faith.

In sum, the plain language of § 348(f)(1) dictates that any property of the estate at the time of the original filing that is still in debtor's possession at the time of conversion once again becomes part of the bankruptcy estate, and our case law dictates that any change in the value of such an asset is also part of that estate. In this case, that property increased in value. In other cases, the value might decline, or the value of one asset in the estate might increase while other property depreciates in value. This is simply a happenstance of market conditions, which sometimes will benefit the debtor and sometimes benefit the estate.[5] The district court and bankruptcy court correctly concluded that the Castlemans' home (including any post-petition, pre-conversion increase in equity) was again part of the bankruptcy estate pursuant

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[5] Note that, for example, the debtor's homestead exemption is fixed as of the "snapshot" value on the date of the original filing. *See Hyman v. Plotkin (In re Hyman)*, 967 F.2d 1316, 1321 (9th Cir. 1992) ("Were we to accept the Hymans' argument that they're entitled to post-filing appreciation, we would also have to hold that a debtor is subject to post-filing *de*preciation, which would give debtors in falling property markets less than the [homestead exemption] guaranteed them by state law.").

to § 348(f)(1) and available to the Trustee for the benefit of the creditors.[6]

AFFIRMED.[7]

TALLMAN, Circuit Judge, dissenting.

As counsel for the trustee aptly put it, John and Kimberly Castleman "tried to do good and tried to pay off their bills" by petitioning for bankruptcy under Chapter 13 and proposing a plan to repay their creditors.[1] But, unable to complete the repayment plan, they were forced into a Chapter 7 liquidation. We now must decide whether appreciation in the value of their home during Chapter 13 proceedings becomes part of the converted Chapter 7 bankruptcy estate—an issue which has confounded judges all over the country. In holding that postpetition, pre-conversion increases in equity belong to the estate, the court both creates a circuit split and effectively punishes the Castlemans for filing under Chapter 13 with the forced sale

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[6] As noted above, in this case it appears that the increased equity was attributable to market conditions. However, the district court indicated that the debtors could file an administrative priority claim for mortgage payments they had made in accordance with the confirmation plan for the benefit of the estate pursuant to § 503(b). *See In re Peter*, 309 B.R. at 795. The resolution of any such claim is not before us at this time.

[7] The motion filed by National Association of Bankruptcy Trustees for leave to file an amicus brief [Dkt. Entry No. 17] is granted. The amicus brief filed on January 9, 2023, is deemed filed.

[1] Oral Argument at 14:07, *Castleman, Sr., v. Burman*, No. 22-35604 (9th Cir. May 9, 2023), https://www.youtube.com/watch?v=_TBWjDPd10k.

of their home. Because that outcome is not the best reading of the Bankruptcy Code or our precedents, I respectfully dissent.

I

A

Upon filing for bankruptcy, a debtor's assets are immediately transferred to a bankruptcy estate. 11 U.S.C. § 541(a). However, the debtor may exempt some property—such as an equitable interest in real property used as a residence—from the estate. *See* § 522(b)(3)(A), (d)(1). This exemption is commonly referred to as the "homestead exemption." In 2019, Washington State allowed a maximum homestead exemption of $125,000. WASH. REV. CODE § 6.13.030 (2019). After creation of the estate, the bankruptcy court appoints a trustee to oversee it for the benefit of creditors and other interested parties. *See* 11 U.S.C. §§ 704, 1302. If, after accounting for encumbrances and exemptions, a particular asset is "of inconsequential value and benefit to the estate," a debtor may ask the court to "order the trustee to abandon" it. § 554(b).

Filing under Chapter 7 "allows a debtor to make a clean break from his financial past, but at a steep price: prompt liquidation of the debtor's assets." *Harris v. Viegalahn*, 575 U.S. 510, 513 (2015). The trustee will sell the non-exempt property of the estate and distribute the proceeds to creditors. *Id*. (citing §§ 704(a)(1), 726). But the Chapter 7 estate does not include wages earned or assets acquired by the debtor after filing for bankruptcy. *Id*. at 513-14. After liquidation, the debtor's pre-petition debts will generally be discharged. § 727(a). "Thus, while a Chapter 7 debtor must forfeit virtually all his prepetition property, he is able to make a 'fresh start' by shielding from creditors his postpetition earnings and acquisitions." *Harris*, 575 U.S. at 514.

A Chapter 13 estate works quite differently: the debtor retains possession of all property, § 1306(b), and proposes a plan to repay creditors over a three-to-five-year period. §§ 1321-22. If the bankruptcy court confirms the plan, confirmation "vests all of the property of the estate in the debtor" unless the plan or a court order says otherwise. § 1327(b). However, "property accumulated during the repayment period becomes part of the bankruptcy estate and is used to repay creditors." *Brown v. Barclay* (*In re Brown*), 953 F.3d 617, 620 (9th Cir. 2020). The Bankruptcy Code encourages Chapter 13 filings because they can "benefit debtors and creditors alike." *Harris*, 575 U.S. at 514. Debtors may keep assets, such as a home or car, and creditors "usually collect more under a Chapter 13 plan than they would have received under a Chapter 7 liquidation." *Id*.

When a debtor converts from Chapter 13 to Chapter 7 in good faith, the property of the converted estate is defined by § 348(f)(1)(A), which provides that the "property of the estate in the converted case shall consist of property of the estate, as of the date of filing of the petition, that remains in the possession of or is under the control of the debtor on the date of conversion."[2] This statute removes a potential disincentive to Chapter 13 filings: if all assets acquired after filing of the Chapter 13 petition were available to creditors after conversion, the debtor would be "in a worse position than if the petition had been filed in Chapter 7 initially."

[2] If a debtor converts in bad faith, § 348(f)(2) makes postpetition, pre-conversion acquisitions available to creditors. Here, all agree the Castlemans converted in good faith due to a pandemic layoff and Mr. Castleman's unfortunate medical diagnosis.

Brown, 953 F.3d at 620. By limiting the converted estate to the property a debtor had at the time of the initial petition, § 348(f) "put[s] the debtor where he would have been, had he filed in Chapter 7 initially." *Id*.

B

On June 19, 2019, when the Castlemans petitioned for bankruptcy under Chapter 13, their home was worth an estimated $500,000. They claimed a homestead exemption of $124,923, which was only $77 less than the legally allowed maximum under then-existing Washington law. The Castlemans also reported that their home was encumbered by a secured mortgage of $375,077. The bankruptcy court confirmed their Chapter 13 plan on September 25, 2019, and the Castlemans made payments under the plan for twenty months, including a mortgage payment.

On January 12, 2021, with Mr. Castleman unable to work and facing a significant loss of income, the couple moved to convert their case to Chapter 7. After conversion, the Chapter 7 trustee hired a realtor, who estimated the Castlemans' Bellingham home was worth $700,000 as of April 19, 2021. Believing the home now had value to the estate, the trustee filed a motion to sell it so that the additional equity could be distributed to creditors. The Castlemans objected, arguing that postpetition, pre-conversion increases in equity are not "property of the estate" upon conversion under § 348(f)(1)(A). This is the question that divides our panel.

II

A

The Castlemans' reading of § 348(f) is correct. In interpreting the Bankruptcy Code, we must begin with the text. *Hawkins v. Franchise Tax Bd. of Cal.*, 769 F.3d 662, 666 (9th Cir. 2014). There is no debate that the phrase "property of the estate" in § 348(f) is a term of art in bankruptcy law or that the term should be defined by looking to the "broader context of the [Bankruptcy Code] as a whole." *Robinson v. Shell Oil Co.*, 519 U.S. 337, 341 (1997). But the court errs in how it applies those principles here. By adopting the trustee's preferred interpretation of § 348(f), the majority sacrifices the text of the bankruptcy statutes on the altar of simplicity.

The court rightly begins by looking to § 541(a), which defines the property of the bankruptcy estate upon filing under either Chapter 7 or Chapter 13. Section 541(a)(1) declares that the estate includes "all legal or equitable interests of the debtor in property as of the commencement of the case." It also includes all "[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." § 541(a)(6). We have already held that in a Chapter 7 case, § 541(a)(6) means that "appreciation enures to the bankruptcy estate, not the debtor." *Schwaber v. Reed* (*In re Reed*), 940 F.2d 1317, 1323 (9th Cir. 1991). This is because in Chapter 7, the "proceeds, product, offspring, rents, or profits of or from property of the estate" under § 541(a)(6) "include[] the appreciation in value of a debtor's home." *Wilson v. Rigby*, 909 F.3d 306, 309 (9th Cir. 2018).

The majority decides that because we have held appreciation becomes part of the estate in a Chapter 7 case, the same must be true in Chapter 13.[3] Admittedly, this is a simple resolution to an issue that has vexed bankruptcy courts across the country.[4] But simplicity cannot take precedence over the text of the Bankruptcy Code, and if we read § 348(f) in light of the Code "as a whole"—rather than just § 541(a)—*Wilson* is not dispositive. *See Robinson*, 519 U.S. at 341. The remainder of the Bankruptcy Code clarifies that in Chapter 13 cases, "property of the estate" is defined differently. § 348(f)(1)(A).

As discussed, a Chapter 7 estate is short-lived: it sweeps in all the debtor's property upon filing and is promptly liquidated to pay creditors. § 541(a)(1); *Brown*, 953 F.3d at 620. But in Chapter 13, the debtor retains possession of all property, § 1306(b), and proposes a plan to repay creditors

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[3] The trustee's briefing faults the Castlemans for not claiming the increase in equity as exempt. But property which does not become part of the converted estate belongs to the debtor regardless of exemptions. *See Harris*, 575 U.S. at 521.

[4] *Compare In re Goins*, 539 B.R. 510, 515-16 (Bankr. E.D. Va. 2015) (holding appreciation belongs to the estate), *In re Goetz*, 647 B.R. 412, 416-17 (Bankr. W.D. Mo. 2022) (same), *aff'd*, 651 B.R. 292 (B.A.P. 8th Cir. 2023), *In re Hayes*, Case No. 15-20727-MER, 2019 Bankr. LEXIS 4203, at *22, (Bankr. D. Colo. March 28, 2019) (same), *and In re Peter*, 309 B.R. 792, 794-95 (Bankr. D. Or. 2004) (same), *with In re Barrera* (*Barrera I*), 620 B.R. 645, 649-54 (Bankr. D. Colo. 2020) (holding appreciation belongs to the debtor), *aff'd*, *Barrera II*, No. BAP CO-20-003, 2020 WL 5869458 (B.A.P. 10th Cir. Oct. 2, 2020), *In re Cofer*, 625 B.R. 194, 202 (Bankr. D. Idaho 2021) (same), *In re Hodges*, 518 B.R. 445, 451 (E.D. Tenn. 2014) (same), *In re Niles*, 342 B.R. 72, 75-76 (Bankr. D. Ariz. 2006) (same), *In re Boyum*, No. 05–1044–AA, 2005 WL 2175879, at *2-3 (D. Or. Sept. 6, 2005) (same), *and In re Nichols*, 319 B.R. 854, 857 (Bankr. D. Ohio 2004) (same).

over a period of years. *See* §§ 1321-22. If the bankruptcy court confirms that plan, confirmation "vests all of the property of the estate *in the debtor*" unless the plan or a court order says otherwise. § 1327(b) (emphasis added).[5] Thus, upon confirmation of a Chapter 13 plan, the debtor is once again the owner of the property. *Cal. Franchise Tax Bd. v. Jones* (*In re Jones*), 420 B.R. 506, 514-15 (B.A.P. 9th Cir. 2009), *aff'd,* 657 F.3d 921, 928 (9th Cir. 2011); *see also Berkley v. Burchard* (*In re Berkley*), 613 B.R. 547, 552-53 (B.A.P. 9th Cir. 2020).

It follows that when a Chapter 13 plan has been confirmed, appreciation accrues to the debtor. In *Black v. Leavitt* (*In re Black*), our Bankruptcy Appellate Panel (BAP) considered a case where the debtor moved to sell a rental property after the bankruptcy court had confirmed a Chapter 13 plan revesting that property in the debtor. 609 B.R. 518, 521 (B.A.P. 9th Cir. 2019). The bankruptcy court ordered the debtor to turn over the proceeds of the sale to the trustee. *Id*. at 523. On appeal, the trustee argued that the proceeds and any postpetition appreciation in the property's value were part of the estate under §§ 541(a)(6) and 1306. *Id*. at 528. The BAP rejected that argument, holding that "the revesting provision of the confirmed plan means that the debtor owns the property outright and that the debtor is entitled to any postpetition appreciation." *Id*. at 529.

The Tenth Circuit reached a similar conclusion in *Rodriguez v. Barrera* (*Barrera III*), 22 F.4th 1217 (10th Cir. 2022). There, the debtors confirmed their Chapter 13 plan, sold their home, and then converted from Chapter 13 to Chapter 7 under § 348(f)(1)(A). *Id*. at 1221-22. Observing that "only proceeds 'of or from property of the estate'

[5] No such provision or order exists in this case.

become property of the bankruptcy estate" under § 541(a)(6), the Tenth Circuit concluded that section is "operative only before confirmation of the Chapter 13 plan because confirmation 'vests all of the property of the estate in the debtor.'" *Id.* at 1223 (quoting § 1327(b)). "Thus, proceeds generated from the debtor's property after confirmation do not become property of the estate as the underlying property no longer belongs to the estate." [6] *Id.*

The Tenth Circuit declined to decide whether postpetition, pre-conversion appreciation would be included in the converted estate when the property has not been sold before conversion. *Id*. at 1223 n.1. But while this case does not involve a pre-conversion sale, we have already held that postpetition appreciation—like the cash proceeds from the sale in *Barrera III*—is "proceeds" of estate property under § 541(a)(6). *Wilson*, 909 F.3d at 309. Here, the underlying property is the Castlemans' home, and their Chapter 13 plan was confirmed on September 29, 2019. When that occurred,

[6] The majority claims this interpretation of § 1327(b) would require a third valuation at confirmation because the trustee would be entitled to pre-confirmation appreciation. Op. at 10-11. But the Tenth Circuit did not adopt this approach, *see Barrera III*, 22 F.4th at 1223-24, and neither should we. In most Chapter 13 cases, the debtor must propose a plan within 14 days of the petition date, *see* FED. R. BANKR. P. 3015(b), and the creditors' meeting generally occurs within 50 days of the petition date, see FED. R. BANKR. P. 2003(a). A confirmation hearing must occur within 45 days of that. 11 U.S.C. § 1324(b). Thus, for most debtors, a Chapter 13 plan will either be confirmed within a few months of the initial petition, or else the case will be dismissed or converted. A property will virtually never significantly change in value in such a short period—in fact, the realtor hired in this case estimated the 2021 value of the Castlemans' home by reviewing sales of comparable homes over a period of six months. If we followed our sister circuit's approach, all postpetition appreciation would belong to the Castlemans.

the home was no longer "property of the estate" and therefore any appreciation in its value is not "[p]roceeds . . . of or from property of the estate."[7] § 541(a)(6). I would hold, consistent with the Tenth Circuit, that postpetition, pre-conversion appreciation belongs to the Castlemans rather than the converted Chapter 7 estate. *See United States v. Anderson*, 46 F.4th 1000, 1005 (9th Cir. 2022) ("In cases requiring statutory interpretation . . . we will not create a circuit split unnecessarily.").

B

While the text of the Bankruptcy Code as a whole establishes that postpetition, pre-conversion appreciation belongs to the Castlemans, the majority's reading of § 348(f)(1)(A) is also inconsistent with the statute's structure, object, policies, and legislative history. *See Hawkins*, 769 F.3d at 666; *Brown*, 953 F.3d at 623.

In the early 1990s, a circuit split developed on the question of what property should be included in a Chapter 7 estate upon conversion from Chapter 13. Some courts held that "upon conversion, all postpetition earnings and acquisitions became part of the new Chapter 7 estate, thus augmenting the property available for liquidation and distribution to creditors." *Harris*, 575 U.S. at 517 (citing *Calder v. Job* (*In re Calder*), 973 F.2d 862, 865-66 (10th Cir. 1992), and *In re Lybrook*, 951 F.2d 136, 137 (7th Cir. 1992)). However, the Third Circuit had taken the opposite view in

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[7] The court implies this approach would mean that debtors must bear the risk of depreciation as well. Op. at 11. But depreciation in a home's value would not change the amount of the debtor's homestead exemption, *see Law v. Siegel*, 571 U.S. 415, 424-25 (2014), and a trustee would probably abandon any asset which depreciated such that it had no value to the estate. *See* § 554(a).

Bobroff v. Continental Bank (*In re Bobroff*), 766 F.2d 797, 802-03 (3d Cir. 1985), and held that a tort claim which accrued during Chapter 13 proceedings was not part of a Chapter 7 estate upon conversion and belonged to the debtor.

Congress resolved this dispute in the Bankruptcy Reform Act of 1994, which added § 348(f) to the Bankruptcy Code. *See* Pub. L. No. 103-394, § 311, 108 Stat. 4106, 4138 (1994) (prior to 2005 amendment). The House Report on the Act made it clear Congress intended to adopt the Third Circuit's view:

> This amendment overrules the holding in cases such as *Matter of Lybrook*, 951 F.2d 136 (7th Cir. 1991) and adopts the reasoning of *In re Bobroff*, 766 F.2d 797 (3d Cir. 1985). However, it also gives the court discretion, in a case in which the debtor has abused the right to convert and converted in bad faith, to order that all property held at the time of conversion shall constitute property of the estate in the converted case.

H.R. REP. NO. 103-835, at 57 (1994), *reprinted in* 1994 U.S.C.C.A.N 3340, 3366. The report included a specific example:

> [Courts following the *Bobroff* approach] have noted that to hold otherwise would create a serious disincentive to chapter 13 filings. For example, a debtor who had $10,000 equity in a home at the beginning of the case, in a State with a $10,000 homestead exemption, would have to be counseled concerning the risk that

> after he or she paid off a $10,000 second mortgage in the chapter 13 case, creating $10,000 in equity, there would be a risk that the home could be lost if the case were converted to chapter 7 (which can occur involuntarily). If all of the debtor's property at the time of conversion is property of the chapter 7 estate, the trustee would sell the home, to realize the $10,000 in equity for the unsecured creditors and the debtor would lose the home.

Id. Clearly, Congress believed that home equity which accrued during Chapter 13 proceedings should not be included in the converted estate.

The example in the House Report discusses an increase in equity resulting from the paydown of a secured loan, but the court's decision today covers equity from any source and creates the same disincentive to Chapter 13 filings. When the Castlemans filed for bankruptcy, all of their home equity was exempt. Between that exemption and a secured mortgage, the home had no value to the estate. Had they filed under Chapter 7, they could have either resolved the case quickly or moved to force the trustee to abandon the property. *See* § 554(b); *Barrera I*, 620 B.R. at 655-54. Instead, the Castlemans committed themselves to a five-year Chapter 13 plan, paid creditors out of their postpetition income, and made payments on their mortgage. By the time they were forced to convert to Chapter 7, their home had appreciated in value, so the trustee sought to sell it. Allowing that sale leaves them "in a worse position than if the[ir] petition had been filed in Chapter 7 initially"—the exact situation Congress sought to prevent. *Brown*, 953 F.3d at 620.

The majority refuses to consider this history because it finds the text of the Bankruptcy Code unambiguously shows that appreciation belongs to the estate. Op. at 9. I respectfully disagree. But that assertion is all the more remarkable in light of the Tenth Circuit's decision in *Barrera III*, 22 F.4th at 1223, and the majority's recognition that courts are "heavily divided" on the proper meaning of § 348(f).[8] Op. at 5. Indeed, even counsel for the trustee seemed to believe that § 348(f) was ambiguous: when asked at oral argument, he admitted the statute is poorly drafted and agreed that "there is no way to reconcile" the text of § 348(f) with § 541(a).[9] To be sure, legislative history is often unhelpful as an aid to statutory construction. *See* ANTONIN SCALIA & BRYAN A. GARNER, READING LAW 376-78 (2012). But here, it is consistent with the text of the Bankruptcy Code, directly relevant to the case at hand, and unequivocally confirms that appreciation in the value of the Castlemans' home should not become part of the converted estate.

III

Because reasonable judicial minds disagree, there is—once again—a need for Congress to clarify the operation of § 348. Though I dissent from my colleagues' reading of the

[8] Certainly a division of authority, standing alone, does not establish ambiguity. But other courts have identified powerful arguments for a different reading of § 348(f), and the creation of a circuit split in particular is to be "avoid[ed] if at all possible." *Anderson*, 46 F.4th at 1008. We ought to employ the full panoply of statutory interpretation tools before departing from the Tenth Circuit's approach.

[9] Oral Argument at 24:06-24:52.

statute, it is far from unfounded. Whether Congress thinks postpetition, pre-conversion appreciation of an asset in the course of Chapter 13 proceedings should or should not become part of the converted Chapter 7 estate, it should amend § 348(f) to make the answer clear. At least one scholar has already proposed amendments to § 348(f) which would resolve the dispute. *See* Lawrence Ponoroff, *Allocation of Property Appreciation: A Statutory Approach to the Judicial Dialectic*, 13 WM. & MARY BUS. L. REV. 721, 756-57 (2022). States may also wish to amend their homestead exemptions. *See* § 522(b)(3)(A). For example, while the change came too late to help the Castlemans, Washington State responded to our decision in *Wilson* by allowing debtors to exempt "[a]ny appreciation in the value of the debtor's exempt interest in the property during the bankruptcy case." *See* Act of May 12, 2021, Ch. 290 § 5, 2021 Wash. Sess. Laws 2306-07 (codified at WASH. REV. CODE § 6.13.070(2) (2022)).

In the absence of legislative action, it remains our duty to read § 348(f) and say what the law is. I have no doubt that in holding that postpetition, pre-conversion appreciation becomes part of the converted bankruptcy estate, my colleagues in the majority have discharged that duty to the best of their abilities. But in striving to do the same, I find the text, structure, and history of the statute compel the opposite conclusion. Because I would hold that the appreciation belongs to the Castlemans, I respectfully dissent.

In re Adams

United States Bankruptcy Court for the Middle District of North Carolina, Durham Division

November 3, 2023, Decided

Case No. 21-80425, Chapter 13

Reporter

2023 Bankr. LEXIS 2744 *; __ B.R. __

In re: Johnny Ray Adams, Debtor.

Counsel: [*1] For Conserv Equipment Leasing, LLC, Creditor: Anna Bryce Hobson, Bradley Arant Boult Cummings, Charlotte, NC.

For Conserv Equipment Leasing, LLC, Creditor: W. Walt Pettit, Hutchens Law Firm LLP, Charlotte, NC.

For Johnny Ray Adams, Debtor: Travis Sasser, Sasser Law Firm, Cary, NC.

For James B. Angell, Trustee: James B. Angell, James B. Angell, Chapter 7 Trustee, Raleigh, NC.

For Anita Jo Kinlaw Troxler, Trustee: Anita Jo Kinlaw Troxler, Greensboro Chapter 13 Office, Greensboro, NC.

Judges: BENJAMIN A. KAHN, UNITED STATES BANKRUPTCY JUDGE.

Opinion by: BENJAMIN A. KAHN

Opinion

ORDER GRANTING MOTION TO MODIFY PLAN TO REQUIRE TURNOVER OF FUNDS AND TO INCREASE LIQUIDATION REQUIREMENT

This matter is before the Court on the Motion to Modify Plan to Require Turnover of Funds and to Increase the Liquidation Requirement (the "Motion"), ECF No. 149, filed by the chapter 13 trustee (the "Trustee"). For the reasons set forth herein, the Court will grant the Trustee's motion.

I. BACKGROUND

Debtor filed a petition under chapter 7 on November 17, 2021. ECF No. 1. On May 6, 2022, Debtor filed Amended Schedules A/B, listing the resale value of his residential real property located at 300 Plaza Dr, Garner, NC 27529 (the "Garner Property") [*2] at $260,000.00, and claiming $35,000.00 in value of his interest in the Garner Property exempt.[1] ECF No. 60. On May 12, 2022, the Court granted Debtor's motion to convert his case to

[1] Debtor states in his response to the Trustee's Motion that the Garner Property was valued at this amount as of the filing date. ECF No. 151, at 1. But Debtor did not file Schedule A/B concurrently with the petition. Debtor's original Schedule A/B, filed on December 16, 2021, listed the value of the Garner Property as "unknown." ECF No. 16. Debtor filed his request to convert his case from chapter 7 to chapter 13 after the chapter 7 trustee filed an application to employ a real estate broker to market the property on April 6, 2022, ECF No. 43, which the Court approved on April 11, 2022. ECF No. 46. Debtor's counsel filed a notice of appearance in the case on April 12, 2022, and a motion to convert to a case under chapter 13 on the same day. ECF Nos. 49 and 50, respectively. On May 5, 2022, Debtor filed an amended Schedule A/B which stated that the resale value of the Garner Property was $260,000.00 and, assuming a six percent cost of sale, that the current value was $244,400.00. ECF No. 60, at 1. The parties do not dispute that $260,000.00 is the appropriate valuation; however, Debtor argues that this valuation relates back to the petition date, November 17, 2021, and represents the value of the Garner Property as of the petition date. Debtor offered no evidence of this valuation; nevertheless, this valuation was used for purposes of determining the liquidation value at confirmation of the original plan.

chapter 13. ECF No. 64. The Court confirmed Debtor's chapter 13 plan (the "Plan") on December 14, 2022. ECF No. 121. The Plan included a liquidation requirement of $79,705.55 under *11 U.S.C. § 1325(a)(4)*,[2] ECF No. 98, at 2, and provided that property of the estate would remain property of the estate, notwithstanding *11 U.S.C. § 1327(b)*.[3] Id. at 5. On June 15, 2023, Debtor moved to sell the Garner Property for $289,000.00, ECF No. 142, and the Court approved the sale on June 30, 2023. ECF No. 144. The sale price represents an 11.2 percent increase from Debtor's valuation on the schedules of $260,000.00, which was used about six months earlier at plan confirmation as the value of the property for purposes of determining whether the Plan complied with the best interests of the creditors test under *§ 1325(a) (4)*. At the hearing on the sale motion, the Trustee requested that the net proceeds of the sale be turned over to the Trustee for payment to creditors to the extent that the proceeds exceeded Debtor's exemption. ECF No. 143, at 00:49-01:14. Because Debtor's [*3] interest in the Garner Property represented a substantial portion of the liquidation value and the Plan did not contemplate the sale of property, the Court permitted the sale but required that all net proceeds above the $35,000.00 exemption amount be held in a Sasser Law Firm Trust Account, subject to the Trustee filing a motion to modify the plan within thirty days of receiving the settlement statement from the sale closing. ECF No. 144, at 1.

The Trustee timely filed the motion to modify the plan on August 8, 2023, recommending that the Plan be modified pursuant to *11 U.S.C. § 1329*: (1) to require the turnover of a minimum of $60,022.38 of the net proceeds to the Trustee for distribution to unsecured creditors; (2) to increase the liquidation requirement to $109,403.00 to include the increased post-petition liquidation value realized from the sale of the Garner Property; and (3) to require the turnover of an additional $31,319.57 of the nonexempt net proceeds to the Trustee for distribution to unsecured creditors. ECF No. 149. Debtor contends that modification should be denied because the Plan is res judicata and modification is not permitted under *§ 1329(b) (1)*. ECF No. 151. Debtor further contends that he should [*4] have "the exclusive right to use and possess estate property in chapter 13 regardless of whether the property is 'subject to depletion,'" including all proceeds of the sale, and be allowed to continue to pay the liquidation value provided under the originally confirmed plan over the life of the plan. ECF No. 151, at 1-2. The Court held a hearing on the Motion on September 18, 2023. Jennifer Harris, attorney for the Trustee, and Travis Sasser, counsel for Debtor, appeared at the hearing. At the conclusion of the hearing, the Court took the matter under advisement.

II. DISCUSSION

The doctrine of res judicata prevents modification of a confirmed plan pursuant to *§ 1329(a)* unless the debtor experiences a

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[2] The parties do not dispute that Debtor's interest in the Garner Property on the petition date represented $63,744.36 of the liquidation value reflected in the original plan. The Trustee's Motion asserts that, as of the date of the Motion, a balance of $60,022.38 remained due to unsecured creditors to meet the Plan's liquidation requirement attributable to Debtor's interest in the Garner Property.

[3] North Carolina property exemptions fall into one of two categories: (1) those exemptions that "allow debtors to exempt items in full, regardless of value;" and (2) those exemptions that allow debtors "to exempt an interest in value up to a specified monetary amount in the particular item." *In re Gregory, 487 B.R. 444, 450-51 (Bankr. E.D.N.C. 2013)*. Under *N.C. Gen. Stat. 1C-1601(a) (1)*, Debtor exempted $35,000.00 in value of his interest in the Garner Property. Debtor's interest in the Garner Property remained property of the estate under the terms of the Plan, notwithstanding Debtor's exemption of a portion of its value.

"substantial and unanticipated post-confirmation change in his financial condition." *In re Murphy, 474 F.3d 143, 149 (4th Cir. 2007)*. The party seeking modification bears the burden of demonstrating that the post-confirmation change in the debtor's ability to pay was both substantial and unanticipated. See id.; *In re Arnold, 869 F.2d 240, 242 (4th Cir. 1989)* (citing *In re Fitak, 92 B.R. 243, 250 (Bankr. S.D. Ohio 1988)* (holding that, where the plan contemplated sale of the debtor's property 57 months into a plan and the property was sold as and when contemplated by the plan, a 20 percent appreciation in value during the first 57 months of the [*5] plan was reasonably foreseeable and did not justify overcoming res judicata)). Once res judicata is overcome, the plan can be modified if the purpose of the proposed modification is one that is identified in *§ 1329(a)*, and if the proposed modification complies with *§ 1329(b)(1)*. *Murphy, 474 F.3d at 150*.

A. Substantial Change

1. Ability to Pay

The Plan did not contemplate selling the Garner Property. Instead, the Plan contemplated that Debtor would retain the property in the estate and pay the equity that otherwise would have been available to creditors over the life of the Plan. Instead, Debtor moved to approve a sale of the property only five months after confirmation. See *In re Stinson, 302 B.R. 828, 830-31 (Bankr. D. Md. 2003)* (holding that an unanticipated sale of property, when the original plan contemplated retention of the property, constituted a substantial and unanticipated change permitting modification, and observing that "Debtors have initiated a *de facto* modification of the plan by voluntarily selling the Property and seeking to pay off their Plan obligation with the proceeds . . . [and] seek[ing] to bind the Trustee to the valuation of the Property at the time of confirmation, and thus obtain the benefit of the Property's appreciation"). As a result, funds realized from [*6] the unanticipated sale of the Garner Property substantially changed Debtor's ability to pay post-confirmation. "A substantial change in circumstances can be increased income . . . or receipt of a large sum of money." *In re Solis, 172 B.R. 530, 532 (Bankr. S.D.N.Y. 1994)* (citing *Arnold, 869 F.2d at 240* and *Fitak, 92 B.R. at 250*; and holding that a post-confirmation sale of the debtor's business that provided the debtor substantial proceeds warranted modification of the plan). In Murphy, the Fourth Circuit held that the "money received" by the debtor from a post-confirmation sale of property was "[u]nquestionably" substantial." *474 F.3d at 152*. There, the debtor, who owned $34,000 of nonexempt equity in real property, sold the real property post-confirmation for $80,000 more than its valuation on his schedules.[4] *Id. at 147*. The Fourth Circuit held that the debtor's financial condition had improved substantially and affirmed the bankruptcy court's order requiring turnover of $30,000[5] of sale proceeds to the trustee for distribution to unsecured creditors. *Id. at 152*.

Although the 11.2 percent appreciation in the value of Debtor's petition-date interest in[6] the

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[4] The debtor owned a condominium that he valued on his schedules at $155,000, subject to a lien of $121,000. *In re Murphy, 474 F.3d 143, 147 (4th Cir. 2007)*. It was sold post-confirmation for $235,000. Id.

[5] The trustee in Murphy only sought turnover of $30,000, rather than the full nonexempt equity, because that amount would be sufficient to pay all unsecured creditors in full. *474 F.3d at 147*.

[6] *Section 541(a)* lists those interests in property that become property of the estate. There is a difference between an interest in property and the property itself. See *In re Gifford, 634 B.R. 909, 917 (Bankr. M.D.N.C. 2021)* (rejecting trustee's

Garner Property is proportionately smaller than the 51.6 percent appreciation in Murphy, the amount of additional funds available for creditors in this [*7] case is almost identical to the amount that was required to pay creditors in full in Murphy. Further, while the proportionate appreciation of the Garner Property alone may not have resulted in a substantial and unanticipated change in this case—especially over a longer post-confirmation period—the sale resulted in a "substantial amount of readily available cash without any debt," and therefore created a substantial change in Debtor's financial condition. Id. Other courts similarly recognize that unanticipated receipt of a substantial amount of readily available cash can constitute a substantial change for purposes of *§ 1329*. In *Fitak*, for example, the Bankruptcy Court for the Southern District of Ohio found that a debtor's post-confirmation withdrawal of $16,000 from her scheduled retirement account constituted a substantial change in the debtor's financial condition. See *92 B.R. at 251*.[7] "When a debtor's financial fortunes improve, the creditors should share some of the wealth." *Arnold, 869 F.2d at 243*. As in *Arnold* and *Solis*, the sale of the Garner Property constituted a substantial change in Debtor's ability to pay post-confirmation.

2. Protection of Creditors' Entitlement to Receive [*8] Liquidation Value Under the Plan

The conversion of estate property into cash constituted a substantial change from the perspective of the creditors. The sale of the property itself materially altered the creditors' protections embodied within the Plan. Debtor's interest in the Garner Property remained property of the estate after plan confirmation, and Debtor's nonexempt equity in the property constituted a substantial portion of the liquidation value required to be paid to creditors under the Plan. In these circumstances, the estate's interest in the real property provided protection to creditors in the event of a reconversion to chapter 7. But if an unanticipated sale of estate property is permitted and the case is later reconverted, the value promised to creditors is at risk if Debtor is granted "the exclusive right to use" the sale proceeds as he requests in his response to the Trustee's Motion. See ECF No. 151 at 1-2. Even if Debtor does not expend any of the proceeds, proceeds from a sale of the property may not constitute property of the chapter 7 estate if the case is reconverted to chapter 7. See *11 U.S.C. § 348(f) (1) (A)* (property of the estate in a case converted from chapter 13 to chapter 7 consists [*9] of property of the estate as of the filing of the petition that remains in the possession of the debtor on the date of conversion); see also *In re Marsh, 647 B.R. 725, 736-37 (Bankr. W.D. Mo. 2023)* (recognizing that proceeds of property of the

argument that conflated debtor's interest in the property with the property itself).

[7] The court in *Fitak* determined that the appreciation in the debtor's real property was insufficiently significant to overcome res judicata where the property was sold as contemplated under the original plan and the appreciation in value was insufficient to be deemed unexpected 56 months after confirmation. The court nevertheless held that the debtor's receipt of cash from her retirement funds constituted a substantial and unanticipated change warranting modification. *92 B.R. at 250-51*. The conversion of retirement funds to cash did not change the debtor's balance sheet, but the court nevertheless held that the receipt of readily available funds warranted modification. Id. As a result, the court confirmed a modified plan that included payment to allowed unsecured claims of the value of the withdrawn retirement funds but not to include payment of the appreciation value of the property. This court respectfully disagrees with the court in *Fitak* to the extent that it held that these issues could be parsed once res judicata is overcome. Instead, once the court determines that modification is appropriate and res judicata has been overcome, the court must ensure that the modified plan meets the requirements for confirmation under *11 U.S.C. § 1325(a)*, including *1325(a)(4)*. See *11 U.S.C. § 1329(b)*; see also Section III, infra.

estate is a different category of property than the property itself, or there would be no need for § 541(a) (6)); In re Barrera, 22 F.4th 1217, 1223 (10th Cir. 2022) (holding in a post-confirmation conversion from chapter 13 to chapter 7 that proceeds from the post-petition, pre-conversion sale of property are not identical to the underlying property the debtor possessed on the chapter 13 petition date and, absent bad faith, do not constitute property of the chapter 7 estate under § 348(f)).

For this reason, when nonexempt proceeds from an unanticipated post-confirmation sale of property are not committed to funding the plan, "conversion or dismissal after the sale could leave creditors with less than they were entitled to in the Chapter 13 case." Keith M. Lundin, Lundin on Chapter 13, § 127.6, at ¶ 3 (2023). As attorney for the Trustee argues, there would be nothing to stop a debtor after a post-confirmation sale of estate property from spending the proceeds and allowing the case to be dismissed or converted. ECF No. 155, at 20:29-21:55; see also Lundin, 120.3, at ¶ 45 ("[A] subsequent conversion [*10] produces a Chapter 7 estate that does not include the equity dissipated by the debtor."). Therefore, under the circumstances of this case, the sale itself was a substantial and material change in the creditors' protection as contemplated in the Plan.

B. **Unanticipated Change**

The change also was unanticipated as required for modification under § 1329. The Fourth Circuit has adopted the test applied in Fitak to determine whether a change in a debtor's financial condition was unanticipated. Arnold, 869 F.2d at 243. The Fitak test asks whether a debtor's "altered financial circumstances could have been *reasonably anticipated* at the time of confirmation by the parties seeking modification." 92 B.R. at 250 (emphasis in original). Debtor's Plan contains a liquidation requirement of $79,705.55. ECF No. 121. The vast majority of this liquidation value is attributable to nonexempt equity of $63,744.36 in the Garner Property. ECF No. 149, at 1. The Plan gave no indication that Debtor intended to sell the Garner Property. "[W]here a Chapter 13 plan provides for unsecured creditors to be paid from income earned from a business and the confirmed plan gives no indication of a debtor's intention to sell the business, a post-confirmation sale could be an [*11] unanticipated change warranting plan modification." In re Suratt, No. 95-6183-HO, 1996 U.S. Dist. LEXIS 22610, 1996 WL 914095, at *2 (D. Or. Jan. 10, 1996); see also Arnold, 869 F.2d at 243 (if income increase was anticipated, debtor's expectations should have been disclosed to the bankruptcy court before the plan was confirmed). Similarly, where the liquidation value of a plan relies on property that will remain property of the estate, the liquidation of that property during the case can be an unanticipated change. See Lundin, § 127.6, at ¶ 1 ("Modification under § 1329 may be required if the debtor sells property after confirmation.").

The court in Surratt rejected the debtor's argument that the plan must specifically provide for payment to creditors of any proceeds in the event of a sale of the property:

> The logical extension of the debtor's argument here is that there must be a provision in all Chapter 13 plans requiring post-confirmation sale proceeds from property originally part of the estate to be paid to creditors, in order to preclude the debtor from receiving those funds. There is no such requirement in the Bankruptcy Code, nor has any court imposed such a requirement. 11 U.S.C. § 1329(a) is intended, in part, to provide the protection the debtor claims is missing.

1996 U.S. Dist. LEXIS 22610, 1996 WL

914095, at *3. Thus, at the time of confirmation, the Trustee could not [*12] have reasonably anticipated the substantial change in Debtor's ability to pay resulting from the sale of the Garner Property.

Because the change in Debtor's post-confirmation ability to pay following the sale of the Garner Property was both substantial and unanticipated, res judicata is overcome, and the Court must consider whether the purpose of the modification is consistent with § 1329(a) and whether the modification satisfies § 1329(b) (1).

C. Purpose of Modification

The purpose of the proposed modification is consistent with 1329(a). Debtor argues that the proposed modification "exceeds the bounds of 11 U.S.C. § 1329 (a) (1) which only allows for payments to be increased to a class of claims," and that Trustee's proposed modification would transform a plan that provides for payments "to be cash flowed out of ongoing disposable income . . . into a liquidating plan." ECF No. 151, at 2. However, this argument is inconsistent with the text of the Bankruptcy Code and relevant caselaw.

Section 1329(a) (1) provides that the trustee may request modification of the plan after confirmation to "increase or reduce the amount of payments on claims of a particular class provided for by the plan." Section 1329(a)(2) provides that the plan can be modified to "extend or reduce the time [*13] for such payments." Debtor's Plan provides for payment over time. The Trustee seeks modification to (1) require immediate turnover of the unpaid balance of the liquidation value attributable to the Garner Property established by the confirmed Plan, (2) increase the liquidation requirement to include the increased post-petition liquidation value realized from the sale of the Garner Property, and (3) require the immediate turnover of the additional nonexempt net proceeds. ECF No. 149. These modifications have the effect of increasing the amount of the distribution to unsecured creditors and to reduce the time for the payment by Debtor. A chapter 13 plan may be modified consistent with § 1329(a) to require turnover of funds that would create a "windfall" to the debtor. See *Murphy, 474 F.3d at 152*; infra Section III (and cases cited therein). Thus, the purpose of the modification is permitted under § 1329(a).

III. COMPLIANCE WITH § 1329(b)(1).

Section 1329(b) (1) sets out the confirmation requirements applicable to modification of plans. Of the four sections made applicable by § 1329(b) (1), Debtor asserts that the proposed modification should be denied pursuant to § 1325(a) (1), § 1325(a)(3), and § 1325(a)(4). ECF No. 151, at 1-2.

A. Section 1325(a)(1)

Section 1325(a) (1) provides that a court shall confirm a plan if the plan "complies with the [*14] provisions of this chapter and with the other applicable provisions of this title." Debtor contends that the proposed plan modification violates §§ 542, 1303, 1306(b), and 1327(a). ECF No. 151, at 1. None of these provisions are explicitly made applicable to modification of confirmed plans under § 1329(b) (1). Debtor asserts that they apply under the general reference in § 1325(a) (1), which § 1329(b) (1) incorporates.

Debtor does not cite authority suggesting that a debtor can use proceeds from a post-confirmation sale of estate property at the exclusion of the trustee and without court approval, and neither § 1303, nor *§ 363(b)* permit a debtor to do so. *Section 1303* provides that "[s]ubject to any limitations on a trustee under this chapter, the debtor shall have, exclusive of the trustee, the rights and powers of a trustee under *sections 363(b)*, *363(d)*, *363(e)*, *363(f)*, and *363(l)*." But *§ 363(b)*, as incorporated by *§ 1303*, provides that the debtor may use, sell, or lease property of the estate "other than in the ordinary course of business" only "after notice and a hearing." As observed by Collier, although the debtor has the right to use or sell property of the estate exclusive of the trustee,

> [i]t is of equal importance, however, that the chapter 13 debtor not be allowed to dispose of property of the estate other than [*15] in the ordinary course of business during the pendency of the plan, absent consent or at least the acquiescence of the chapter 13 trustee and creditors.

8 Collier on Bankruptcy ¶ 1303.02 (16th 2023). Implicit in this observation that the creditors and trustee are entitled to be heard on the disposition of the estate's interest in property is that the estate's interest must be sufficiently protected. Here, there cannot be any dispute that Debtor's interest in the Garner Property remained property of the estate. Debtor's nonexempt equity in that interest represents a significant portion of the liquidation requirement in the Plan, and the additional nonexempt net proceeds represent a significant portion of the proposed increased liquidation requirement.

Because Debtor's interest in the Garner Property remained property of the estate post-confirmation, the interest of the estate in the property must be protected in the event that the case is reconverted to chapter 7. See supra Section II.A.2. Therefore, Debtor cannot use the proceeds from the sale of the Garner Property without court approval, and turnover of the proceeds to the Trustee does not violate *§ 1325(a) (1)* or otherwise frustrate the "purposes and spirit of the Bankruptcy [*16] Code." ECF No. 151, at 1. On the contrary, turnover protects the expectations of the creditors in this case both before conversion and under the terms of the confirmed plan.

B. ***Section 1325(a)(3)***

The proposed modification satisfies *§ 1325(a) (3)*. *Section 1325(a) (3)* provides that a court shall confirm a plan if "the plan has been proposed in good faith and not by any means forbidden by law." The Fourth Circuit has held that this good faith test is satisfied when modification would prevent a debtor from receiving a "substantial windfall." *Murphy, 474 F.3d at 153*; see also *Arnold, 869 F.2d at 242* ("Certainly Congress did not intend for debtors who experience substantially improved financial conditions after confirmation to avoid paying more to their creditors."). Other courts have similarly found good faith when the proposed modification reflects a "'significant increase in income and a commensurately increased payout to unsecured creditors.'" *In re Wetzel, 381 B.R. 247, 254 (Bankr. E.D. Wis. 2008)* (quoting *In re Brown, 332 B.R. 562, 566 (Bankr. N.D. Ill. 2005)*). The Murphy Court found that the trustee's modification was made in good faith to prevent the debtor, who realized an $80,000 appreciation in property value by selling his house less than a year after plan confirmation, from receiving a substantial windfall. *474 F.3d at 153*. As in *Murphy*, the Trustee here recognized that Debtor's liquidation of [*17] the substantial appreciation in property value significantly altered Debtor's ability to pay. Furthermore, in this case, permitting Debtor to expend all the proceeds to which the creditors are entitled transfers the entire risk of nonpayment to the creditors, substantially frustrates the creditors' legitimate expectations when this case was commenced and subsequently converted to avoid the chapter 7 trustee's liquidation of the property, and would be inequitable. See supra note 1. Therefore, the Trustee's proposal to increase the liquidation requirement to include the post-petition liquidation value realized from the sale of the Garner Property and to require turnover of the nonexempt proceeds was made in good faith to prevent Debtor from receiving a substantial and unanticipated windfall not contemplated in the original plan and impermissibly shifting the risk of nonpayment entirely to creditors.

C. *Section 1325(a)(4)*

Section 1325(a) (4) provides that a court shall confirm a plan if "the value, as of the effective date of the plan, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated [*18] under chapter 7 of this title on such date." This test, generally known as the "best interests of the creditors" or "liquidation value" test, is applied using the values as of the effective date of the plan as modified. See, e.g., *In re Barbosa, 236 B.R. 540, 552-53 (Bankr. D. Mass. 1999)*; *In re Walker, 153 B.R. 565, 568-69 (Bankr. D. Or. 1993)*; *In re Morgan, 299 B.R. 118 (Bankr. D. Md. 2003)*; *In re Nott, 269 B.R. 250, 255 (Bankr. M.D. Fla. 2000)*; *In re Auernheimer, 437 B.R. 405, 409 (Bankr. D. Kan. 2010)*; *In re Taylor, 631 B.R. 346, 354 (Bankr. D. Kan. 2021)* (analyzing cases and finding that the liquidation test is applied as of the date of confirmation of the modified plan, but that property acquired post-petition is not included in the best interests calculation); see also Lundin, § 126.2, at 91 11 ("[A] majority of reported decisions fix the effective date for best-interests-of-creditors test purposes at modification as the effective date of the plan as modified.").

Reading the phrase "effective date of the plan" to constitute the petition date ignores the plain language of the statute. Although Judge Lundin argues for a petition date valuation to "avoid vagaries of the court's scheduling of confirmation," among other potential problems associated with a roving valuation determination, he concedes that "Congress demonstrated its ability to identify the date of the petition or entry of the order for relief as the magic date for other consequences." Lundin, § 90.1, at 91 5.[8] Using the date of confirmation of the original [*19] plan for purposes of determining liquidation value at modification similarly is at odds with the logic of *§ 1329(a)*, "which permits modification after confirmation to reflect changes after the effective date of the original plan." Id. § 126.2, at 91 8. Regardless, using an earlier date—whether petition date or prior confirmation date—is irreconcilable with the holding in Murphy, which required the debtor to pay the appreciated value of the debtor's petition-date property interest to the creditors.

Thus, the effective date of the plan for purposes of this test is the date of the plan as modified. This conclusion, however, does not necessarily determine which property interests are considered for purposes of determining the liquidation value on the effective date of the modified plan, or, specifically to this case, which portion of the sale proceeds from the Garner Property should be included in that calculation. This Court agrees with the court in *Taylor* that the property interests to be included in the valuation as of the effective

[8] Not only does Congress know how to say either "the petition date" or "the order for relief" when it means to refer to that date, but the "effective date of the plan" also does not describe the petition date under any other section of the Code. See *Hall v. U.S., 566 U.S. 506, 519, 132 S.Ct. 1882, 1891, 182 L. Ed. 2d 840 (2012)* ("[I]dentical words and phrases within the same statute should normally be given the same meaning.'") (quoting *Powerex Corp. v. Reliant En. Servs., Inc., 551 U.S. 224, 232, 127 S.Ct. 2411, 2417, 168 L. Ed. 2d 112 (2007)*).

date of the modified plan include only those interests under *§ 541*, and excludes those interests that have come into the estate post-petition under *1306*. *631 B.R. at 353*. Courts have struggled to [*20] delineate this concept. In determining that the proceeds from the settlement of a post-petition personal injury claim should not be included in the calculation, the court in *Taylor* cites Judge Lundin and Collier for the proposition that post-petition property is excluded from this calculation. *Id. at 354*.

Finding an ambiguity in the operative statutes, the court in In re Barrera looked to legislative history. *620 B.R. 645, 652-53 (Bankr. D. Colo. 2020)* (citing H.R. Rep. No. 103-835, at 57 (1994), as reprinted in 1994 U.S.C.A.N. 3340, 3366, for the proposition that a debtor should not be penalized for paying down equity during the chapter 13 case because to do so would "create a serious disincentive to chapter 13 filings"), aff'd *22 F.4th 1217 (10th Cir. 2022)*. The court recognized that "one could . . . attempt to distinguish between increased equity that arises from the debtor's repayment of secured debt from an increase that results from a change in market conditions," but declined to make that distinction, finding no language in *§ 348(f)(1)(A)* or elsewhere in the Bankruptcy Code to support such a distinction. Id.

This Court respectfully disagrees that any additional statutory language is necessary. The distinction is in the property interests at issue. Appreciation is attributable to [*21] the property interest Debtor held on the petition date, while paydown of equity is attributable to Debtor's interest in his post-petition income that would not have been property of the estate in a hypothetical chapter 7. See *Goins, 539 B.R. at 511, 515* (holding that the trustee was entitled to value attributable to the appreciation of the real estate because it "was *always* property of the estate under *Section 541(a)*," but nevertheless allowing the debtor to retain proceeds reflecting the reduction of debt from post-petition income). This distinction is fully consistent with the policy that a debtor should be no worse off by choosing chapter 13 than he would have been by filing a chapter 7. Had the debtor in this case remained in chapter 7, he would have been entitled to the value of his exemption in the Garner Property upon its sale, and he would have been entitled to retain his post-petition income. *11 U.S.C. § 541(a) (6)*.[9] The creditors, in turn, had the expectation to receive the value of the Garner Property, less Debtor's exemption, but did not have an expectation that they would be entitled to further reduction of any liens by payments made by Debtor toward the debt. Both these expectations are fulfilled by allocating proceeds between these [*22] interests in the Garner Property. Further, this distinction is required in this circuit under Murphy, which held that the creditors were entitled to the appreciated value of the estate property once it is sold during the chapter 13 case.

For these reasons, the proposed modification satisfies *§ 1325(a) (4)*. Because the effective date of the plan is the date of modification, the liquidation value requirement includes the nonexempt net value realized from the post-confirmation sale of the Garner Property, less any principal reduction attributable to Debtor's post-petition property. Accordingly, the best interests of the creditors test requires Debtor to turn over all nonexempt net proceeds from the sale of the Garner Property to the Trustee for distribution to the unsecured creditors, less any amount of proceeds attributable to principal reduction resulting from Debtor's post-petition payments and any portion of the

[9] This distinction also would apply to the hypothetical posed by the court in *Barrera* in which there is an increase in value attributable to improvements to a property made by a debtor using post-petition income. *620 B.R. at 653-54*.

liquidation value previously paid to creditors in this case (the result being the "Estate Proceeds"). Neither Debtor, nor the Trustee adduced any evidence of the amount of this principal reduction, if any. The Trustee's motion indicates that $60,022.28 of the original $63,744.36 attributable [*23] to the liquidation value of the Garner Property remains unpaid, and she requests an additional $31,319.57 in proceeds be turned over for distribution to unsecured creditors pursuant to the increased liquidation requirement of $109,403.00 under the proposed modificiation. Accordingly, the Trustee has requested turnover of a total of $91,341.85. The parties do not dispute that the remaining net proceeds held by counsel for Debtor (after payment of Debtor's exemption at closing) is $95,063.93. Therefore, it appears that Trustee has not sought turnover of $3,722.08 of the remaining net proceeds held by Debtor's counsel and that this amount may fully account for previous payments toward liquidation value and reduction in principal. Nevertheless, the record is unclear. Therefore, the Court will permit the parties fourteen (14) days to submit a stipulation of the appropriate amounts of remaining unpaid liquidation value and any principal reduction that occurred prior to the sale as a result of payments made by Debtor after the date of the filing of the chapter 7 petition.

IV. CONCLUSION

IT IS THEREFORE ORDERED, ADJUDGED, and DECREED as follows:

1. The Trustee's Motion to Modify Plan to Require [*24] Turnover of Funds and to Increase the Liquidation Requirement is granted as provided herein;

2. The plan as modified consistent with the Trustee's Motion to increase the liquidation value of the plan to $109,403.00 is approved;

3. Contemporaneous with filing the stipulation in paragraph 4 below, Counsel for Debtor shall turn over all Estate Proceeds to the Trustee for distribution consistent with the terms of the plan as modified. If the parties do not file a stipulation as contemplated by paragraph 4, Counsel for Debtor shall turnover the undisputed portion of the Estate Proceeds based on calculations as directed herein within fourteen (14) days of the date of this order, and retain any disputed portion of the Estate Proceeds pending further order of the Court. Nothing herein shall be construed as permitting counsel to retain any portion of Estate Proceeds on any basis other than a calculation of principal reduction or previous payment of liquidation value, including without limitation an appeal or contemplated appeal of this order, absent a stay of this order.

4. The parties shall have fourteen (14) days from the entry of this order to file a stipulation of the amount of Estate Proceeds. [*25] If a stipulation is timely filed, the amount in the stipulation will be deemed incorporated herein without further order, and this order shall be deemed a final order as of the date of the filing of the stipulation. If the parties do not file a timely stipulation as contemplated in this order, the Court will conduct a hearing on November 20, 2023, at 2:00 p.m. in the United States Bankruptcy Court, Courtroom 1, 101 S. Edgeworth St., Greensboro, North Carolina 27408 to determine the amount of Estate Proceeds consistent with this order.

SO ORDERED.

SIGNED this 3rd day of November, 2023.

/s/ Benjamin A. Kahn

BENJAMIN A. KAHN

UNITED STATES BANKRUPTCY JUDGE

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ABI EXCLUSIVE

SEPTEMBER 13, 2023

Rising Home Values and Chapter 13: A Deepening Split

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> When, post-confirmation, a chapter 13 debtor sells his or her home, who gets the benefit of the appreciation: the debtor, or his or her creditors? Judge Randon in Michigan adopted the so-called "estate replenishment approach" and held that sale proceeds derived from post-confirmation appreciation of a home belong to the debtor.

Bill Rochelle is on vacation. Please enjoy this piece written by Guest Writer Paul R. Hage, who co-chairs Taft, Stettinius & Hollister, LLP's Bankruptcy and

Restructuring practice group in Southfield, Mich., and is an executive editor of the ABI Journal.

Hon. Mark Randon of the U.S. Bankruptcy Court for the Eastern District of Michigan recently weighed in on an issue that has divided bankruptcy courts over the past few years. Debtors who opt for chapter 13 often do so to save their homes. Because of the appreciation in home values in recent years, debtors frequently find themselves with equity in their homes that was not contemplated at the time of plan confirmation. When, post-confirmation, a chapter 13 debtor sells his or her home, who gets the benefit of the appreciation: the debtor, or his or her creditors? In *In re Elassal,* Judge Randon adopted the so-called "estate replenishment approach" and held that sale proceeds derived from post-confirmation appreciation of a home belong to the debtor.

An Unexpected Asset

In 2021, the debtor confirmed a chapter 13 plan, committing three years of disposable income to keep her assets, including a $250,000 home. The home was encumbered by $228,000 in liens. Although unsecured creditors would have received nothing in a chapter 7 liquidation (the debtor could have exempted the equity in the home), the debtor's plan contemplated payment of a minimum of $1,227.16 toward $93,805.83 in general unsecured claims.

Two years later, the debtor sold her home for $435,000. The sale netted $177,695.13 in proceeds after payment of liens. The debtor filed a motion seeking authorization to use the sale proceeds to buy a new home, while continuing to make her promised plan payments to creditors. The chapter 13 trustee objected, arguing that the debtor could only keep the net proceeds from the sale after she had paid her unsecured creditors in full.

A Deep Split in the Case Law

In all chapters of the Bankruptcy Code, Section 541(a) creates a bankruptcy estate that broadly sweeps in "all legal or equitable interests of the debtor in property as of the commencement of the case" and all "[p]roceeds, product, offspring, rents, or profits of or from property of the estate…." Section 1306(a)(1) expands on the property-of-the-estate concept by pulling in, among other things, all property "that the debtor acquires after the commencement of the case but before the case is closed, dismissed, or converted."

Based on the foregoing, one might assume that post-petition appreciation in a chapter 13 debtor's home becomes property of the estate. However, Section 1327(b) generally provides that the confirmation of a plan vests all of the property of the estate in the debtor." Moreover, Section 1327(c) provides that the vested property is generally "free and clear of any claim or interest of any creditor provided for by the plan." The argument is frequently raised that because, upon confirmation of the plan, the home is vested in the debtor, then the proceeds from the sale of such home do not become property of the estate.

In an effort to reconcile the apparent contrasting language in Sections 1306 and 1327, courts have come up with no fewer than five different approaches to the question of how the post-confirmation vesting of property in the debtor affects the entitlement to the appreciation from a post-confirmation sale of a home. Some approaches result in the appreciation becoming property of the estate and being distributed to creditors. Others allow the debtor to retain the appreciation. There is a deep split in the caselaw.

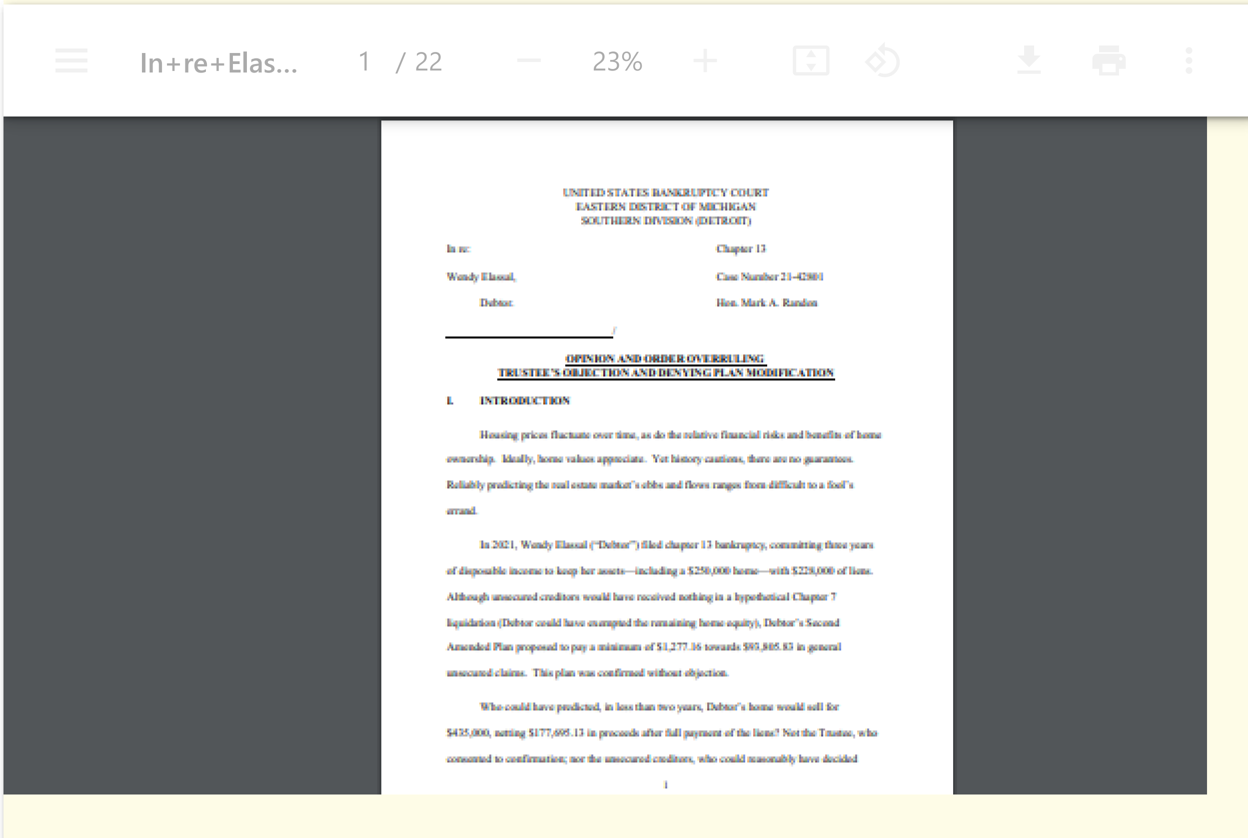
The Estate-Replenishment Approach Dictates that the Debtor Retains the Proceeds

Judge Randon adopted the so-called "estate-replenishment approach" to harmonize Sections 1306 and 1327, which, unlike other approaches in the caselaw, avoided rendering any statutory provision superfluous. Under that approach, property that vests in the debtor cannot re-enter the estate, but property later acquired by the debtor becomes property of the estate, which continues to exist throughout the duration of the plan.

Applying the "estate replenishment approach," the court held that the sale proceeds did not replenish the estate because they were not newly acquired property. The proceeds, the court stated, "cannot be untethered" from the home, which the debtor was permitted to keep under the plan. This result, the court reasoned, was consistent with the policies of chapter 13 and the bargain struck between the debtor and her creditors. The court further reasoned that, because chapter 13 debtors assume the risk of depreciation in their revested assets, “It stands to reason they should also enjoy the benefit of any post-confirmation appreciation of revested property when sold.”

Opinion Link

PREVIEW



UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION (DETROIT)

In re:	Chapter 13
Wendy Elassal,	Case Number 21-42801
Debtor.	Hon. Mark A. Randon

_______________________________/

OPINION AND ORDER OVERRULING TRUSTEE'S OBJECTION AND DENYING PLAN MODIFICATION

I. INTRODUCTION

Housing prices fluctuate over time, as do the relative financial risks and benefits of home ownership. Ideally, home values appreciate. Yet history cautions, there are no guarantees. Reliably predicting the real estate market's ebbs and flows ranges from difficult to a fool's errand.

In 2021, Wendy Elassal (“Debtor”) filed chapter 13 bankruptcy, committing three years of disposable income to keep her assets—including a $250,000 home—with $228,000 of liens. Although unsecured creditors would have received nothing in a hypothetical Chapter 7 liquidation (Debtor could have exempted the remaining home equity), Debtor's Second Amended Plan proposed to pay a minimum of $1,277.16 towards $93,805.83 in general unsecured claims. This plan was confirmed without objection.

Who could have predicted, in less than two years, Debtor's home would sell for $435,000, netting $177,695.13 in proceeds after full payment of the liens? Not the Trustee, who consented to confirmation; nor the unsecured creditors, who could reasonably have decided

1

https://abi-opinions.s3.amazonaws.com/In+re+Elassal.pdf-128861355-v1.pdf

Case Details

Case Citation	In re Elassal, 2023 WL 5537061 (Bankr. E.D. Mich. Aug. 28, 2023).

Case Name	In re Elassal
Case Type	Consumer
Court	6th Circuit Michigan Michigan Eastern District
Bankruptcy Tags	Creditors' Committee Consumer Bankruptcy Mortgage Finance and Banking

ORDERED in the Southern District of Florida on December 13, 2023.

Robert A. Mark, Judge
United States Bankruptcy Court

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF FLORIDA
MIAMI DIVISION

In re: CASE NO. 21-11633-RAM
CHAPTER 13

RAQUEL V. MONTENEGRO,

Debtor.
______________________________/

ORDER GRANTING MOTION FOR
EARLY PAYOFF AND MOTION TO MODIFY

The debtor in this chapter 13 case wants to refinance the debt on non-exempt real property for significantly more than the secured debt determined by a valuation order entered early in the case. The question is, can the debtor use the new loan proceeds to pay the secured and unsecured plan obligations early and keep any remaining proceeds? Or must the proceeds in excess of the stripped-down secured debt be used to increase the distribution to unsecured creditors? These are the questions presented in a motion to modify the confirmed chapter 13 plan and motion for early payoff.

Factual and Procedural Background

Raquel V. Montenegro (the "Debtor") filed a chapter 13 petition on December 19, 2021. The Debtor owns non-exempt real property located at 961 NE 96th Street, Miami Shores, Florida 33138 (the "Property"). On January 6, 2022, the Debtor filed Debtor's Motion to Value Collateral of U.S. Bank National Association as Trustee for Lehman XS Trust Series 2006-GP4 and PHH Mortgage Corp., and Determine Secured Status of Lien on Real Property [DE# 97] (the "Motion to Value"), valuing the Property at $500,000 and proposing to reduce to that amount the secured claim of U.S. Bank National Association as Trustee for Lehman XS Trust Series 2006-GP4 and PHH Mortgage Corp. ("PHH Mortgage"). The Court scheduled an evidentiary hearing, but the Debtor and PHH Mortgage settled the valuation dispute and agreed on a valuation of $560,000. This value was reflected in the Court's November 7, 2022 Order Granting the Debtor's Motion to Value and Determine Secured Status of Lien on Real Property Held by U.S. Bank National Association as Trustee for Lehman XS Trust, Series 2006-GP4 and PHH Mortgage Corp. [DE# 177] (the "Valuation Order"). The Valuation Order resulted in a secured debt of $560,000 and an unsecured debt of $560,000.[1]

The Debtor's fourteenth amended chapter 13 plan [DE# 175] (the "Plan") was confirmed on December 27, 2022 [DE# 182]. Using the amounts agreed to in the Valuation Order, the Plan pays the stripped-down PHH Mortgage debt of $560,000 at 5.25% interest. Unsecured creditors, including PHH Mortgage's unsecured debt of $560,000, are receiving

[1] PHH Mortgage filed Claim No. 10-2 in the amount of $1,129,917.66. Based on the valuation of $560,000, the remaining unsecured debt would have been $569,917.66. Apparently, PHH Mortgage agreed to round its unsecured claim down to $560,000.

their pro rata share of $54.20 per month for months 21 through 59 and $72,844.35 in month 60, for a total distribution of just under $75,000.

On March 9, 2023, the Debtor filed a Motion to Payoff Chapter 13 plan [DE# 189] (the "Motion for Early Payoff"), seeking relief to pay off the balance due under the Plan by refinancing the Property for $600,000. The next day, the Debtor filed a Motion to Modify Chapter 13 Plan [DE# 194] (the "Motion to Modify") and filed a First Modified Plan [DE# 193] (the "Modified Plan"). The Modified Plan proposes a lump-sum payment in month 25 of $588,050.63 to fully pay the amounts remaining due under the confirmed plan to tax creditors, to PHH Mortgage on its stripped-down secured debt ($437,121.59), and to unsecured creditors ($74,958.15).

Nancy K. Neidich, chapter 13 trustee (the "Trustee") opposes both motions. She cites to 11 U.S.C. § 1329(b) which states that § 1325(a) applies to modified plans. Section 1325(a)(4) requires a chapter 13 debtor to provide value to the unsecured creditors on the "effective date" of the plan that is not less than the amount the unsecured creditors would receive in a chapter 7 liquidation on that date. The Trustee argues that the "effective date" for purposes of § 1325(a)(4) is the effective date of the Modified Plan, so the value that unsecured creditors would receive on the effective date must be based on the appreciated value of the Property. *See* Trustee's Amended Response to Motion to Modify [DE# 210].

The Debtor says okay, I'll just withdraw the Motion to Modify. I'm not really modifying the confirmed Plan; I'm just paying it off early. So, we don't need to re-value the non-exempt property and do a new best interest calculation under § 1325. *See* Debtor's Response to Trustee's Amended Response to Motion to Modify [DE# 212]. Back comes the Trustee in her reply [DE# 213] saying, sorry, you can't do an early payoff without a modification because § 1329(a)(2) says you need a modified plan to "extend or reduce the time" for payments under the confirmed plan.

After considering the record, and upon review of applicable law, the Court is granting both the Motion for Early Payoff and the Motion to Modify. The Court agrees with the Trustee that (1) the Debtor must modify the Plan to do an early payoff; and (2) the effective date for the best interest test is the modification date. But the Modified Plan still meets the liquidation test for two reasons. First, the Court agrees with courts that hold a debtor is entitled to the appreciated value upon conversion. Second, even if a chapter 7 trustee could sell the Property, all the proceeds would be paid to PHH Mortgage. That is so because, under § 348(f)(1)(B) and (C), the Valuation Order stripping down PHH Mortgage's secured debt would not apply in the chapter 7 case. Therefore, the appreciated value would not be available to unsecured creditors and would not increase the liquidation value in applying the best interest test in § 1325(a)(4). In sum, the Modified Plan is confirmable.

Discussion

A. Early Payoff is Permitted Under Modified Plans

In bench rulings and in unpublished orders, this Court has allowed debtors to pay off plans early. The Court has rejected the Trustee's argument that the Bankruptcy Code and Eleventh Circuit authority require a debtor to stay in chapter 13 for the applicable three-year or five-year commitment period. Knowing my view, the Trustee has not pressed this argument here, but the Court will nonetheless address the issue.

There is a split of opinion in the Bankruptcy Court for the Southern District of Florida and in the Eleventh Circuit. My colleague, Judge Isicoff, held that chapter 13 debtors are prohibited from paying off their confirmed plans early. *In re Rhymaun*, 2011 WL 9378787 (Bankr. S.D. Fla. Aug. 8, 2011). The statutory issue is whether § 1325(b), which requires above-median debtors to commit to a five-year plan, applies to modified plans. *Rhymaun* concedes that § 1329(b), which specifies the sections that apply to modifications, says that § 1325(a) applies but does not say that 1325(b) applies. But *Rhymaun* agrees with courts that find that § 1325(b) applies by implication because § 1325(a) incorporates the restrictions in § 1325(b). *Rhymaun, 2011 WL 9378787* at *2. *Rhymaun* also relies on the Eleventh Circuit's decision in *Whaley v. Tennyson* (*In re Tennyson*), 611 F.3d 873 (11th Cir. 2010). *Tennyson* held that a debtor is obligated to remain in chapter 13 for the "applicable commitment period" which is 3 years for below-median debtors and 5 years for above-median debtors. *Tennyson*, 611 F.3d at 880. *Rhymaun* held that *Tennyson* was applicable to modifications, not just at confirmation. *Rhymaun*, 2011 WL 9378787 at *3.

Rhymaun cites opinions from two bankruptcy courts in the Eleventh Circuit reaching the same result: *In re Heideker*, 455 B.R. 263 (Bankr. M.D. Fla. 2011) and *In re Buck*, 443 B.R. 463 (Bankr. N.D. Ga. 2010). After *Rhymaun* was decided, another bankruptcy court in the Eleventh Circuit applied the same analysis and denied early payoff. *In re Carreiro*, 2013 WL 2353784 (Bankr. M.D. Fla. May 30, 2013). However, as noted in *Rhymaun,* other courts have held that § 1325(b) does not apply to modifications. *See, e.g., Sunahara v. Burchard* (*In re Sunahara*) 326 B.R. 768 (B.A.P. 9th Cir. 2005); *In re Davis*, 439 B.R. 863 (Bankr. N.D. Ill. 2010).

Also after *Rhymaun* was decided, another colleague, Judge Kimball, issued a lengthy opinion disagreeing with *Rhymaun* and allowing early payoff. *In re Tibbs*, 478 B.R. 458 (Bankr. S.D. Fla. 2012). In *Tibbs*, Judge Kimball provides a well-reasoned statutory analysis in support of his conclusion that plans modified under § 1329(b) are not subject to the applicable commitment period requirements in § 1325(b)(4). *Tibbs*, 478 B.R. at 462-66. This Court agrees with *Tibbs* that "neither traditional approaches to statutory construction nor the wording of § 1329(b)(1) support the conclusion that § 1329(b)(1) incorporates § 1325(b)." *Id.* at 463.

Tibbs also addressed and rejected the argument that the Eleventh Circuit's *Tennyson* decision applies to modifications, stating that "[n]othing in *Tennyson* indicates that the Eleventh Circuit intended its broad statements in the context of chapter 13 plan confirmation to apply in the context of a later request to modify a confirmed plan." *Id.* at 467. And, referring again to the statutory argument, *Tibbs* noted that *Tennyson*'s "central analysis focused on the effect of § 1325(b), a provision not applicable to modification under § 1329." *Id.* Further, Judge Kimball noted that his decision did not open the door to abuse because § 1325(a)(3) applies to modifications and requires the court to find that a modified plan has been filed in good faith. *Id.* at 465.

Prior to *Tibbs* and *Rhymaun*, at least one other bankruptcy court in the Eleventh Circuit held that *Tennyson* was not controlling. *In re Smith*, 449 B.R. 817 (Bankr. M.D. Fla. 2011). In *Smith,* Judge McEwen held that *Tennyson* was a confirmation case not applicable to motions for early payoff. *Smith*, 448 B.R. at 819. For motions for early payoff, *Smith* held that creditors should have the right to choose the "bird in hand." *Id*. at 820. Stated more formally, *Smith* held that unsecured creditors, not the chapter 13 trustee, should have the choice to receive the full plan payment early rather than objecting because of the possibility that the debtor's income could go up and creditors could compel a modification to increase their distribution. *Id*.

The chapter 13 trustee in the Miami division of our district generally objects to early payoff regardless of whether creditors object. Certainly, the Trustee has standing to object. However, since this Court concludes that neither § 1329(b) nor *Tennyson* preclude early payoff, the Court will grant the Motion for Early Payoff here and likely, in future cases, absent creditor objection or evidence of bad faith.[2]

Although this Court permits early payoff, it must be done by a modified plan. As described in the introduction, the Debtor hopes to avoid an analysis of the "best interests test" in § 1325(a)(4) by withdrawing her Motion to Modify. She cannot. Paying off a plan early is reducing the time set forth in the plan for paying creditors. And § 1329(b)(2) requires a modification to "extend or reduce the time" for making plan payments.

B. The Modified Plan Must Satisfy the Best Interest of <u>Creditors Test in § 1325(a)(4) on the Effective Date of the Modification</u>

Section 1329(b)(1) instructs courts to apply § 1325(a) in considering modified plans. Section 1325(a)(4) requires a plan to provide value to unsecured creditors as of "the effective date" that is not less than the amount they would receive if the Debtor's estate was liquidated under chapter 7 on that date. In applying this statutory requirement, the Court must first determine whether "the effective date" under § 1325(a)(4) is the effective date of the original Plan or the effective date of the proposed Modified Plan.

Courts are split on whether the value is measured as of the original date of confirmation or at the time of modification. Some courts have held that the effective date of the confirmed plan still applies when the plan is modified. *See, e.g., In re Forbes*, 215 B.R. 183, 189 (8th Cir. BAP 1997) (holding that the effective date of the plan is not altered by a plan modification and therefore post-petition, post-confirmation assets are not included in the liquidation analysis for purposes of approving a modified plan); *In re Gibson*, 415 B.R. 735 (Bankr. D. Ariz. 2009) (holding that "the effective date of the plan" is the date of

[2] In *In re Carreiro*, 2013 WL 2353784 (Bankr. M.D. Fla. May 30, 2013), Judge Delano denied a motion for early payoff, declining to follow Judge McEwen's decision in *In re Smith*, 449 B.R. 817. In *Carreiro,* the debtor filed a motion for early payoff just 30 days after confirmation. Although this Court does not agree with Judge Delano's conclusion that § 1325(b) applies to modifications, I would probably have reached the same result under those facts based on a lack of good faith in the proposed modification.

confirmation unless the plan specifies a different date). However, a majority of courts apply the effective date of the modification in determining whether a modified plan satisfies the best interests test under § 1325(a)(4). *See, e.g., In re Barbosa,* 236 B.R. 540 (Bankr. D. Mass.1999), *aff'd* 235 F.3d 31 (1st Cir. 2000) (holding that the effective date of a modified plan for purposes of liquidation value is the date of the plan modification); *In re Madrid*, 2023 WL 3563019 (Bankr. W.D. Wash. May 18, 2023); *In re Nachon-Torres*, 520 B.R. 306, 313-14 (Bankr. S.D. Fla. 2014); *In re Nott*, 269 B.R. 250, 255 (Bankr. M.D. Fla. 2000).

This Court adopts the majority view and concludes that the effective date of the modified plan controls. As noted by my colleague, Judge Isicoff, in *Nachon-Torres*, and by Judge Heston in *Madrid*, the legislative history indicates that "the application of the liquidation value test must be redetermined at the time of the confirmation of the modified plan." H.R. Rep. No. 95-595, 95th Cong. 1st Sess. 431 (1977). Moreover, it seems that there would be no purpose in referencing § 1325(a)(4) as applicable to modifications if the same values established at confirmation of the original plan controlled in evaluating a modified plan.

Agreeing with the Trustee that the effective date of the Modified Plan applies does not mean that the Trustee prevails. The Court must still determine whether the appreciation in value would be value that a chapter 7 trustee could administer.

C. The Modified Plan Satisfies the Liquidation Test in § 1325(a)(4)

Summarizing where we are, the Court has found that (1) early payoff is permitted absent creditor objection or bad faith, (2) that early payoff requires a modified plan, and (3) that the Modified Plan must satisfy the best interest of creditors test in § 1325(a)(4), viewed on the effective date of the modification. So, would unsecured creditors be better off in a hypothetical chapter 7 liquidation on the effective date of the Modified Plain in this case?

The answer is no for two reasons.

First, the Circuits are split over who gets the appreciation in real property when a chapter 13 converts to chapter 7. Recently, the Ninth Circuit held that the appreciated value of the debtor's home could be administered by the chapter 7 trustee. *Castleman v. Burman (In re Castleman),* 75 F.4th 1052 (9th Cir. 2023). However, the Tenth Circuit reached the opposite conclusion last year, holding that post-petition appreciation in a non-exempt asset belongs to a debtor upon conversion from chapter 13 to chapter 7. *Rodriguez v. Barrera (In re Barrera),* 22 F.4th 1217 (10th Cir. 2022). The Eleventh Circuit has not yet ruled on the issue.

Why the split? It's complicated and requires an analysis of several apparently conflicting provisions of the Bankruptcy Code, including § 1306(a) which says that all property acquired during a chapter 13 case is property of the estate, and § 1327(b) which vests all property with the debtor on confirmation. And then there's § 348(f), which tells us what happens upon conversion. As one court aptly put it, "[h]armonizing the inharmonious is a tall order." *In re Elassal*, 654 B.R. 434, 438 (Bankr. E.D. Mich. 2023).

Because there is a second reason for finding the best interest test satisfied, discussed below, the Court is not taking a deep dive into the "who gets the appreciation" issue outlined above. However, as an alternate ground for approving the Modified Plan, the Court finds that the appreciation in the Property would not be subject to administration by a hypothetical chapter 7 trustee. Under the facts presented in this case, the Trustee could not compel a modification to increase the payout to unsecured creditors simply because the Property increased in value. Nor could the Debtor modify the Plan to reduce PHH Mortgage's secured debt if the value of the Property declined. The Court agrees with the court in *Elassal*, which stated that "[c]hapter 13 debtors assume the risk of depreciation in their revested assets. It stands to reason they should also enjoy the benefit of any post-confirmation appreciation of revested property when sold." *Elassal*, 654 B.R. at 446.

There is a second reason for finding the best interest test satisfied. If a hypothetical chapter 7 trustee sold the Property, all the proceeds would be paid to PHH Mortgage and not result in a distribution to unsecured creditors greater than that provided in the Modified Plan. That is so by operation of § 348 which describes what happens upon conversion. Specifically, § 348(f)(1)(B) tells us that "valuations of property and of allowed secured claims in the chapter 13 case shall apply only in a case converted to a case under chapter 11 or 12, but not in a case converted to a case under chapter 7." Therefore, the Valuation Order valuing the Property and PHH Mortgage's secured claim at $560,000 would not be in force if this case was converted to chapter 7. If there was any doubt about what this means, there is further explanation in § 348(f)(1)(C)(i) which states that "with respect to cases converted from chapter 13—

> the claim of any creditor holding security as of the date of the filing of the petition shall continue to be secured by that security unless the full amount of the claim … has been paid in full as of the date of conversion, <u>notwithstanding any valuation or determination of the amount of an allowed secured claim made for the purposes of the case under chapter 13</u>[.]

11 U.S.C. § 348(f)(1)(C)(i) (emphasis added).

Applied here, this means that if the Property was sold by a chapter 7 trustee for anything less than the remaining debt to PHH Mortgage (approximately $1.2 million less amounts received in the chapter 13 case) all the sale proceeds would be paid to PHH Mortgage. So, under the Modified Plan, the unsecured creditors are not receiving less on the effective date of the modification than they would receive if the Debtor was liquidated under chapter 7 on that date. Therefore, the Modified Plan satisfies the best interest of creditors test in § 1325(a)(4).[3]

Conclusion

The Debtor's largest creditor, PHH Mortgage, agreed to the valuation of the Property securing its debt. The unsecured creditors, including PHH Mortgage on account of its large unsecured claim resulting from the valuation, accepted the Plan that pays them each their pro rata share of $75,000. The Debtor now seeks to refinance the Property, which has increased in value, to pay off the Plan. The appreciated value belongs to the Debtor. Absent objection by the creditors or evidence of bad faith, and despite objection by the Trustee, the Court finds that the Debtor has the right to utilize the proceeds from the refinancing to pay off the Plan early and finds that the Modified Plan that the Debtor filed to accomplish the early payoff satisfies the requirements of § 1329. Therefore, it is –

ORDERED as follows:

1. The Motion for Early Payoff [DE# 189] is granted.
2. The Motion to Modify [DE# 194] is granted.
3. The Modified Plan [DE# 193] is approved.

###

Copies to:

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2000 NW 89th Place, Suite 201
Doral, Florida 33172
(Counsel for Debtor)

[3] In determining what the liquidation value would be in a hypothetical chapter 7, the Trustee asks the Court to consider the potential equity in two other non-exempt properties. The secured debt on these other properties is being paid directly under the Plan and the Modified Plan. The Court questions whether the equity, if any, in these properties at confirmation of the Plan was considered in evaluating the payments to unsecured creditors. Regardless, the Court finds that the equity, if any, in these properties that are treated outside of the Plan, should not be considered now, in ruling on the proposed modification.

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Faculty: Post-Petition Appreciation: When Things Go Up, Who Gets What?

Edward C. Boltz is the managing partner of the Law Offices of John T. Orcutt, P.C. in Durham, N.C., where he represents clients in not only chapter 13 and 7 bankruptcies, but also in related consumer rights litigation, including fighting abusive mortgage practices and developing solutions for student loans. Mr. Boltz served as the president of the National Association of Consumer Bankruptcy Attorneys (NACBA) from 2013-16 and remains on its board of directors, co-chairing its Legislative Committee. He served on ABI's Consumer Bankruptcy Commission from 2017-19 and on the Bankruptcy Council for the North Carolina Bar Association, for which he co-chaired the committee that created a mortgage-modification program for the North Carolina bankruptcy courts. Mr. Boltz is a frequent speaker on bankruptcy issues at both national and local seminars, including at NACBA conventions and workshops, past NCLC workshops and the North Carolina Bankruptcy Institute. In June 2019, he testified on behalf of NACBA in Congress regarding the need for changes to the Bankruptcy Code to make student loans dischargeable and to the means test for disabled veterans. In 2008, he testified before Congress to similarly protect those in the National Guard and reservists, which was enacted as the National Guard and Reservists Debt Relief Act. For the spring 2020 semester, Mr. Boltz served as an adjunct professor at the University of North Carolina School of Law, assisting clients in the Consumer Financial Transactions clinic with student loans. He is a member of the North Carolina State Bar, which certified him as a specialist in consumer bankruptcy law, and he is admitted to practice before the districts courts in both the Eastern and Middle Districts of North Carolina. Mr. Boltz received his B.A. from Washington University in St. Louis in 1993 and his J.D. from George Washington University in 1996.

Hon. Elizabeth L. Gunn is a U.S. Bankruptcy Judge for the District of Columbia in Washington, D.C., appointed on Sept. 4, 2020. A COVID-era selection and appointment, she was sworn in by Zoom from her living room. Prior to her appointment, Judge Gunn served as an Assistant Attorney General for the Commonwealth of Virginia as the bankruptcy specialist for the Division of Child Support Enforcement. She also practiced law in Richmond, Va., at Sands Anderson PC and McGuireWoods LLP. In 2017, Judge Gunn was honored as a member of ABI's inaugural class of "40 Under 40." In 2022, she was recognized by the Bar Association of the District of Columbia as its Judicial Honoree and recipient of the BADC's Suzanne V. Richards Foundation Grant. Judge Gunn serves on the advisory board of the American Bankruptcy Law Journal and is a coordinating and associate editor of the ABI Journal. In addition, she sits on the boards of the Federal Bar Association Bankruptcy Section, International Women's Insolvency & Restructuring Confederation, American Bar Association, National Conference of Federal Trial Judges and the Chesapeake Chapter of the Turnaround Management Association. She also is a member of the Walter Chandler Bankruptcy Inn of Court and is Board Certified in Consumer Bankruptcy Law by the American Board of Certification. Judge Gunn received her B.A. cum laude from Willamette University and her J.D. cum laude from Boston College Law School.

Prof. Jonathan M. Seymour is an associate professor of law at Duke University School of Law in Durham, N.C. A bankruptcy scholar whose research spans topics in business and consumer bankruptcy law, his most recent work focuses on bankruptcy procedure and the governance of bankruptcy cases, examining the distinct legal culture of bankruptcy courts and its effect on the process and practice of bankruptcy on the ground. His work has been published or is forthcoming in the University of Chicago Law Review, the Illinois Law Review and the Emory Journal of Bankruptcy Developments. Prof. Seymour joined the faculty in July 2022 after serving for three years as a Visiting Assistant Professor at Duke Law. Prior to coming to Duke, he was a senior associate specializing in bankruptcy litigation in the Washington, D.C., office of WilmerHale. His experience has included participation in two merits-stage Supreme Court cases, as well as a number of appeals court cases involving bankruptcy issues, the representation of a trade association in connection with a major report proposing reforms to business bankruptcy law, and the representation of financial institutions in consumer cases in the bankruptcy courts. Prof. Seymour holds a first-class degree in law with German Law from Oxford University, and he received his J.D. with highest honors from The George Washington University Law School.