

**Confirming the Plan in the Individual Chapter 11 Case**

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## **Introduction**

This article discusses issues attendant the confirmation of the Chapter 11 plan in the individual case and suggests that the individual Chapter 11 plan can be confirmed quickly and cost-effectively if the process is well-planned at the beginning. We use as a point of reference a “model plan” developed by San Francisco Bankruptcy Judge Thomas E. Carlson in conjunction with the Bench-Bar Liaison Committee of the Northern District of California, integrating ideas from plans used throughout the state, including the small business plan and disclosure statement forms designed to implement the final Bankruptcy Rules effective December 1, 2008.<sup>2</sup> We also suggest the use of a simplified disclosure statement as an alternative to the 25-page Official Form 25B.<sup>3</sup>

## **Why Chapter 11?**

With the number of cases dramatically rising, as well as their complexities, *e.g.* nondischargeable debt, priority taxes, contingent claims, personal guarantees, and the like, the need to make Chapter 11 work for the individual is acute. A debtor trying to save a house or buy time may be disqualified from Chapter 13 or 7, and may be using Chapter 11 to delay foreclosure while finding an apartment (the costs to file the petition are sometimes less than rent or the mortgage payment). The serious Chapter 11 debtor is looking to maintain control over his affairs, whether it be the preservation of a business, the liquidation of his assets, or a combination of both. In what was then considered a major change in bankruptcy practice, the Bankruptcy Reform Act of 1978 included §1123(b)(4) in the new Code, allowing a Chapter 11 plan to “provide for the sale of all or substantially all property of the estate.”<sup>4</sup> (Under prior law, liquidation was considered inappropriate for Chapter 11, and grounds for “adjudication” under the then equivalent of Chapter 7.<sup>5</sup>) Now, the debtor who wishes to control the liquidation of his assets in order to maximize asset values, thereby protecting a third-party guarantor, avoiding a deficiency claim, or preserving a surplus, can use Chapter 11 instead of Chapter 7.

## **Planning the Exit Strategy**

Counsel must have the Chapter 11 confirmation requirements in mind at the time of the initial client interview in order to determine whether Chapter 11 is appropriate for the client.<sup>6</sup> The outline of the plan must be in place early for at least two important reasons: firstly, if the debtor is not going to be able to satisfy the many confirmation requirements of Bankruptcy Code §1129(b), or draft a plan that satisfies each requirement of §1122(a), then the Chapter 11 case may be a waste of time and effort and an exercise in frustration for all concerned. Second, and equally important, is the need to be prepared to defend the Chapter 11 to the U.S. Trustee, the creditors, and the court. The debtor will be called upon to explain the reason for the Chapter 11 at various times in the case such as the Initial Debtor Interview, the §341 meeting, and the first status conference before the court. Moreover, under revised §1112(b), the court is required to convert a Chapter 11 case to one under Chapter 7 upon motion of a party in interest

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<sup>2</sup> Fed. Rules Bankr. Prac. Refs & Annos, 11 U.S.C.A. FRBP Refs & Annos.

<sup>3</sup> Official Bankruptcy Form 25A, 11 U.S.C.A., FRBP Official Form 25A

<sup>4</sup> 11 U.S.C. §1123(b)(4)

<sup>5</sup> The Bankruptcy Statute of 1898, as amended, §§776-780, 11 U.S.C. §376

<sup>6</sup> A suggested interview checklist is provided at the end of this article.

unless the debtor shows a “reasonable likelihood that a plan will be confirmed” within the timeframes of a small business case, discussed below. In order to avoid conversion, the debtor’s game plan needs to be in place at the outset of the case, because opponents will seize on the debtor’s lack of purpose and direction to argue that the case is a delaying tactic without a bona fide reorganization purpose.

BAPCPA<sup>7</sup> imposes new requirements on the individuals entering Chapter 11. Indeed, Judge Markel says BAPCPA “works mischief at all stages of the reorganization process.”<sup>8</sup> The lawyer comfortable with business bankruptcies will find himself in a whole new world of BAPCPA consumer-related rules, deadlines and penalties imposed for incorrect or untimely action.<sup>9</sup> Nevertheless, if used cleverly, Chapter 11 will be more amendable to small business debtors and individuals by functioning for individual debtors much as does Chapter 13. BAPCPA created several new provisions that raise issues<sup>10</sup> relevant to the individual Chapter 11 debtor; among those pertinent to the individual chapter 11 plan, which will be addressed here, are:

- Not only are the debtor’s post-petition earnings brought into the estate,<sup>11</sup> but the debtor’s plan must provide for payment to creditors from post-petition earnings,<sup>12</sup> and propose to distribute property worth *at least* as much as the debtor’s projected disposable income for a five-year period;<sup>13</sup>—exactly what commitment of post-confirmation income must the debtor make to fund the plan, and is it not really as bad as it looks?
- The exception to the absolute priority rule allows the debtor to keep property of the estate without paying in full a class of unsecured creditors that rejected the plan;<sup>14</sup> Does this mean *all* property of the estate, or only the post-petition earnings brought into the estate by §1115?
- Chapter 11 plans usually provide for the revesting of property of the estate in the reorganized debtor upon confirmation, but the discharge is delayed in the individual case until completion of payments—should the revesting also be delayed until the time of discharge, and what are the implications?

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<sup>7</sup> Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. Pub. L. No. 109-8, 119 Stat. 23 (2005). We refer to the legislation as “BAPCPA” throughout the article. Most of the provisions of BAPCPA became effective as of October 17, 2005, although there were some exceptions. For a summary of the effective dates for various BAPCPA provisions, *See*, Hon. William Houston Brown and Lawrence Ahern III, 2005, *Bankruptcy Reform Legislation With Analysis*, §§ 1.3, 1.4 and 1.5 (Feb. 2006).

<sup>8</sup> Markell: *The Sub Rosa Subchapter: Individual Debtors in Chapter 11 After BAPCPA*, 2007 V. Ill. L. Rev. 67 (2007)

<sup>9</sup> For example, termination of the automatic stay where the debtor has failed to act upon his statement of intention, discussed at p. 21, *infra*.

<sup>10</sup> BAPCPA’s susceptibility to conflicting interpretations has spawned several studies of the competing theories of statutory interpretation, particularly “purposivism” versus “textualism,” as applied to BAPCPA. *See*, for example, *Principled Principles of Statutory Interpretation: A Judicial Perspective After Two Years of BAPCPA*, Waldron & Berman, 81 Am. Bankr. L.J. 195. *See also*, *In re PW, LLC, debtor; Clear Channel Outdoor, Inc. v. Nancy Knupjer*, 391 B.R. 25 (9<sup>th</sup> Circuit BAP (Cal.) 2008)

<sup>11</sup> 11 U.S.C. §1115

<sup>12</sup> 11 U.S.C. §1123(a)(8)

<sup>13</sup> 11 U.S.C. §1129(a)(15)

<sup>14</sup> 11 U.S.C. §1129(b)(2)(B)(ii)

- While entry of the debtor’s discharge is delayed until completion of all payments under the plan, the Code also allows for a “non-payment discharge” -- is “hardship” required as a condition of receiving this discharge?<sup>15</sup>
- Modification of a confirmed plan, by a creditor as well as the debtor, is permitted even after substantial consummation<sup>16</sup>—does this allow a hostile creditor to hold the debtor hostage indefinitely by obtaining modification at every opportunity?
- An objection by an unsecured creditor triggers the debtor’s obligation to commit post-petition income to the plan—can this be anticipated and mollified, if not prevented, by aggressively classifying claims?

In addition, the administration of the individual Chapter 11 case entails many complexities, such as record-keeping requirements at a level the debtor may not be used to; monthly operating reports that sometimes confuse and challenge the debtor; community property issues requiring the involvement of the non-debtor spouse; dischargeability problems, including the ever-present priority taxes. Because the Chapter 11 case spans a longer time frame than the Chapter 13 case, counsel is tempted to become complacent and take the maximum time allowed, generally six to nine months, to develop the plan. This is not constructive, and can impair the chances of success. Rather, counsel should be moving quickly to conclude the case because the complexities of chapter 11 make it more important than ever to develop the exit strategy sooner rather than later.

### **Who May File the Plan and When is it Due?**

There is a common misconception that the Chapter 11 plan is due within four months of the petition date. This time period is actually the 120-day exclusivity period of §1121(b), which applies to Chapter 11 cases generally. There is generally no due date for the filing of the Chapter 11 plan and disclosure statement unless the debtor is a “small business debtor”,<sup>17</sup> in which case the plan is due 300 days after the order for relief.<sup>18</sup>

The exclusivity period in a small business case is 180 days, after which time (unlike chapter 13<sup>19</sup>) any party in interest may file a plan.<sup>20</sup> Both this and the 300 day plan-filing deadline may be extended, after notice and a hearing, if the debtor demonstrates by a preponderance of the evidence that he is more likely than not to confirm a plan in a reasonable time.<sup>21</sup> The order granting the extension must be signed before the existing deadline expires.<sup>22</sup>

In the small business case it will generally not be necessary to extend the exclusivity period, because there is probably no other party who is going to file a plan that is adverse to the debtor. Counsel should have a sense about whether a third party plan is likely, and should also be aware of the propensities of the court to extend exclusivity. As we suggest later, control of exclusivity can be important in a case with a hostile creditor because of the debtor’s vulnerability respecting control of his post-

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<sup>15</sup> 11 U.S.C. §1141(d)(5)

<sup>16</sup> 11 U.S.C. §1127(e)

<sup>17</sup> 11 U.S.C. §101[51(D)]

<sup>18</sup> 11 U.S.C. § 1121(e)(1)(J)

<sup>19</sup> 11 U.S.C. §1321

<sup>20</sup> 11 U.S.C. §1121(e)(1)

<sup>21</sup> 11 U.S.C. §1121(e)(3)(A)

<sup>22</sup> 11 U.S.C. §1121(e)(3)(C)

confirmation income.<sup>23</sup> The 9<sup>th</sup> Circuit Bankruptcy Appellate Panel has noted that “before 1994, there was a perceived abuse in the practice of some courts routinely extending exclusivity without requiring proof of “cause,” in circumstances that were effectively unreviewable due to the difficulty of obtaining leave to appeal, and thus upset the balance of competing interests reflected by the 120 and 180-day periods is §1121.”<sup>24</sup> In reviewing an order extending exclusivity, the BAP, citing the factors of the *Dow Corning*<sup>25</sup> and *Express One*<sup>26</sup> cases regarding §1121(d) stated that it is a mixed question of law and fact, and found “cause” for the extension where: “(1) a first extension; (2) in a complicated case; (3) that has not been pending for a long time relative to its size and complexity; (4) in which the debtor did not appear to be proceeding in bad faith; (5) had improved operating revenues so that it was paying current expenses; (6) had shown a reasonable prospect for filing a viable plan; (7) was making satisfactory progress negotiating with key creditors; (8) did not appear to be seeking an extension of exclusivity to pressure creditors; and (9) was not depriving the Committee of material or relevant information.”<sup>27</sup>

### **Small Business Debtors**

The Bankruptcy Code defines a “small business debtor” as a person (i.e. not necessarily an individual) engaged in a commercial or business activity, with aggregate non-contingent, liquidated secured and unsecured debt of not more than \$2,190,000.00, in a case where there is either no creditors’ committee,<sup>28</sup> or the court finds that the committee “has not been sufficiently active and representative to provide effective oversight of the debtor.”<sup>29</sup> There is no longer an election to be made<sup>30</sup>—the petition must indicate whether or not the debtor is a “small business,” and the debtor’s statement determines the status of the case unless an objection is filed within 30 days after the conclusion of the §341(a) meeting.<sup>31</sup> Among the implications of the small business designation, those relating to the plan process are:

1. The plan and disclosure statement must be filed within the first 300 days of the case.<sup>32</sup> The plan must be confirmed within 45 days after it is filed, subject to extension.<sup>33</sup>
2. The plan confirmation process may be streamlined by use of a combined plan and disclosure statement; the court can “conditionally approve” the disclosures and combine the final approval of the disclosure statement with confirmation of the plan.<sup>34</sup>

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<sup>23</sup> See, discussion of 11 U.S.C. §1129(a)(15) *infra*.

<sup>24</sup> *In re Henry Mayo Newhall Memorial Hospital* 282 B.R. 444 (9<sup>th</sup> Cir. BAP 2002)

<sup>25</sup> *In re Dow Corning Corp.* 208 B.R. 661, 664-665 (Bankr. E.D. Mich. 1997)

<sup>26</sup> *In re Express One Int, Inc.* 194 B.R. 98, 100 (Bankr. E.D. Tex. 1996)

<sup>27</sup> *In re Henry Mayo Newhall Memorial Hospital*, *supra* 282 B.R. 444 at p. 7

<sup>28</sup> 11 U.S.C. § 101(51D)

<sup>29</sup> F. Rule Bankr. P. 1020(c)

<sup>30</sup> F. Rule Bankr. P. 1020 was amended in 2008 to delete the election.

<sup>31</sup> F. Rule Bankr. P. 1020(b)

<sup>32</sup> 11 U.S.C. § 1121(e)

<sup>33</sup> 11 U.S.C. § 1129(e)

<sup>34</sup> 11 U.S.C. § 1126(f)(3)(A)

## **Major Considerations in Drafting the Individual's Plan**

Between §1123 and §1129 there are close to two dozen issues that either may or must be addressed in the plan. In keeping with the scope of this article, we focus on those peculiar to the individual case.

### *A. The Absolute Priority Rule and the BAPCPA Exception*

The absolute priority rule is a judicially-developed doctrine prohibiting confirmation of a plan, over a creditor's objection, if the plan allows the debtor to retain any property of the estate without paying creditors in full. The "absolute priority rule" only applies in the context of a "cramdown" situation, and when a creditor has raised the objection.<sup>35</sup> If all classes have approved the Plan, the cramdown provisions, including the "absolute priority rule" are not implicated.

BAPCPA created an exception to this rule by providing that "in a case in which the debtor is an individual, debtor may retain property included in the estate under §1115..."<sup>36</sup> This provision overrules the Supreme Court decision in *Norwest Bank Worthington v. Ahlers*,<sup>37</sup> which stated that the new value exception, if it exists at all, could not be satisfied by the contribution of postconfirmation personal services ("sweat equity") that a farmer may contribute in growing crops.

§1115 provides that, in a Chapter 11 case involving an individual, property of the estate includes, in addition to the property defined in §541, after-acquired property and the debtor's personal earnings.<sup>38</sup> But the new language of §1129 and §1115 is worded in such a way that the exception could be construed either narrowly, to cover only the additional, post-petition property brought into the Chapter 11 bankruptcy estate by §1115(a), or broadly, to cover not only that property but also all the property brought into the estate by §541, most of which is property the debtor had before filing bankruptcy.<sup>39</sup> The former construction is disfavored because it greatly limits the impact of the new exception under §1129(b)(2)(B)(ii).<sup>40</sup> The latter exempts the individual Chapter 11 debtor from the main facet of the absolute priority rule, allowing him to retain both pre- and post-petition property under a plan even though a class of unsecured creditors is not being paid in full. This more expansive view of the change in existing law allows an individual Chapter 11 case to resemble a Chapter 13 case, and is the favored view.<sup>41</sup>

### *B. Funding the Plan Through Payments-Can the Debtor Survive After Confirmation for Five Years?*

The feasibility of the plan must be analyzed carefully, because the debtor must make a substantial commitment of his post-confirmation resources as a condition of confirmation. The "checklist" at the end of this article is useful to give the prospective debtor an idea of what he is undertaking. Most significantly, the Code now requires an

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<sup>35</sup> 11 U.S.C. §1129(b); *Steelcase, Inc. v. Johnston*, 21 F.3d 323, 329 (9th Cir. 1994); *In re United Marine*, 197 B.R. 942, 947-48 (Bankr. S.D. Fl. 1996); *In re Hoosier Hi-Reach, Inc.*, 64 B.R. 34, 36-37 (Bankr. S.D. Ind. 1986).

<sup>36</sup> 11 U.S.C. §1129(B)(2)(b)(ii)

<sup>37</sup> 485 U.S. 197, 108 S. Ct. 963, 99 L. Ed. 2d 169 (1988)

<sup>38</sup> 11 U.S.C. §1115

<sup>39</sup> See, *In Re Bullard* 358 B.R. 541 (Bkrty. D. Conn., 2007)

<sup>40</sup> See, e.g. *In re Roedemeier* is discussed extensively by Martin at 29 Cal. Bankr. J. 545 (2008); 374 B.R. 264 (Bankr. D Kansas 2007), where a dentist retained his practice and did not pay unsecured creditors in full. *Roedemeier* is discussed extensively by Martin at 29 Cal. Bankr. J. 545 (2008)

<sup>41</sup> 5 *Norton Bankr. L. & Prac.* 3d §106:1

individual debtor, where an unsecured creditor has objected to confirmation of the plan, to distribute property of a value that is not less than the “projected disposable income” of the debtor for the greater of five years or the term of the plan.<sup>42</sup> But there are several things that take the sting out of this provision:

- While the chapter 13 plan must provide that a debtor’s projected disposable income be applied to make payments to *unsecured creditors* under the plan,<sup>43</sup> in the chapter 11 plan the debtor’s income need not be so dedicated and may be used to make *all* plan payments.<sup>44</sup> Therefore, the required payments to, for example, priority and secured creditors, will count against the five-year benchmark. Moreover, the result could be a significantly lower total payout to creditors in Chapter 11 than in Chapter 13, more than offsetting the additional cost of a Chapter 11 case.
- Although §1129(a)(15)(B) refers to §1325(b)(2) for the definition of “projected disposable income,” defining it as “current monthly income received by the debtor,” the Chapter 7 means test does not apply. The expense portion of the calculation of projected disposable income under §1325(b)(2) for an above-median-income debtor is not determined by the Chapter 7 means test, but is instead determined by the court.<sup>45</sup> It is therefore up to the creditor to question the reasonableness of the debtor’s claimed expenses and provide evidence in support of any such objection.
- There is an argument to be made that “projected disposable income” is no more than “disposable income” annualized and “projected” over the applicable commitment period. That is to say, disposable income in the context of a chapter 13 is income for the six months prior to the petition date. Chapter 13 cases interpreting “projected disposable income” fall into two camps. The majority approach utilized by approximately 40 courts essentially holds that Form 22 is merely a starting point for determining “projected disposable income” and that the court can consider the debtor’s circumstances at the time of the plan confirmation and the debtor’s future finances.<sup>46</sup>

The minority approach, which to date has been followed by approximately 20 courts, hinges on a “plain meaning” approach to determining “projected disposable income.”<sup>47</sup> Under this approach, “projected disposable income, is merely “disposable income” annualized over the applicable commitment period, and to hold otherwise would be to render the definition of “disposable income” in §1325(b)(2) a meaningless, superfluous definition.<sup>48</sup>

The bankruptcy court in *Roedemeier*, *supra* was untroubled by the fact that “projected disposable income” meant the same thing as “disposable income,”

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<sup>42</sup> 11 U.S.C. §1129 (a)(15)

<sup>43</sup> 11 U.S.C. §1325(b)(1)(B)

<sup>44</sup> 11 U.S.C. §1129(a)(15)

<sup>45</sup> *In re Roedemeier*, *supra*. 7 COLLIER ON BANKRUPTCY, 1129.03[15][a] at p. 1129-74.9 (15<sup>th</sup> ed. rev’d 2007)

<sup>46</sup> *See, In re Wilson*, 397 B.R. 299 Bankr. (M.D.N.C. 2008) (summarizing decisions)

<sup>47</sup> *Id* at p. 4

<sup>48</sup> *See, In re Mancl*, 381 B.R. 537, 541 (W.D. Wis. 2008); *In re Frederickson*, 375 B.R. 829, 832 (Bankr. 8<sup>th</sup> Cir. 2007); *In re Berger*, 376 B.R. 42, 47 (Bankr. M.D. Ga. 2007); and *In re French*, 383 B.R. 402 (Bkrcty. W.D. Ky (2008)

which is likely due to the specific wording of §1129(a)(15). At least one commentator has opined that the wording of § 1129(a)(15) “rather unequivocally implies that ‘projected disposable income’ is simply annualized disposable income.”<sup>49</sup> However, one court has challenged this conclusion, noting that it is just as likely that §1129(a)(15) is another example of the loose drafting of the BAPCPA as it is a clear expression of Congress’ intent.<sup>50</sup>

- The minimum duration of the plan may not be what it appears—although §1129(a)(15) requires that the value of property to be distributed is not less than five years of the debtor’s projected disposable income, this is a benchmark and not a timeline, i.e. if property from any other source, whether estate property or otherwise, is used to fund the plan, it may be shorter. In a case where the debtor will have significant post-petition income, the “best interests” requirement of chapter 11 is rendered immaterial.<sup>51</sup> This is because of the interplay of §§1115 and 348, which provides that, in a converted case, the estate is deemed to have been created as of the filing date.<sup>52</sup> All disposable income brought into the estate under §1115 is then recharacterized as property of the debtor under §541(a)(6). The debtor’s projected disposable income is therefore not used in the “liquidation analysis,” and the liquidation value of the other property of the estate will not increase the minimum plan distribution, although it can be used to fund the plan in lieu of the actual income received for five years, as long as it is not less than that amount.
- It is possible for the debtor to obtain a discharge if he does not complete payments, if the value, on the plan’s effective date, of property actually distributed to creditors, is at least what creditors would receive in a chapter 7 liquidation.<sup>53</sup>

The drafting of the plan to accommodate §1129(a)(15) will require careful consideration because counsel does not yet know if an unsecured creditor will object and raise the §1129(a)(15) issue. The disclosure statement provides for schedules I and J to be attached, and a calculation made as to the amount of the five years’ projected disposable income.<sup>54</sup> The Model Plan allows for flexibility in presenting this.<sup>55</sup>

It should be noted that the Model Plan does not provide for appointment of a disbursing agent to monitor the debtor’s performance under the plan.<sup>56</sup> The Model Plan spells out the creditor’s rights upon material default, creditors may either proceed under applicable non-bankruptcy law to enforce their rights, or file and serve a motion to convert the case to one under Chapter 7.<sup>57</sup>

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<sup>49</sup> Randolph J. Haines, *Chapter 11 May Resolve Some Chapter 13 Issues*, 8 *Norton Bankr. L. Advisor* 1 (Aug. 2007).

<sup>50</sup> *See, In re Pak*, 378 B.R. 257, 264 n.7 (Bankr. 9<sup>th</sup> Cir. 2007)

<sup>51</sup> The “best interests” test is that each creditor receive as much in a chapter 7 liquidation as he will under the plan. *See*, 11 U.S.C. §1129(a)(8).

<sup>52</sup> 11 U.S.C. §348(f)(2)

<sup>53</sup> This is discussed *infra* at section H.

<sup>54</sup> *See*, Model Disclosure Statement ¶D, under section entitled Financial Information.

<sup>55</sup> *See*, Model Plan, part 8.

<sup>56</sup> Some courts *e.g.* Judge Morgan of the San Jose division of the Northern District, use a model plan that appoints a disbursing agent as a counterpart to the chapter 13 trustee. The Model Plan rejects this approach in favor of allowing creditors to monitor the debtor’s performance.

<sup>57</sup> *See*, Model Plan, Section 10(d)

C. *Vesting Property of the Estate in the Reorganized Debtor*

Chapter 11 plans usually provide for the vesting of all property of the estate in the reorganized debtor upon the effective date.<sup>58</sup> The debtor is usually anxious to get out of chapter 11 and get his property back as soon as possible. But the Code also recognizes that the immediate vesting of property might not always be appropriate and allows that the plan might provide that assets *not* revest until a later time, *i.e.* the entry of discharge. There are two ways to approach this: on the one hand, the debtor may wish to continue to operate subject to the jurisdiction of the Bankruptcy Court, with the opportunity to return to court to obtain orders as needed. The estate will remain open, protected by the automatic stay, which would otherwise terminate.<sup>59</sup> On the other hand, as suggested by *Norton*, “once the plan has been confirmed, the debtor will want to close the case and file a final decree under chapter 11 in order to stop the accrual of the U.S. Trustee’s fees. Thus it is likely that chapter 11 debtors will seek to close a case upon the confirmation of the plan and then file a motion to reopen the case once the plan is completed in order to obtain the entry of the chapter 11 discharge order.”<sup>60</sup>

There are some problems with the *Norton* approach: for one thing, as discussed in the next section, the court may not allow the debtor to close the case upon confirmation. For another, there may be tax problems that can be avoided by continuing the estate as a taxable entity.<sup>61</sup>

Because the estates are still under administration, Bankruptcy Code §505(b)(2) will allow the debtor to annually request determination of any unpaid liability, giving the tax collector 60 days after such request to give the debtor notice that the return has been selected for examination, and 180 days to complete the examination. Also, there will be no reduction of the net operating losses which are in the estate, allowing them to be used post-confirmation.

Moreover, deferring the closing of the estate avoids any issue as to which entity—the estate or the individual—is liable for the debtor’s post confirmation income and capital gains on sales of assets whose proceeds are distributed to creditors. If the estate is closed, the individual will likely be liable for taxes on post-confirmation income and gains on asset sales that are distributed to creditors under the plan rather than the estate being responsible for the taxes.<sup>62</sup> In *Hollywell Corp. v. Smith*,<sup>63</sup> the plan established a trust and appointed a trustee to liquidate the property of the estate. The Court held that the trustee was obligated to file income tax returns and pay taxes attributable to the corporate debtor’s property as well as to the individual debtor’s property, notwithstanding

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<sup>58</sup> Model Plan, part 9(b), which is consistent with 11 U.S.C. §1141(b)

<sup>59</sup> See, *In re Hillis Motors* 997 F2d 581 (9<sup>th</sup> Cir. 1993).

<sup>60</sup> 5 *Norton Bankr. L. & Prac.* 3d §106:1. But at least one court disagrees. See, *In re Ball*, 2008 WL 2223865 (Bkrcty.N.D.W.Va.), Discussed *infra* at p. 19

<sup>61</sup> Martin, *The Path for the Pursuit of Fairness in Chapter 11 Cases of Individuals* 29 Cal. Bankr. J. 429 (2007)

<sup>62</sup> Martin *supra*.

<sup>63</sup> 503 U.S. 47, 112 S. Ct. 1021, 117 L. Ed. 2d 196 (1992)

The lesson of *Hollywell* to be applied to answer the question of who pays taxes on post-confirmation income of an individual debtor is that it depends on what the plan says. If the plan does not revest income in the debtor, then clearly the estate should be paying taxes on it. It is the revesting which occurs by default in Chapter 11 and 13 cases upon confirmation which is the root of all of the uncertainty over who pays what tax.

the terms of the plan. Essentially, the Court held that the plan created a separate entity which was liable for the tax.

It might be mentioned in passing that the Central District of California does not re-vest property in a Chapter 13 debtor upon confirmation. Every plan provides that “Property of the estate shall not re-vest in the debtor until such time as a discharge is granted or the case is dismissed or closed without discharge. . . . Prior to any discharge or dismissal, the Debtor must seek approval of the court to purchase, sell, or refinance real property.” But the Northern District Form Chapter 13 Plan provides for immediate vesting. This is mentioned for illustrative purposes only because the chapter 13 model is not analogous—the chapter 13 estate is not a separate entity for tax purposes as is the chapter 11 estate.<sup>64</sup> The debtor is the taxpayer and is responsible for staying current with all post-petition taxes. The definitions of property of the estate for chapter 11<sup>65</sup> and chapter 13<sup>66</sup> are nearly identical and include the debtor’s earnings; however, in chapter 13, the debtor’s future earnings are submitted to the supervision of the trustee to the extent necessary to fund the plan.<sup>67</sup> Thus, even if a debtor in chapter 13 elects to have all of the property of the estate re-vest at the time of confirmation, the income is not re-vested because it is a mandatory plan provision to have the debtor’s post-petition income under the control of the trustee to assure that the plan can be funded.

#### *D. Delayed Discharge and Closing the Case*

Having made the decision whether to re-vest property of the estate, counsel must be consistent respecting the timing of discharge and the closing of the case. Inconsistency will create confusion, *e.g.* if the plan dedicates future earnings to creditors, immediate re-vesting coupled with delayed closing ends the automatic stay and leaves the debtor liable for taxes that the estate should be paying; immediate closing coupled with delayed re-vesting leaves the estate in questionable status. Put another way, the plan must avoid conflict between §1115 (earnings are property of the estate until the estate closes) and §1141 (property of the estate re-vests on confirmation unless otherwise provided).

Even if the debtor’s plan re-vests property of the estate upon the effective date, it is not certain that the will grant a final decree closing the case until payments have been completed. Chapter 11 cases are usually closed upon “substantial consummation”.<sup>68</sup> The Code provides that “after an estate is fully administered in a Chapter 11 reorganization case, the court, on its own motion or on motion of a party in interest, shall enter a final decree closing the case.”<sup>69</sup> But some courts feel this is not appropriate in the individual case because discharge is not entered in an individual case until “completion of all payments under the plan.”<sup>70</sup> The BAPCPA changes to the Code make the individual Chapter 11 case more akin to the administration of a Chapter 13 case, which is not closed

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<sup>64</sup> 11 U.S.C. §§346(b)(1), 346(d)

<sup>65</sup> 11 U.S.C. §1115

<sup>66</sup> 11 U.S.C. §1306

<sup>67</sup> 11 U.S.C. §1322(a)

<sup>68</sup> 11 U.S.C. §1101(2) defines “substantial consummation” to mean (A) transfer of all or substantially all of the property proposed by the plan to be transferred; (B) assumption by the debtor or by the successor to the debtor under the plan of the business or of the management of all or substantially all of the property dealt with by the plan; and (C) commencement of distribution under the plan.

<sup>69</sup> *See*, 11 U.S.C. §350 (a) and Fed. R. Bankr. P. 3022

<sup>70</sup> 11 U.S.C. §1141(d)(5)

until all plan payments have been made and discharge is entered,<sup>71</sup> or so the argument goes. The desire to avoid accrual of U.S. Trustee fees<sup>72</sup> is not grounds for closing the case.<sup>73</sup>

On the other hand, there is authority to grant the discharge at time of confirmation and some courts will do so. In *In re Sheridan*<sup>74</sup> Bankruptcy Judge Small noted that the bankruptcy court is given the power to deviate from the general rule of §1141(d)(5) if the court finds “cause” and “after notice and a hearing” to creditors that the discharge is being sought early. The Court found that the notice requirement was fulfilled by a conspicuous notice in the disclosure statement in bold and capital letters that the debtor was requesting that the discharge be effective upon confirmation. The Court found persuasive the significant evidence that payments under the plan would be made, and that this supported entry of discharge.<sup>75</sup>

*E. Classification of Claims.*

Before considering the nuances of claims classification in the individual chapter 11 context, we review the basic rules applicable to all chapter 11 cases:

§1123(a) of the Bankruptcy Code sets forth the mandatory provisions that must be included in a plan. First and foremost, the plan must designate classes of claims subject to §1122 of the Bankruptcy Code.<sup>76</sup> The plan must propose the same treatment for each claim included within a class unless the holder of a particular claim consents to less favorable treatment.<sup>77</sup> Claims classification is important to the plan confirmation process because creditors vote to accept or reject a plan of reorganization by class, and a plan will be deemed accepted by a class of impaired claims if it is accepted by more than one-half in number of claimants that hold at least two-thirds in amount of allowed claims that have voted on the plan.<sup>78</sup>

Creditor classification is always done with an eye towards voting and confirmation, because the debtor must obtain the consent of at least one impaired class in order to confirm the plan.<sup>79</sup> If he wishes to proceed without the vote of each impaired

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<sup>71</sup> *In re Ball* (2008 WL 2223865 (Bkrcty.N.D.W.Va. 2008)). However, the automatic stay of 11 U.S.C. §362(a) terminates upon confirmation of the plan. See, Model Plan part 10(a).

<sup>72</sup> *In re Celebrity Home Entertainment, Inc.* 210 F 3d 995 (9<sup>th</sup> Circuit BAP 2000)

<sup>73</sup> *Ball, supra; In re SLE, Inc.*, 2005 Bankr.LEXIS 1322 at \*7-8, 2005 WL 1668396

<sup>74</sup> 391 B.R. 287 (Bkrcty E.D.N.C. 2008)

<sup>75</sup> Judge Small comments that “delaying the discharge until all payments are made presents several practical problems. How will the court know when all payments have been made? Typically, there is no trustee in a chapter 11 case, so presumably it will be up to the debtor to notify the court that all plan payments have been made. In the Eastern District of North Carolina, notification of the completion of plan payments is accomplished by a notice and request for discharge that is sent to the court and served on all creditors and the bankruptcy administrator.

“A delayed discharge also raises questions regarding the timing of the closing of the case. If the debtor does not get a discharge until all payments are made, must the case remain open until the discharge is entered? If no notice of payment completion is filed will the case remain open indefinitely? Must the clerk’s office or the bankruptcy administrator’s office monitor the case to see that the notice is filed? And, as long as the case remains open, must the debtor pay the chapter 11 quarterly fees required by 28 U.S.C. § 1930(a)(7)?” (*Id.* at p 291)

<sup>76</sup> 11 U.S.C. §1123(a)(1)

<sup>77</sup> 11 U.S.C. §1123(a)(4)

<sup>78</sup> 11 U.S.C. §1126(c)

<sup>79</sup> 11 U.S.C. § 1129(a)(10)

class, the debtor must ask the court to confirm the plan by way of “cramdown,” i.e. to confirm the plan over the “no” vote of a class.<sup>80 81</sup>

In addition to designating classes of claims, the plan must also identify the classes of claims that are not impaired under the plan and specify the treatment that those impaired classes will receive under the plan.<sup>82</sup> “Impairment” is a term of art crafted by Congress to determine a creditor’s standing in the confirmation phase of the bankruptcy plan proceedings.<sup>83</sup> Generally speaking, if the “legal, equitable and contractual rights” of the creditors of the class are “unaltered,” the class is unimpaired<sup>84</sup> and cannot vote on the plan.<sup>85</sup>

The individual chapter 11 debtor’s obligation to commit an amount equal to five years’ disposable income to payment of creditors is triggered by the objection of a single unsecured creditor.<sup>86</sup> He should therefore avoid an objection by either providing a satisfactory treatment of unsecured creditors generally or by way of separately classifying the potential objector (with a creative excuse other than gerrymandering).<sup>87</sup> Also, the debtor is not obligated to make payments for five years; rather, he must pay an amount equal to five years’ disposable income. Therefore, the plan should take the opportunity to identify all payments to secured creditors so that maximum credit is obtained against the five-year’s requirement.

#### F. Secured Claims

The Model Plan observes the practice of placing each secured claim in a separate class,<sup>88</sup> and offers an example of each of eight recognized treatments of secured claims.<sup>89</sup>

(a.) *Surrender of collateral* results in full satisfaction of the secured claim. Here, the secured creditor is given relief from stay to dispose of collateral and is given a general unsecured claim for any deficiency. In contrast to the chapter 12 and 13 models,<sup>90</sup> there is nothing in the code specifically permitting a chapter 11 debtor’s plan to surrender collateral, although the plan may provide that undersecured claimants may be forced to accept the “indubitable equivalent” (i.e., surrender) of their collateral.<sup>91</sup> Such a plan

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<sup>80</sup> 11 U.S.C. §1129(b)

<sup>81</sup> Consumer bankruptcy attorneys use the term “cramdown” in the Chapter 13 context to mean paying a secured creditor the value of its collateral, with interest, and treating the balance of that creditor’s claim as an unsecured claim. The term is used differently in Chapter 11.

<sup>82</sup> 11 U.S.C. §§1123(a)(2), (a)(3) (2006)

<sup>83</sup> *In re L7J Anaheim Association* 995 F.2d 940,942-43 (9<sup>th</sup> Cir. 1993)

<sup>84</sup> 11 U.S.C. §1124(1)

<sup>85</sup> *See, In re PPI Enterprises U.S., Inc.* 324 F.3d 197 (3d Cir., 2003) (statutory cap of §502(b)(6) on landlord’s claim for breach of lease was not “impairment” of its rights, but part of its rights that it possessed in bankruptcy, so that when debtor’s plan proposed to pay its claim in full, with postpetition interest, it had no right to vote on whether the plan should be confirmed.

<sup>86</sup> 11 U.S.C. §1129(a)(15)

<sup>87</sup> *See, e.g. In re Zaruba* 383 B.R. 254 (Bkrptcy D. Alaska 2008)

<sup>88</sup> *In re Johnston* 21 F3d 323 (9<sup>th</sup> Cir. (Cal) 1994)

<sup>89</sup> Model Plan, Part I

<sup>90</sup> 11 U.S.C. §§ 1325(a)(5)(C) and 1225(a)(5)(C)

<sup>91</sup> 11 U.S.C. § 1129(b)(2)(A)(iii); 7 COLLIER ON BANKRUPTCY ¶¶1129.05[2], 1129.05[2][c] (15th ed. rev’d 2007), citing *Sandy Ridge Dev. Corp. v. Louisiana Nat’l Bank*, 881 F.2d 1346, 1350 (5th Cir. 1989); *In re Pennave Properties Assocs.*, 165 B.R. 793 (E.D. Pa. 1994).

provision may not provide for the partial transfer of collateral (i.e., a “dirt for debt” plan provision).<sup>92</sup>

(b.) *Rights left unaltered*, or “ride through,”<sup>93</sup> is treated much differently in chapter 11 and chapter 13. As a general rule, the chapter 13 plan may simply ignore the lien that is being unaltered because confirmation of the plan reverts property in the debtor “free and clear of any claim or interest of any creditor *provided for by the plan*,” and the secured claim not provided in the plan remains unmodified.<sup>94</sup> But the result is the opposite under chapter 11, where confirmation reverts property in the debtor free and clear of claims against “*property dealt with by the plan*,”<sup>95</sup> Therefore, the lien not provided for in the plan (where the underlying property is dealt with) is effectively stripped-off by confirmation.<sup>96</sup> However this is *not* the rule for personal property, where BAPCPA eliminated the ride-through option.<sup>97</sup> Where the debtor has failed to file a statement of intention with respect to personal property or an unexpired lease<sup>98</sup> or failed to take the action required by the statement,<sup>99</sup> the automatic stay is terminated and the property ceases to become property of the estate.<sup>100</sup>

(c.) *Sale of collateral* with payment of lien from proceeds is used when liens are undisputed.<sup>101</sup>

(d.) *Collateral to be sold free and clear of liens*.<sup>102</sup> The Code allows the plan to provide for the “sale of all or any part of property of the estate, either subject to or free of any lien, or the distribution of all or any part of the property of the estate among those having an interest in such property of the estate”<sup>103</sup> and “overrides nonbankruptcy law restrictions on the distribution of collateral to satisfy a claim secured by the same.”<sup>104</sup> The Model Plan further provides that claimants whose liens are not in bona fide dispute “may credit bid the amount of [their] lien[s] at the sale.” In *Clear Channel Outdoor, Inc. v. Knupfer*, the Bankruptcy Appellate Panel held that the debtor could not sell its property to a senior lienholder (under a “credit bid”) free and clear of the liens of a junior lienholder on the property.<sup>105</sup> Judge Markell offers a scholarly and thorough analysis of §363(f), which makes the opinion worth reading just for that; however, the decision has sparked fears that §363(f) is emasculated, preventing its use wherever the sale price is less than the amount of the junior lienholder’s claim.

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<sup>92</sup> In *Arnold & Baker Farms v. United States ex rel. Farmers Home Admin. (In re Arnold & Baker)*, 85 F.3d 1415 (9th Cir. 1996) the court refused to permit the debtor to value the farm property collateral, and then only transfer an equivalent amount of property to the secured creditor in satisfaction of its claim.

<sup>93</sup> Model Plan, Class 1(b)

<sup>94</sup> 11 U.S.C. §1327(c)

<sup>95</sup> 11 U.S.C. §1141(c)

<sup>96</sup> *In re Regional Building Systems* 254 F.3d 528 (4<sup>th</sup> Cir. (Md) 2001)

<sup>97</sup> *Dumont vs. Ford Motor Company*, 383 B.R. 481 (9<sup>th</sup> Cir., BAP 2008)

<sup>98</sup> 11 U.S.C. §521(a)(2)(A)

<sup>99</sup> 11 U.S.C. §521(a)(2)(B)

<sup>100</sup> 11 U.S.C. §362(h)(1)

<sup>101</sup> Model Plan, Class 1(c)

<sup>102</sup> 103 Model Plan, Class 1(d)

<sup>103</sup> 11 U.S.C. §1123(a)(5)(D)

<sup>104</sup> 7 COLLIER ON BANKRUPTCY ¶1123.01[5][d] (15<sup>th</sup> ed. rev’d 2007), citing *Valente v. Savings Bank of Rockville*, 34 B.R. 362 (D. Conn. 1983).

<sup>105</sup> 391 B.R. 25; 2008 Bankr. LEXIS 1934; 50 Bankr. Ct. Dec. 70

(e.) *Maintain current payments* and spread arrearages over term of plan.<sup>106</sup> A common use of the plan is to cure defaults on long-term secured debt. Chapter 11 cases do not involve a trustee as does a chapter 13 case with the attendant issues of whether the debtor can pay the secured creditor directly and avoid the trustee's 10% fee;<sup>107</sup> instead the issue will be whether the direct payments will be "property distributed under the plan" for purposes of satisfying the "projected disposable income" requirement of §1129(a)(15).

(f.) *Amortize entire debt ("roll up")*.<sup>108</sup> This is frequently used in what is called a "negative amortization" plan, the requirements of which are set forth in *Great Western Bank v. Sierra Woods Group*,<sup>109</sup> where the Ninth Circuit noted that courts considering negative amortization plans have considered accrual or payment of a market rate of interest to be a necessary, but not sufficient, requirement for confirmation.<sup>110</sup> Also noteworthy is *In re Entz-White Lumber & Supply, Inc.*,<sup>111</sup> where the Ninth Circuit held that a debtor need not pay interest at the default rate when the claim was being paid in full at confirmation.<sup>112</sup> In *General Electric Capital Corp. v. Future Media Productions, Inc.*,<sup>113</sup> the Court declined to extend this principle to secured claims paid through sale of the collateral property outside the plan. It remanded the case to the bankruptcy court to consider the viability of the rule adopted by other Circuits, requiring payment at default interest rate unless unenforceable under nonbankruptcy law.

(g.) *Pay value of collateral over time*.<sup>114</sup> This is the "cram down" as understood in the Chapter 13 context,<sup>115</sup> but in chapter 11, there are two important departures from chapter 13 practice: firstly, the retail valuation standard of §506(a)(2) does not apply; secondly, the anti-cramdown provision of §1325(a), which prohibits bifurcation of certain purchase money security claims when the secured creditor is undersecured, does not apply. When the property is the debtor's residence, the plan may not modify a fully-secured or partially-secured claim.<sup>116</sup> While the plan may strip-down a wholly unsecured lien<sup>117</sup> the lien reduction has no *res judicata* effect unless the debtor confirms his plan and receives his discharge.<sup>118</sup>

(h.) *Pay value of collateral on effective date of plan*.<sup>119</sup> This is the concept of "redemption" imported from chapter 7.<sup>120</sup> The secured claim is valued and paid in full.<sup>121</sup>

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<sup>106</sup> Model Plan, Class 1(e); 11 U.S.C. §1123(a)(5)(A),(G); 11 U.S.C. §1123(b)(1)

<sup>107</sup> *In re Lopez*, 372 B.R. 40 (9<sup>th</sup> Cir. BAP 2007)

<sup>108</sup> Model Plan, Class 1(f)

<sup>109</sup> 953 F.2d 1174, 1177-78 (9<sup>th</sup> Cir. 1992)

<sup>110</sup> *Id.* at 1177.

<sup>111</sup> 850 F.2d 1338 (9<sup>th</sup> Cir. 1988)

<sup>112</sup> 850 F.2d at 1339-43.

<sup>113</sup> 536 F.3d 969, 973-74 (9<sup>th</sup> Cir. 2008)(as amended)

<sup>114</sup> Model Plan, Class 1(g)

<sup>115</sup> 11 U.S.C. §1123(b)(5)

<sup>116</sup> 11 U.S.C. §1123(b)(5); *Nobelman vs American Sav. Bank*, 508 U.S. 324, 113 S.Ct. 2106, 124 L.Ed.2d 228 (1993).

<sup>117</sup> *In re Lam* 211 B.R. 36 (9<sup>th</sup> Cir., BAP (Cal.) 1997

<sup>118</sup> *In re 1441 Veteran Street Co.* 144 F.3d 1288 (9<sup>th</sup> Cir. 1998); *In re Akram* 259 B.R. 371 (Bkrcty C.D. Cal. 2001

<sup>119</sup> Model Plan, Class 1(h)

<sup>120</sup> 11 U.S.C. §722

<sup>121</sup> 11 U.S.C. §506(a),(d); 11 U.S.C. §1123(b)(E); Rule 3012

The chapter 11 debtor is not constrained by the retail valuation standard applicable in chapters 7 and 13.<sup>122</sup>

*G. General Unsecured Claims*

The Model Plan contains a “convenience class” as allowed by §1122(b), and one class for general unsecured creditors. But this is not to say that unsecured claims may not be placed in more than two classes. Counsel should consider creating sub-classes of unsecured claims, particularly a class for unliquidated claims.<sup>123</sup> There is no automatic co-debtor stay as in chapter 13<sup>124</sup>, nor the ability to classify guarantee claims separately for full payment as in chapter 13.<sup>125</sup> However, the debtor may wish to attempt to separately classify one or more unsecured claims in order to avoid an objection that will trigger the five years’ disposable income requirement of §1129(a)(15).

*H. The Liquidating Plan and the “Engaged In Business” Requirement*

Chapter 11 may be used by a debtor to liquidate the property of the estate,<sup>126</sup> but he cannot receive a discharge unless he “engages in business” after consummation of the plan. §1141(d)(3). This is generally an evidentiary issue to be resolved at the confirmation hearing. Neither “business” nor “engaged in business” is defined by the Bankruptcy Code. Therefore, one must assume that the drafters meant to include the everyday meaning of the term. For that, one must resort to common-sense or the dictionary.<sup>127</sup> Among the possible choices, it is presumed that the drafters of the Bankruptcy Code intended that definition #3(a) as the type of business referred to, i.e., a “commercial or mercantile activity engaged in as a means of livelihood.”

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<sup>122</sup> 11 U.S.C. §506(a)(2)

<sup>123</sup> *In re Derron M. Simon*, 2008 WL 2953471 (Bkrcty.E.D.Va.) (Medical doctor’s plan allowed to separately classify unliquidated medical malpractice claims by placing in a class different from liquidated general unsecured claims.) *In re Gen. Teamsters, Warehousemen & Helpers Union Local 890*, 225 B.R. 719, 735 (Bankr.N.D.Cal.1998) (a plan does not discriminate unfairly as to classification when there were three classes of unsecured nonpriority creditors: convenience claims, undisputed and liquidated contract claims, and disputed and unliquidated tort claims).

<sup>124</sup> 11 U.S.C. §1301

<sup>125</sup> 11 U.S.C. §1322(b)(1)

<sup>126</sup> 11 U.S.C. §1123(b)(4)

<sup>127</sup> Merriam-Webster Collegiate Dictionary (America OnLine Ed. 1999), definition of “business:” 1 archaic : purposeful activity : BUSYNESS 2 a : ROLE, FUNCTION <how the human mind went about its ~ of learning -- H. A. Overstreet> b : an immediate task or objective : MISSION <what is your ~ here> c : a particular field of endeavor <the best in the ~> 3 a : a usu. commercial or mercantile activity engaged in as a means of livelihood : TRADE, LINE <in the restaurant ~> b : a commercial or sometimes an industrial enterprise; also : such enterprises <the ~ district> c : usu. economic dealings : PATRONAGE <took their ~ elsewhere> 4 : AFFAIR, MATTER <the whole ~ got out of hand> <~ as usual> 5 : CREATION, CONCOCTION 6 : movement or action (as lighting a cigarette) by an actor intended esp. to establish atmosphere, reveal character, or explain a situation -- called also stage business 7 a : personal concern <none of your ~> b : RIGHT <you have no ~ speaking to me that way> 8 a : serious activity requiring time and effort and usu. the avoidance of distractions <got down to ~> <she means ~> b : maximum effort 9 a : a damaging assault b : REBUKE, TONGUE-LASHING c : DOUBLE CROSS 10 : a bowel movement -- used esp. of pets

### **Modification Post-Confirmation**

In a chapter 11 case in which the debtor *not* an individual, only the proponent of the plan or the reorganized debtor can seek to modify the plan after confirmation.<sup>128</sup> The request for post-confirmation modification must be made prior to substantial consummation of the plan.<sup>129</sup> In the chapter 11 case in which the debtor is an individual, rules regarding post-confirmation modification of a plan differ in two important respects: firstly, the Chapter 11's plan individual debtor cases may be modified at any time after confirmation but before completion of payments, whether or not the plan has been substantially consummated; secondly, the plan may be modified upon request of the debtor, the trustee, the U.S. Trustee or the holder of an allowed unsecured claim (but not a secured creditor) to increase or reduce the amount of payments, extend or reduce the time period for such payment, or 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 made other than under the plan.<sup>130</sup>

Modification may require additional disclosures. Bankruptcy Rule 3015(g) requires a motion to modify on not less than twenty days' notice to all creditors. Bankruptcy Rule 3019, dealing with pre-confirmation modification, permits an accepted plan to be modified and deemed accepted if the modification does not adversely affect the treatment of the accepting creditor. There is no corresponding rule for post-confirmation modification.

There are no other limitations on how a plan can be modified, and there is no required showing that must be made to justify a modification. The only substantive requirements are that the plan as modified must conform to the requirements of §1122 (classification) and §1123 (plan provisions), and be confirmable under §1129.<sup>131</sup>

Debtors may fear that there will be a belligerent creditor who repeatedly petitions the bankruptcy court to modify the amount and duration of payments every time there is a significant increase in the debtor's income, keeping the plan payments open until creditors are paid in full. §1127(e) provides no guidance on the issue of the duration of an individual debtor's chapter 11 plan. Collier notes that we should look to §1229 and §1329 for guidance,<sup>132</sup> but the problem is that those two code sections expressly limit any extension of plan payments to five years after the first payment under the originally confirmed plan. Congress, though either intent or neglect, failed to include such a limitation in §1127(e).

Some are alarmed that these provisions may allow peonage, but others feel it is unlikely that they will be challenged as such unless the debtor is put into chapter 11 involuntarily (through an involuntary petition or conversion) and the court confirms a creditor's plan over the debtor's dissent.<sup>133</sup> Weapons in the debtor's arsenal to prevent this from happening include:

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<sup>128</sup> 11 U.S.C. §1127(b). However, a liquidating trustee may qualify as a representative of the reorganized debtor. *In re US Repeating Arms Co.* 98 BR 138 (Bkrtcy D. Conn. 1989).

<sup>129</sup> *Id.*

<sup>130</sup> 11 U.S.C. §1127(e)

<sup>131</sup> *See*, 11 U.S.C. §1127(b) and (f). *See*, e.g., *In re A.J. Mackay Co.*, 50 B.R. 756, 95 (D. Utah, 1985).

<sup>132</sup> 7 COLLIER ON BANKRUPTCY ¶¶ 1127.04 [2] and 1127. LH [2] (15<sup>th</sup> ed. rev'd 2007)

<sup>133</sup> Klee, *The Bankruptcy Abuse Protection and Consumer Protection Act of 2005-Business Bankruptcy Amendments* SLO 51 ABA-305(2005).

- Preserving the exclusivity period<sup>134</sup> in order to prevent a creditor’s plan being filed (300 days in the small business case and 120 days in chapter 11 cases generally).
- Confirming a plan that pays five years’ disposable income over the shortest period of time. There is no temporal commitment period in a chapter 11 proceeding, i.e. the debtor must simply commit to pay five years’ worth of “projected disposable income” to his creditors, which could be paid in one year or ten years. The debtor should try to propose a very short plan and possibly escape the risk that §1127(e) will be used to string him out.
- Calculating projected disposable income to conservatively state income over the ensuing five years and meticulously detailing all possible expenses.
- Refusing to concede that the plan may be extended indefinitely; it is submitted that a more reasonable reading of §1129(a)(15) is that the five-year projected disposable income requirement is intended to be a cap as in chapter 13, and is not expressly stated simply because of sloppy drafting. The “whichever is longer” limitation is simply intended to prevent a debtor from shortening the period of projected disposable income to less than five years.
- Arguing the unconstitutionality of §1129(a)(15).<sup>135</sup>

Some fear that creditors will thwart the debtor’s exclusivity period by moving to modify his plan immediately after confirmation. But this is unfounded because modification most likely requires a showing of changed circumstances.<sup>136</sup> As cautioned by *Norton*, whether or not a request of the bankruptcy court for post-confirmation relief is construed as a request to ‘modify’ the confirmed plan has significant ramifications. If the requested relief is deemed to constitute a §1127 modification,’ the relief should not be granted unless the requirements of that section are satisfied. On the other hand, if the requested relief is construed to constitute something other than a §1127 modification,’ the court may grant the relief even though the requirements of Code §1127 are not satisfied. Courts should be wary, however, of calling a ‘modification’ by another name in order to allow the remedy without meeting the requirements. Likewise, a court should not use Code §105 to circumvent the requirements of Code §1127.”<sup>137</sup>

### **The Nonpayment Discharge**

The Code allows the court to grant the debtor a discharge if he does not complete payments. This discharge differs from the Chapter 13 model in two respects: firstly, it does not require as a condition to the discharge that “the debtor’s failure to complete [payments under the plan] is due to circumstances for which the debtor should not justly be held accountable.”<sup>138</sup> As such, there is no express statutory standard for the noncompletion discharge other than the court’s discretion. As explained by Collier, “it appears, however, that the omission of Chapter 13’s accountability requirements from the

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<sup>134</sup> See, Who may File A Plan, *supra*.

<sup>135</sup> *The Shackles of an Individual Chapter 11 Debtor’s Servitude—Where’s the Key?*—Cal. Bankr. J.—(2008)

<sup>136</sup> *In re Richardson*, 192 B.R. 224 (Bkrtcy. S.D. Cal. 1996), citing *In re Anderson* 31 F3d 355 (9<sup>th</sup> Cir. (Wash) 1994)

<sup>137</sup> 6 *Norton Bankr. L. & Prac.* 3d §111:2

<sup>138</sup> 11 U.S.C. §1328(b)(1)

Chapter 11 provision should be interpreted to mean that accountability should not enter into the court's determination of whether to grant the noncompletion discharge; the only consideration other than payment of at least liquidation value is whether plan modification is practicable.<sup>139</sup>

### **Post-Confirmation Administration**

It is imperative that the issue of the proper tax treatment of the debtor's post-petition income, when used to pay claims, is properly addressed. Presumably, the debtor set up the accounting for the estate as a separate entity at the outset of the case<sup>140</sup> and it would appear that the procedure implemented upon the filing of the petition would simply continue post-confirmation

Debtor's counsel needs to be particularly sensitive to the tax implications of chapter 11, particularly because the changes to the Code impact how the individual debtor and the debtor's bankruptcy estate are each taxed under IRC §1398. Following the filing of an individual chapter 11 case the individual and the individual's estate are treated as separate taxpayers, filing separate returns on Forms 1040 and 1041, respectively. Given the broad definition of property of the estate under §1115, income that would otherwise be taxable to the chapter 11 debtor is taxable to the estate. Such income may include all wages and other income from the performance of services; as well as all rents, dividends and other income from property acquired after the filing. Although not without its faults, Internal Revenue Service Notice 2206-83 provides guidance to individual chapter 11 debtors and their estates regarding the tax treatment of post petition income.<sup>141</sup> This treatment of the debtor's income will continue after the confirmation until the case is closed as a result of the enactment of §1115.

- The notice sets forth the rules for preparing and filing the income tax returns of the estate, if required under IRC §6012.
- Where the debtor in possession has been compensated by the estate to manage or operate his trade or business, the debtor should report such payments as miscellaneous income in his individual tax return,<sup>142</sup> and amounts paid by the estate to the debtor in possession, which qualify as administrative expenses will generally be deductible by the estate.<sup>143</sup>
- Within a reasonable time after the commencement of the chapter 11 case, the debtor should provide notification of the bankruptcy estate's EIN to persons that are required to file information returns with respect to the bankruptcy estate's gross income, gross proceeds or other types of reportable payments.<sup>144</sup>
- The debtor should not provide the estate's EIN to his employer or other person filing form W-2 with respect to the debtor's wages or other compensation. The debtor is not required to file a new form W-4 with his employer to adjust his withholding allowances.

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<sup>139</sup> 8 COLLIER ON BANKRUPTCY ¶1141.05[2][b] at p. 1141-24 (15th ed. rev'd 2007).

<sup>140</sup> The procedures implemented at the beginning of the case should continue post-confirmation where the estate remains open.

<sup>141</sup> Martin, *supra*

<sup>142</sup> 26 U.S.C. §61(a)

<sup>143</sup> 26 U.S.C. §1398(h)(1)

<sup>144</sup> 26 U.S.C. §619(a)(2)

The debtor must allocate his W-2 income between himself and the estate in accordance with rules set forth in Notice 2006-83 and claim a credit on the debtor's income tax return.<sup>145</sup> The debtor must attach a statement to his income tax returns stating that he filed a chapter 11 bankruptcy case, reflecting the allocations of income and withheld income tax and describing the method used to allocate the income and withheld tax between the debtor and the estate. Notice 2006-83 offers a model statement to be used by debtors complying with the requirements of the notice.<sup>146</sup>

*Plan payments and post-confirmation reporting requirements.*

Upon the effective date of the plan, payments generally commence. Any delay in payment could constitute a default under the plan and be grounds for a motion to convert the case to chapter 7.<sup>147</sup> The debtor must continue to file monthly operating reports with the U.S. Trustee's office after the plan confirmation in a format that is usually much shorter than the form of the report filed prior to plan confirmation. Upon completion of the plan payments, or such other period of time that the court may allow, the debtor will file a motion for final decree requesting that the court grant the discharge and request that the case be closed.

### **Disclosure Statement Approval**

We discuss the disclosure statement after the plan because it is generally prepared after the plan is drafted. The extent of the disclosures depends on the complexity of the case. §1125(a) defines "adequate information" as "information of a kind, and in sufficient detail, as far as is reasonably practicable in light of the nature and history of the debtor and the condition of the debtor's books and records..." BAPCPA added that "in determining whether a disclosure statement provides adequate information, the court shall consider the complexity of the case, the benefit of additional information to creditors and other parties in interest, and the cost of providing additional information..."<sup>148</sup> *Id.* Therefore, the 25-page Official Form 25(B) should not be necessary in many individual cases. The Model Disclosure Statement focuses on the liquidation analysis<sup>148</sup> to allow creditors and the court to determine whether the plan is in the best interests of creditors,<sup>149</sup> it provides other basic financial information so that the feasibility of the plan can be assessed.<sup>150</sup>

While some courts provide long lists of various categories of information to be included in a disclosure statement, Collier explains that such disclosure statements are found in cases involving medium to large reorganizations, often where securities are issued in connection with the plan, and suggests that, for a small business like that of most individual debtors, much less information is necessary.<sup>151</sup>

The disclosure statement is generally approved by the court before it is transmitted to creditors with the plan. 11 U.S.C. §1125(b); Fed. R. Bankr. P. 2002(b) requires that creditors receive twenty five days' notice of the time to object to the

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<sup>145</sup> 26 U.S.C. §31(a)

<sup>146</sup> Notice 2006-83 §6.04. Notice 2006-83, 2006-40I.R.B 596, 2006-2 C.B. 596 2006W.L. 2663467(IRS NOT)

<sup>147</sup> 11 U.S.C. 1112(b)(4)(n); Model Plan 10(d)

<sup>148</sup> Model Disclosure Statement, page 3

<sup>149</sup> 11 U.S.C. §1129(a)(9)

<sup>150</sup> 11 U.S.C. §1129(a)(11)

<sup>151</sup> 7 COLLIER ON BANKRUPTCY ¶1125.02[2] at p. 1125-12 (15<sup>th</sup> ed. rev'd 2007).

disclosure statement, so the hearing is usually set out at least thirty two days so objections can be raised a week in advance of the hearing . The Model Disclosure Statement assumes that the individual debtor is a small business debtor, in which case the court conditionally approves the disclosure statement subject to final approval at the time of the confirmation hearing.<sup>152</sup> This procedure should be used to save money as well as time, because it avoids the time lag of two noticed hearings and appearances. Local practice varies on the procedure, and counsel should ascertain the inclination of the court to utilize this procedure. If the court is not in a position to review the disclosure statement and grant preliminary approval, it may be quicker to follow the traditional procedure of noticing it for hearing separately.

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<sup>152</sup> 11 U.S.C. §1125(f)

**Checklist for Assessing Prospects of Confirming Chapter 11 Plan**

| <b>Issue</b>                                    | <b>Requirement</b>  | √ |
|---|---|---|
| Cost of proceeding:                             | Professional fees for attorneys and accountants, when combined with UST Quarterly Fees ranging from \$325 to \$30,000 per quarter. UST fees must be paid during case, other fees by arrangement.                              |   |
| Is he a small business debtor?                  | He is a small business case if total debt is no more than \$2,190,000 and there is no creditor's committee. §101(51D) plans must be filed within 300 days.  |   |
| Can taxes and priority claims be paid?          | §1129(a)(9) requires regular installment payments may not extend beyond 5 years from the date of the order for relief. Treatment must be at least as favorable as most favored non-priority unsecured claims. §1129(a)(9)(C). |   |
| Does he have domestic support obligations?      | Obligations must be current in order to confirm plan. §1129(a)(14).   |   |
| Can he obtain votes to confirm plan?            | Majority in number and 2/3rds in dollar amount in each impaired class, unless proceeding by way of cramdown, in which case must have the consent of at least one impaired class.  |   |
| Treatment of secured claims?                    | Debtor must provide each secured claim one of the eight recognized treatments.  |   |
| Treatment of unsecured claims?                  | (1) Debtor's projected disposable income as defined in §1325(b)(2) for five years must fund plan, and (2) a non-accepting class must receive not less than the amount it would receive in a Chapter 7 liquidation.            |   |
| Will the debtor receive an effective discharge? | Scope of discharge is the same as for a Chapter 7 debtor, but in a liquidating plan the debtor must engage in business following confirmation.  |   |

United States Bankruptcy Court  
Northern District of California

In re:

Case No.

**PLAN OF REORGANIZATION (Date)**

**INTRODUCTION**

This plan of reorganization (the Plan) provides for the Restructuring of the debts of \_\_\_\_\_ (name of debtor). If confirmed, the Plan will bind all creditors provided for in the Plan, whether or not they file a proof of claim or accept the Plan, and whether or not their claims are allowed.

All creditors should refer to Parts 1 - 5 of the Plan for information regarding the precise treatment of their claims. A disclosure statement that provides additional information is being circulated with the Plan. The disclosure statement is descriptive and explanatory only; the language used in the Plan is binding. **Your rights may be affected. You should read these papers carefully and discuss them with your attorney, if you have one.**

**PART 1: SECURED CREDITORS**

**Class 1(a). Collateral to be Surrendered.**

Debtor will surrender the following collateral on the Effective Date of the Plan. The confirmation order will constitute an order granting relief from stay permitting the secured creditor(s) to possess and dispose of their collateral. Any secured claim is deemed satisfied in full through surrender of the collateral. Any deficiency claim is a general unsecured claim. This class is not impaired and is not entitled to vote on confirmation of the Plan.

| Name of Creditor | Description of Collateral |
|------------------|---------------------------|
|                  |                           |
|                  |                           |

**Class 1(b). Rights Unaltered.**

Debtor will leave unaltered the creditor's contractual, legal, and equitable rights with respect to the following collateral. This class is not impaired and is not entitled to vote on confirmation of the Plan.

| Name of Creditor | Description of Collateral |
|------------------|---------------------------|
|                  |                           |
|                  |                           |

**Class 1(c). Collateral to be Sold.**

Debtor will sell the following collateral by \_\_\_\_\_ (date), paying all claims secured by the collateral in full with interest at the closing of the sale.

| Name of Creditor | Description of Collateral | Value of Collateral | Estimated Amount Due |
|------------------|---------------------------|---------------------|----------------------|
|                  |                           |                     |                      |
|                  |                           |                     |                      |

[Debtor will make the following monthly payments pending the closing of the sale].

| Name of Creditor | Monthly Payment |
|------------------|-----------------|
|                  |                 |
|                  |                 |

[The payments will be due the \_\_\_\_\_ day of the month, starting \_\_\_\_\_ (month & year).

[Debtor will make no payments pending the closing of the sale.]

Creditors in this class may not possess or dispose of their collateral so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10. This class is impaired and is entitled to vote on confirmation of the Plan. For instructions re voting see the Disclosure Statement.

**Class 1(d). Collateral to be Sold Free and Clear of Liens.**

Debtor will sell the following collateral by \_\_\_\_\_ (date). The collateral will be sold free and clear of liens. Upon closing, the proceeds of sale will be distributed to the holders of undisputed liens in order of priority, and disputed liens will attach to the proceeds of

sale, which will be held until disputes regarding the validity and/or amounts of liens are resolved by the court.

| Name of Creditor | Description of Collateral | Value of Collateral | Amount Claimed Due | Amount Disputed |
|------------------|---------------------------|---------------------|--------------------|-----------------|
|                  |                           |                     |                    |                 |
|                  |                           |                     |                    |                 |

[Debtor will make the following monthly payments pending the closing of the sale.]

| Name of Creditor | Monthly Payment |
|------------------|-----------------|
|                  |                 |
|                  |                 |

The payment will be due the \_\_\_\_\_ day of the month, starting \_\_\_\_\_ (month & year).

[Debtor will make no payment pending the closing of the sale.]

All lienholders will be afforded at least 28 days notice of the hearing on the sale. Unless the court orders otherwise, a lienholder whose lien is not in bona fide dispute may credit bid the amount of its lien at the sale. At the hearing on the sale, the court will schedule further such proceedings as are necessary to resolve disputes regarding the amount due each lienholder.

Creditors in this class may not possess or dispose of their collateral so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10. This class is impaired and is entitled to vote on confirmation of the Plan. For instructions re voting see the Disclosure Statement.

**Class 1(e). Continue Regular Monthly Payment Debtor and Pay Arrears Over Time.**

Debtor will pay the entire amount due by making all post-confirmation regular monthly payments, and by paying all pre-confirmation arrears (including attorneys fees and late charges) with interest in \_\_\_\_\_ equal monthly payments. All payments will be due the \_\_\_\_\_ day of the month, starting \_\_\_\_\_ (month & year).

| Name of Creditor | Description of Collateral | Regular Monthly Payment | Estimated Arrears | Rate on Arrears | Monthly Payment on Arrears |
|------------------|---------------------------|-------------------------|-------------------|-----------------|----------------------------|
|                  |                           |                         |                   |                 |                            |

|  |  |  |  |  |  |
|--|--|--|--|--|--|
|  |  |  |  |  |  |
|  |  |  |  |  |  |

Creditors in this class may not possess or dispose of their collateral so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10. This class is impaired and is entitled to vote on confirmation of the Plan. For instructions re voting see the Disclosure Statement.

Class 1(f). Pay Amount Due in Full over Time. Debtor will pay the entire amount due with interest through \_\_\_\_\_ equal monthly payments. Payments will be due the \_\_\_\_\_ day of the month, starting \_\_\_\_\_ (month & year).

| Name of Creditor | Description of Collateral | Amount Due | Interest Rate | Monthly Payment |
|------------------|---------------------------|------------|---------------|-----------------|
|                  |                           |            |               |                 |
|                  |                           |            |               |                 |

Creditors in this class may not possess or dispose of their collateral so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10. This class is impaired and is entitled to vote on confirmation of the Plan. For instructions re voting see the Disclosure Statement.

**Class 1(g). Pay Value of Collateral over Time.**

Debtor will pay the amount of the underlying debt that is equal to the value of the collateral. Debtor will pay that amount with interest from the Effective Date of the Plan through \_\_\_\_\_ equal monthly payments. Payments will be due on the \_\_\_\_\_ day of the month, starting \_\_\_\_\_ (month & year).

| Name of Creditor | Description of Property | Amount Due | Estimated Value of Property | Interest Rate | Monthly Payment |
|------------------|-------------------------|------------|-----------------------------|---------------|-----------------|
|                  |                         |            |                             |               |                 |
|                  |                         |            |                             |               |                 |

If a lienholder disputes the value of the collateral stated above by Debtor, such lienholder must timely file an objection to confirmation, or the value stated by Debtor will be determined to be the value of the collateral. Such objection shall be accompanied by competent evidence of value, which need not include an appraisal. If the value of the collateral is disputed, the court, after consultation with the parties, will schedule a hearing for determining value.

Creditors in this class may not possess or dispose of their collateral so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10. This class is impaired and is entitled to vote on confirmation of the Plan. For instructions re voting see the Disclosure Statement.

**Class 1(h). Pay Value of Collateral on Effective Date of Plan.**

Debtor will pay the amount of the underlying debt that is equal to the value of the collateral in cash on the Effective Date of the Plan. If a lienholder disputes the value of the collateral stated above by Debtor, such lienholder must timely file an objection to confirmation, or the value stated by Debtor will be determined to be the value of the collateral. Such objection shall be accompanied by competent evidence of value, but need not include an appraisal. If the value of the collateral is disputed, the court, after consultation with the parties, will schedule a hearing for determining value.

Creditors in this class may not possess or dispose of their collateral so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10. This class is impaired and is entitled to vote on confirmation of the Plan. For instructions re voting see the Disclosure Statement.

| Name of Creditor | Description of Collateral | Amount Due | Interest Rate | Monthly Payment |
|------------------|---------------------------|------------|---------------|-----------------|
|                  |                           |            |               |                 |
|                  |                           |            |               |                 |

**Part 2: GENERAL UNSECURED CREDITORS**

**Class 2(a). Small Claims.**

This class includes any creditor whose allowed claim is \$\_\_\_\_\_ or less, and any creditor whose allowed claim is

larger than \$\_\_\_\_\_ but agrees to reduce its claim to \$\_\_\_\_\_. Each member of this class shall receive on the Effective Date of the Plan a single payment equal to \_\_\_\_\_ percent of that creditor's allowed claim.

| Name of Creditor | Amount of Claim | Is Claim Disputed? | Amount to be Paid |
|------------------|-----------------|--------------------|-------------------|
|                  |                 |                    |                   |
|                  |                 |                    |                   |
|                  |                 |                    |                   |

[If more than 10 creditors, list in Appendix A, and show in this space "See Appendix A."]

Creditors in this class may not take any collection action against Debtor so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10. This class is impaired and is entitled to vote on confirmation of the Plan. For instructions re voting and objections to confirmation see the Disclosure Statement.

**Class 2(b). Other General Unsecured Claims.** Every other general unsecured creditor (including claims from rejected executory contracts) shall be paid \_\_\_\_\_ percent of its allowed claim in \_\_\_\_\_ equal [monthly] [quarterly] installments. Payments will be due on the \_\_\_\_\_ day of the [month] [quarter], starting \_\_\_\_\_ (month & year).

| Names of Creditor | Amount of Claim | Is Claim Disputed? | Amount to be Paid | [Monthly] [Quarterly] Payment |
|-------------------|-----------------|--------------------|-------------------|-------------------------------|
|                   |                 |                    |                   |                               |
|                   |                 |                    |                   |                               |

|  |  |  |  |  |
|--|--|--|--|--|
|  |  |  |  |  |
|--|--|--|--|--|

[If more than 10 creditors, list in Appendix A, and show in this space "See Appendix A."]

Creditors in this class may not take any collection action against Debtor so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10. This class is impaired and is entitled to vote on confirmation of the

Plan. For instructions re voting and objections to confirmation see the Disclosure Statement.

**PART 3: PRIORITY CLAIMS AND EXPENSES OF ADMINISTRATION**

(a) Professional Fees. Professional fees may be paid only upon application and approval by the Bankruptcy Court. Holders of administrative claims for unpaid professional fees are not entitled to vote on confirmation of the Plan.

(1) Debtor will pay the following professional fees in full on the Effective Date, or upon approval by the court, whichever is later.

| Name and Role of Professional | Estimated Amount |
|-------------------------------|------------------|
|                               |                  |
|                               |                  |

(2) The following professionals have agreed to accept payment in full over time without interest as follows. Payments will be made (monthly/quarterly), due on the \_\_\_\_\_ day of the (month/quarter), starting \_\_\_\_\_ (month & year).

| Name and Role of Professional | Estimated Amount of Claim | Payment Amount | Number of Payments |
|-------------------------------|---------------------------|----------------|--------------------|
|                               |                           |                |                    |
|                               |                           |                |                    |

Administrative priority creditors may not take any collection against Debtor so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10.

(b) Other Administrative Claims. Debtor will pay other claim entitled to priority under section 503(b) in full on the Effective Date. Ordinary course of business payments will be made when due. Holders of administrative claims are not entitled to vote on confirmation of the Plan.

| Name of Creditor (other than ordinary course) | Estimated Amount of Claim |
|---|---------------------------|
|   |                           |
|   |                           |

Administrative priority creditors may not take any collection action against Debtor so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10.

(c) Tax Claims. Debtor will pay claims entitled to priority under section 507(a) (8) in full over time with interest in equal amortizing payments in accordance with section 511 of the Bankruptcy Code. Payments will be made (monthly/quarterly), due on the \_\_\_\_\_ day of the (month/quarter), starting \_\_\_\_\_ (month & year). Holders of priority tax claims are not entitled to vote on confirmation of the Plan.

| Name of Creditor | Estimated Amount of Claim | Statutory Interest Rate | Payment Amount | Number of Payments |
|------------------|---------------------------|-------------------------|----------------|--------------------|
|                  |                           |                         |                |                    |
|                  |                           |                         |                |                    |

Priority tax creditors may not take any collection action against Debtor so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10.

(d) Priority Wage Claims. Debtor proposes to pay claims entitled to priority under section 507(a) (4) in full over time with interest. Payments will be made (monthly/quarterly), due on the \_\_\_\_\_ day of the (month/quarter), starting \_\_\_\_\_ (month & year).

| Name of Creditor | Estimated Amount of Claim | Interest Rate | Payment Amount | Number of Payments |
|------------------|---------------------------|---------------|----------------|--------------------|
|                  |                           |               |                |                    |
|                  |                           |               |                |                    |

This class is impaired and is entitled to vote on confirmation of the Plan. For instructions re voting see the Disclosure Statement. If this class does not vote to accept the Plan, the claims will be paid in full on the Effective Date. Creditors in this class may not take any collection action against Debtor so long as Debtor is not in

Material Default in performing its obligations under the Plan. Material Default is defined in Part 10.

(e) Employee Benefit Plans. Debtor proposes to pay claims entitled to priority under section 507(a)(5) in full over time with interest. Payments will be made (monthly/quarterly), due on the \_\_\_\_\_ day of the (month/quarter) starting \_\_\_\_\_ (month & year).

| Name of Creditor | Estimated Amount of Claim | Interest Rate | Payment Amount | Number of Payments |
|------------------|---------------------------|---------------|----------------|--------------------|
|                  |                           |               |                |                    |
|                  |                           |               |                |                    |

This class is impaired and is entitled to vote on confirmation of the Plan. For instructions re voting see the Disclosure Statement. If this class does not vote to accept the Plan, the claims will be paid in full on the Effective Date. Creditors in this class may not take any collection action against Debtor so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10.

(f) Grain and Fish Storage. Debtor proposes to pay claims entitled to priority under section 507(a)(6) in full over time with interest. Payments will be made (monthly/quarterly), due on the \_\_\_\_\_ day of the (month/quarter), starting \_\_\_\_\_ (month & year).

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| Name of Creditor | Estimated Amount of Claim | Interest Rate | Payment Amount | Number of Payments |
|------------------|---------------------------|---------------|----------------|--------------------|
|                  |                           |               |                |                    |
|                  |                           |               |                |                    |

This class is impaired and is entitled to vote on confirmation of the Plan. For instructions re voting see the Disclosure Statement. If this class does not vote to accept the Plan, the claims will be paid in full on the Effective Date. Creditors in this class may not take any collection action against Debtor so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10.

(g) Customer Deposit Claims. Debtor proposes to pay claims entitled to priority under section 507(a)(7) in full over time with interest. Payments will be made (monthly/quarterly), due on the \_\_\_\_\_ day of the (month/quarter), starting \_\_\_\_\_ (month & year).

| Name of Creditor | Estimated Amount of Claim | Interest Rate | Payment Amount | Number of Payments |
|------------------|---------------------------|---------------|----------------|--------------------|
|                  |                           |               |                |                    |
|                  |                           |               |                |                    |

This class is impaired and is entitled to vote on confirmation of the Plan. For instructions re voting see the Disclosure Statement. If this class does not vote to accept the Plan, the claims will be paid in full on the Effective Date. Creditors in this class may not take any collection action against Debtor so long as Debtor is not in Material Default in performing its obligations under the Plan. Material Default is defined in Part 10.

**PART 4: EXECUTORY CONTRACTS AND UNEXPIRED LEASES**

(a) Executory Contracts/Leases Assumed. The Debtor assumes the following executory contracts and/or unexpired leases effective upon the date of the entry of the order confirming this Plan and shall perform all obligations thereunder, both pre-confirmation and post-confirmation. Any pre-confirmation arrearage will be paid on the Effective Date, unless the parties agree otherwise, or the court finds that

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a proposed payment schedule provides adequate assurance of future performance. Post-confirmation obligations will be paid as they come due.

| Name of Lessor/Counterparty | Property Address or Description | Lease/Contract Arrears as of Effective Date |
|-----------------------------|---------------------------------|---|
|                             |                                 |   |
|                             |                                 |   |

(b) Executory Contracts/Leases Rejected. The Debtor rejects the following executory contracts and/or unexpired leases and surrenders any interest in property securing these executory contracts and/or unexpired leases. The Debtor waives the protection of the automatic stay and allows the affected creditor to obtain possession and dispose of its collateral, without further order of the court. Upon the date of the entry of the order confirming this Plan, the Debtor will be conclusively deemed to have

rejected all executory contracts and/or unexpired leases not previously assumed or listed in paragraph (a) above. A proof of claim arising from the rejection of an executory contract or unexpired lease must be filed not later than sixty (60) days after the date of the order confirming this Plan. Claims arising from rejection of executory contracts shall be included in Class 2 (general unsecured claims).

| Name of Creditor/Lessor | Property Address or Description |
|-------------------------|---------------------------------|
|                         |                                 |
|                         |                                 |

**PART 5: EQUITY INTERESTS**

[Shareholders] [Partners] [Members] of the Debtor shall retain their interests with their legal and equitable rights unaltered by the Plan. This class is not impaired and not entitled to vote on confirmation of the Plan.

**PART 6: DISPUTED CLAIMS**

(a) Distribution on Allowed Claims. Debtor will make distributions only on account of undisputed claims. If a creditor has filed a proof of claim, that claim is considered disputed only if a party-in-interest has filed an objection to the claim. If a party has not filed a proof of

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 claim, but its claim is listed in Debtor's schedules and is not scheduled as disputed, contingent, or unliquidated, such claim is considered disputed only if a party-in-interest has filed an objection to the claim. Listing a claim as disputed in the Plan, without filing an objection to the claim, does not make the claim a disputed claim.

(b) Delayed Distribution on Disputed Claims. Debtor will make no distribution on account of a claim to which an objection has been filed by a party-in-interest, until such claim is allowed by a final order. Instead, Debtor will establish and hold an appropriate reserve pending determination of the disputed claims, and will pay the appropriate amount to claimant once the dispute is resolved.

(c) Settlement of Disputed Claims. The Debtor is authorized to settle and compromise a disputed claim [without a court approval] [with court approval and compliance with Rule 9019 of the Federal Rules of Bankruptcy Procedure].

**PART 7: LAWSUITS RESERVED**

(a) Debtor retains, and may seek to enforce, the following claims against parties who are or were creditors of the bankruptcy estate, or officers, agents, and other parties related to creditors of the estate.

| Party | Nature of Action |
|-------|------------------|
|       |                  |
|       |                  |

(b) Debtor retains, and may seek to enforce, all claims against parties other than creditors of the estate, or officers, agents, or other parties related to creditors of the estate.

**PART 8: MEANS OF EXECUTION**

The Plan will be funded through [monthly] [quarterly] payments from future income. [Insert any other provision for implementing the Plan, such as the sale of property.]

**PART 9: DISCHARGE AND OTHER EFFECTS OF CONFIRMATION**

(a) Discharge. Confirmation of the Plan discharges Debtor from all debts provided for in the Plan, whether or not the creditor files a proof of claim, whether or not the creditor

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accepts the Plan, and whether or not the creditor's claim is allowed, except as provided in section 1141 of the Bankruptcy Code.

(b) Vesting of Property. On the [Effective Date] [the entry of discharge], all property of the estate will vest in the reorganized Debtor pursuant to § 1141(b) of the Code free and clear of all claims and interests except as provided in this Plan, [subject to revesting upon conversion to Chapter 7 as provided in Part 10(f) below, provided that the vesting of said property will be without prejudice and will not act as a bar to a post-confirmation motion to convert this case to one under Chapter 7 by any party-in-interest on any appropriate grounds. The granting of such motion will re-vest all of the Debtor's property not already administered into the Chapter 7 estate.]

(c) Plan Creates New Obligations. Except as provided in Part 10, paragraph (e), the obligations to creditors that Debtor undertakes in the confirmed Plan replace those obligations to creditors that existed prior to the Effective Date of the Plan. Debtor's obligations under the confirmed Plan constitute binding contractual promises that, if not

satisfied through performance of the Plan, create a basis for an action for breach of contract under California law. To the extent a creditor retains a lien under the Plan, that creditor retains all rights provided by such lien under applicable non-Bankruptcy law.

**PART 10: REMEDIES IF DEBTOR DEFAULTS IN PERFORMING THE PLAN**

(a) Automatic Stay Vacated: The automatic stay of section 362(a) of the Bankruptcy Code terminates as of the Effective Date of the Plan.

(b) Creditor Action Restrained. The confirmed Plan is binding on every creditor whose claims are provided for in the Plan. Therefore, notwithstanding paragraph (a) above, a creditor may not take any action to enforce either the pre-confirmation obligation or the obligation due under the Plan, so long as Debtor is not in Material Default under the Plan, as defined in paragraph (c) below.

(c) Material Default Defined. If Debtor fails to make any payment required under the Plan, or to perform any other obligation required under the Plan, for more than 10 calendar days after the time specified in the Plan for such payment or other performance, the affected creditor may serve upon Debtor and Debtor's attorney (if any) a written notice of Debtor's default. If Debtor fails within 20 calendar days after the date of service of the notice of

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default either: (i) to cure the default; or (ii) to obtain from the court an extension of time to cure the default, or a determination that no default occurred, then Debtor is in Material Default under the Plan.

(d) Remedies Upon Material Default. Upon Material Default, an affected creditor may:

(i) Take any actions permitted under applicable non-Bankruptcy law to enforce the obligation due the affected creditor under the Plan, and may accelerate the time for performance of all payments and other performance due to the creditor over the course of the Plan and not yet performed at the time of the Material Default; or

(ii) File and serve a motion to convert the case to one under Chapter 7.

(e) Claim not Affected by Plan. Upon confirmation of the Plan, any creditor whose claims are left unimpaired under the Plan may, notwithstanding paragraphs (a), (c), and (d) above, immediately exercise all of its contractual, legal, and equitable rights, except right based on default of the type that need not be cured under section 1124(2)(A) and (D).

(f) Effect of Conversion to Chapter 7. If the case is at any time converted to one under Chapter 7:

(i) All property of the Debtor as of the date of conversion, whether acquired pre-confirmation or post-confirmation, shall vest in the Chapter 7 bankruptcy estate; and

(ii) All creditors, whether their claims arose pre-confirmation or post-confirmation, are prohibited from taking action against the Chapter 7 bankruptcy estate or property of the estate by section 362 of the Bankruptcy Code.

(g) Retention of Jurisdiction. This court shall retain jurisdiction over proceedings: (i) to determine whether Debtor has defaulted in performance of any Plan obligation; (ii) to determine whether the time for performing any Plan obligation should be extended; (iii) to determine whether the case should be converted to one under Chapter 7 (and proceedings following any such conversion); (iv) to determine whether Debtor is in Material Default; and (v) any enforcement action permitted under paragraph (d)(1) of Part 10 above.

#### **PART 11: GENERAL PROVISIONS**

(a) Effective Date of Plan. The Effective Date of the Plan is the eleventh business day following the date of the entry of the order of confirmation, if no notice of appeal from that order has been filed. If a notice of appeal has been

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Filed, the Plan proponent may waive the finality requirement and put the Plan into effect, unless the order confirming the Plan has been stayed. If a stay of the confirmation order has been issued, the Effective Date will be the first business day after that date on which no stay of the confirmation order is in effect, provided that the confirmation order has not been vacated.

(b) Cramdown. Pursuant to section 1129(b) of the Bankruptcy Code, Debtor reserves the right to seek confirmation of the Plan notwithstanding the rejection of the Plan by one or more classes of creditors.

(c) Severability. If any provision in the Plan is determined to be unenforceable, the determination will in no way limit or affect the enforceability and operative effect of any other provision of the Plan.

(d) Binding Effect. The rights and obligations of any entity names or referred to in the Plan will be binding upon, and will inure to the benefit of the successors or assigns of such entity.

(e) Captions. The heading contained in the Plan are for convenience of reference only and do not affect the meaning or interpretation of the Plan.

(f) Controlling Effect. Unless a rule of law or procedure is supplied by federal law (including the Code or the Federal Rules of Bankruptcy Procedure), the laws of the State of California govern the Plan and any agreements, documents, and instruments executed in connection with the Plan, except as otherwise provided in the Plan.

(g) Notices. Any notice to the Debtor shall be in writing and mailed, and will be deemed to have been given three days after the date sent by first class mail, postage prepaid and addressed as follows:

Attorney for the Debtor

Debtor

(Name & Address)

(Name & Address)

UNITED STATES BANKRUPTCY COURT  
Northern District of California

In re:

Case No.

DISCLOSURE STATEMENT (Date)

**Introduction.**

Attached is Debtor's Chapter 11 plan (the Plan). (The court has tentatively determined that this Disclosure Statement provides adequate information to creditors.) You may be entitled to vote on the Plan, or object to confirmation of the Plan or final approval of the Disclosure Statement.

**Ballots must be received by Debtor's counsel, and objections to the Plan or Disclosure Statement must be filed with the court, on or before \_\_\_\_\_.** A hearing on confirmation of the Plan and final approval of the Disclosure Statement will be held on \_\_\_\_\_.

**Proposed Treatment of Claims.**

- A. **Secured creditors:** see Part 1 of the Plan.
- B. **General unsecured creditors** will be paid \_\_\_\_\_ percent of their allowed claim in \_\_\_\_\_ equal [monthly] [quarterly] installment over \_\_\_\_\_ [months] [years]. See Part 2 of the Plan.
- C. **Administrative, tax, and other priority claims** will be paid in full. See Part 3 of the Plan.
- D. **Executory contracts and leases:** see Part 4 of the Plan.

**Lawsuits.** Debtor may bring suit against certain creditors. See Part 7 of the Plan.

**Discharge and Enforcement of Plan.** Upon completion of payments under the Plan, Debtor will receive a discharge of pre-confirmation debts. The payments promised in the Plan constitute new contractual obligations that replace the discharged pre-confirmation debts. Creditors may not sue so long as Debtor is not in material default under the Plan. If Debtor materially defaults in performing the Plan, affected creditors may sue Debtor to enforce the terms of the Plan or move to convert to Chapter 7. See Parts 9 and 10 of the Plan.

**Voting.**

- A. **Who may vote.** Creditors are entitled to vote on confirmation of the Plan unless (i) the class is unimpaired (presumed to accept) or is to receive no distribution (presumed to reject); (ii) an objection as been filed to

that creditor's claim; or (iii) the claim is unclassified (required by law to be paid in full). A creditor whose claim has been objected to and who wishes to vote must move to have its claim allowed for voting purposes by filing a motion for such relief in time for that motion to be heard at or before the confirmation meeting.

**B. How to Vote.** Fill out and return the attached ballot so that it is received by Debtor's counsel on or before \_\_\_\_\_.

**C. Effect of Vote.** The Plan will be confirmed only if it is accepted by each impaired class, or if it is accepted by at least one impaired class (exclusive of insiders) and the court determines it is fair and equitable to all dissenting classes. A class of creditors accepts the Plan if it is accepted by a majority in number and two-thirds in dollar amount of creditors who cast ballots. A class of interests accepts the Plan if it is accepted by two-thirds in dollar amount of interest holders who cast ballots.

**Financial Information.** Debtor intends to make the payments required under the Plan from [cash available on the effective date], [revenues from future operations], [the sale of certain property], [new capital contributions], [and] [new loans]. See Part 8 of the Plan.

**A. Operations in Chapter 11.** During the \_\_\_\_\_ months since the petition date, Debtor had a cumulative operating profit] [loss] of \$ \_\_\_\_\_ on [an accrual] [a cash] basis, excluding professional expenses and filing fees incurred in the bankruptcy case. Upon request, Debtor will provide copies of monthly operating reports filed with the court.

**B. Cash Available on Effective Date.**

- (1) Cash on hand as of \_\_\_\_\_: \$ \_\_\_\_\_.
- (2) Additional cash in the amount of \$ \_\_\_\_\_ will be [invested] [loaned] by \_\_\_\_\_ (name) by \_\_\_\_\_ (date)
- (3) The total amount to be paid on the Effective Date is \$ \_\_\_\_\_.

**C. Liquidation Analysis.** General unsecured creditors might expect to receive the following in a chapter 7 liquidation.

**D. Projected Disposable Income.** Debtor calculates his projected disposable income for the five year period following confirmation to be the sum of \$ \_\_\_\_\_. This is based on the monthly income and expenses set forth on the schedules attached hereto as I and J, multiplied by 60 months.

**Assets:**

Cash on hand \$ \_\_\_\_\_





In re \_\_\_\_\_,  
Debtor

Case No. \_\_\_\_\_  
(if known)

### SCHEDULE J - CURRENT EXPENDITURES OF INDIVIDUAL DEBTOR(S)

Complete this schedule by estimating the average or projected monthly expenses of the debtor and the debtor's family at time case filed. Prorate any payments made bi-weekly, quarterly, semi-annually, or annually to show monthly rate. The average monthly expenses calculated on this form may differ from the deductions from income allowed on Form 22A or 22C.

Check this box if a joint petition is filed and debtor's spouse maintains a separate household. Complete a separate schedule of expenditures labeled "Spouse."

- 1. Rent or home mortgage payment (include lot rented for mobile home) \$ \_\_\_\_\_
  - a. Are real estate taxes included? Yes \_\_\_\_\_ No \_\_\_\_\_
  - b. Is property insurance included? Yes \_\_\_\_\_ No \_\_\_\_\_
- 2. Utilities:
  - a. Electricity and heating fuel \$ \_\_\_\_\_
  - b. Water and sewer \$ \_\_\_\_\_
  - c. Telephone \$ \_\_\_\_\_
  - d. Other \_\_\_\_\_ \$ \_\_\_\_\_
- 3. Home maintenance (repairs and upkeep) \$ \_\_\_\_\_
- 4. Food \$ \_\_\_\_\_
- 5. Clothing \$ \_\_\_\_\_
- 6. Laundry and dry cleaning \$ \_\_\_\_\_
- 7. Medical and dental expenses \$ \_\_\_\_\_
- 8. Transportation (not including car payments) \$ \_\_\_\_\_
- 9. Recreation, clubs and entertainment, newspapers, magazines, etc. \$ \_\_\_\_\_
- 10. Charitable contributions \$ \_\_\_\_\_
- 11. Insurance (not deducted from wages or included in home mortgage payments)
  - a. Homeowner's or renter's \$ \_\_\_\_\_
  - b. Life \$ \_\_\_\_\_
  - c. Health \$ \_\_\_\_\_
  - d. Auto \$ \_\_\_\_\_
  - e. Other \_\_\_\_\_ \$ \_\_\_\_\_
- 12. Taxes (not deducted from wages or included in home mortgage payments)  
(Specify) \_\_\_\_\_ \$ \_\_\_\_\_
- 13. Installment payments: (In chapter 11, 12, and 13 cases, do not list payments to be included in the plan)
  - a. Auto \$ \_\_\_\_\_
  - b. Other \_\_\_\_\_ \$ \_\_\_\_\_
  - c. Other \_\_\_\_\_ \$ \_\_\_\_\_
- 14. Alimony, maintenance, and support paid to others \$ \_\_\_\_\_
- 15. Payments for support of additional dependents not living at your home \$ \_\_\_\_\_
- 16. Regular expenses from operation of business, profession, or farm (attach detailed statement) \$ \_\_\_\_\_
- 17. Other \_\_\_\_\_ \$ \_\_\_\_\_

18. AVERAGE MONTHLY EXPENSES (Total lines 1-17. Report also on Summary of Schedules and, if applicable, on the Statistical Summary of Certain Liabilities and Related Data.) \$ \_\_\_\_\_

19. Describe any increase or decrease in expenditures reasonably anticipated to occur within the year following the filing of this document:

20. STATEMENT OF MONTHLY NET INCOME
- a. Average monthly income from Line 15 of Schedule I \$ \_\_\_\_\_
  - b. Average monthly expenses from Line 18 above \$ \_\_\_\_\_
  - c. Monthly net income (a. minus b.) \$ \_\_\_\_\_