INDIVIDUAL CHAPTER 11 CASES AFTER BAPCPA: WHAT HAPPENED TO THE "FRESH START?"

By Debra Grassgreen[*]

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*Pachulski Stang Ziehl Young Jones & Weintraub LLP, San Francisco, California

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I. INTRODUCTION

For the last 25 years, since the Supreme Court made it clear that individuals not engaged in business are eligible for Chapter 11 relief,[1] thousands of individuals with significant assets or earning potential have availed themselves of Chapter 11.[2] Chapter 11 served several purposes for these individuals. For some, Chapter 11 enabled them to reject oppressive personal services contracts and start anew, reaping the benefits of their personal services. For others, it allowed them to pay nondischargeable debts over time in accordance with their reorganization plan. For others, it provided breathing space from litigation. And it wasn't only Chapter 11 debtors who benefited. When individual debtors chose Chapter 11 over Chapter 7, creditors' recoveries were typically greater than they would have been in a Chapter 7 liquidation because in order to confirm a plan, debtors often contributed exempt assets or future earnings that would be unavailable to creditors in a Chapter 7 case.

However, because Chapter 11 was designed for businesses, not individuals, it was always an imperfect fit. As a result, there were a number of issues that were unique to individual Chapter 11 cases under the old law. These included application of the so-called "Earnings Exception" in order to determine what constitutes personal earnings that are excluded from the bankruptcy estate, whether a Chapter 11 plan can contain an injunction prohibiting collection of a nondischargeable debt, whether a debtor can reject a personal services contract and the effect of that rejection, and the application of the "good faith standard" and "Absolute Priority Rule" in connection with confirmation of an individual Chapter 11 plan. The Chapter 11 debtors that managed to wade their way through

these issues received the benefit of the same fresh start that Chapter 7 debtors receive.

With the bankruptcy amendments contained in the Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA"),[3] Congress attempted to address two of the issues that plagued many Chapter 11 individual cases: the Earnings Exception and the Absolute Priority Rule. However, in doing so, Congress radically changed Chapter 11 for individuals. Regrettably, these changes created more confusion than they cleared up and stripped Chapter 11 individual debtors of many of benefits of the coveted "fresh start."

Notwithstanding the sweeping changes to individual Chapter 11 cases, Congress failed to address some of the most basic issues that flow from those changes. The most drastic (and, some argue, unconstitutional)[4] change is that an individual's earnings from personal services after the commencement of the bankruptcy case are now part of the estate. Under the old law, bankruptcy courts consistently held that they had no jurisdiction to restrict the use of an individual Chapter 11 debtor's postpetition earnings.[5] But now, because those earnings are part of the bankruptcy estate, an individual's personal expenditures (even those for basic living expenses such as food, clothing, and entertainment) will be subject to review by (and possibly prior approval of) a bankruptcy judge. This level of scrutiny was not previously necessary in Chapter 11 cases. And since there is no mechanism for review or approval of such expenses and no modification to the standard for allowance of an administrative claim, individuals have no certainty about how their lifestyle will be impacted by Chapter 11. This lack of clarity will discourage individuals from filing Chapter 11. Individuals who are eligible will be more likely to file Chapter 7, leaving creditors with a smaller pool of assets from which to collect their debts.

This article will discuss some of the issues that faced Chapter 11 individual debtors before BAPCPA was enacted. It will then discuss the BAPCPA amendments relating to individual Chapter 11 cases and the expected impact of these amendments on future individual Chapter 11 cases.

II. KEY ISSUES IN INDIVIDUAL CHAPTER 11 CASES BEFORE BAPCPA

A. THE "EARNINGS EXCEPTION"

Before the 2005 bankruptcy amendments, section 541(a)(6)[6] of the Bankruptcy Code applied equally to Chapter 7 and Chapter 11. Accordingly, "earnings from services performed by an individual debtor after the commencement of the case" were nearly universally excluded from

an individual Chapter 11 debtor's bankruptcy estate.[7] One of the key issues that often arose in individual Chapter 11 cases (and Chapter 7 cases) was defining what portion of postpetition income was from personal services. In a simple case where a debtor worked for a third-party employer and received a weekly paycheck, it was not difficult to determine what income constituted personal earnings—the exercise required nothing more than prorating the weekly pay between pre and postpetition periods. But in many individual cases, the line was not as clear. This is particularly true where the debtor was a professional, such as a doctor or a lawyer; a sole proprietor; or a professional athlete or entertainer. In those cases, under the old law, courts struggled to allocate the portion of postpetition income derived directly from personal services of the individual and the portion of postpetition income derived from business or estate assets.[8] This issue has been taken off the table by the BAPCPA amendments because under new Bankruptcy Code section 1115, all property acquired after the commencement of a bankruptcy case, including earnings from services performed during the Chapter 11, are property of the estate.[9]

Interestingly, this portion of the new law will encourage debtors to select Chapter 7 liquidations rather than Chapter 11 repayment plans—a result directly at odds with what has been a stated purpose of the BAPCPA amendments. For many high-income debtors that find themselves in financial distress, their debts would not qualify as "consumer debts" for purposes of Bankruptcy Code section 707(b), which contains the new "means test." Thus, although concerns about good faith could result in dismissal of such a Chapter 7, individuals who have significant future earning capacity may very well choose to try Chapter 7 over Chapter 11. And since courts cannot compel conversion to Chapter 11 under the new law,[10] courts may be leery of applying section 707(b) to dismiss a case solely because of ability to pay in light of constitutional concerns.[11]

B. CONFIRMING A PLAN—THE ABSOLUTE PRIORITY RULE AND CONTRIBUTING FUTURE EARNINGS TO ESTABLISH "GOOD FAITH"

One of the other key issues that faced individual Chapter 11 debtors under the old bankruptcy law was whether a debtor must use personal earnings to fund a plan and if it did so, whether that would satisfy the "new value" corollary to the "Absolute Priority Rule." The Absolute Priority Rule, found in Bankruptcy Code section 1129(b),[12] bars any junior class of creditors or interest holders from receiving or retaining any property unless all senior classes have been paid in full. An exception to this rule has been upheld where the junior class is receiving property on

account of "new value" rather than its junior interest.[13] The problem that arose before the BAPCPA amendments was that because the term "property" in section 1129 is defined broadly, some courts held that an individual could not even retain exempt property unless the absolute priority rule were satisfied.[14] And since a contribution of future earnings does not satisfy the "new value exception," some individual debtors who could not confirm a consensual plan were left with the choice of converting their cases to Chapter 7 using substantial position of their future earnings to pay their creditors in full.

Other creditors have successfully required future earnings to be contributed to a plan by objecting to any plan that did not include earnings contributions as not satisfying the "good faith" confirmation requirement.[15] Some courts have held that an individual Chapter 11 plan is not in good faith *unless* the debtor contributes future earnings. For example, in *Gardner*, the court determined that an individual's Chapter 11 case must be converted where the debtor had no hope for meaningful reorganization based on the low amount of surplus future earnings that the debtor could contribute to a plan of reorganization.[16] And at least one other court has held that debtors must make full use of their resources to pay creditors, including using postpetition earnings.[17]

As is discussed in section III of this article, the BAPCPA changes to individual Chapter 11 cases address both of these confirmation issues by adding requirements that a certain portion of an individual's disposable income be contributed to a Chapter 11 plan.

C. COLLECTION INJUNCTIONS—PAYING NONDISCHARGEABLE DEBTS OVER TIME

Under the old law, one of the benefits of Chapter 11 was that a Chapter 11 plan could contain an injunction that would prevent the holders of nondischargeable debts from enforcing their claims against assets that were not property of the bankruptcy estate (such as exempt assets and postpetition earnings) as long as the plan provided for full payment of the nondischargeable claim and the debtor was making payments in accordance with his or her confirmed plan. These types of collection injunctions were permitted where assets that were not part of the estate (including future earnings) were necessary to the performance of the plan, and any action, employment of process, or act to collect, offset, or recover the claims, liens, and interests provided for under the plan would frustrate the debtor's rehabilitation.

Section 1141(d)(2) only precludes a reorganization plan from discharging nondischargeable debt.[18] Several courts in the Ninth Circuit have held that this provision does not restrict a plan from temporarily enjoin-

ing collection of a nondischargeable debt if the delay is necessary for the success of the plan and the other requirements of section 1129 of the Bankruptcy Code are satisfied.[19]

In *In re Brotby*, the court reviewed the legislative history of section 1141 of the Bankruptcy Code and found that although section 1141(d)(2) was intended to make clear that a debtor will remain obligated to pay nondischargeable debts, including tax debts, after plan confirmation, the statute was not intended to prohibit a temporary restriction on the collection activities of creditors holding nondischargeable claims.[20] "[Section] 1141(d)(2) was intended by Congress to answer the question *whether* after confirmation of a plan a creditor can collect a nondischargeable claim, not *when*."[21]

The *Brotby* court emphasized the importance of temporarily preventing holders of nondischargeable debts from collecting such debts from a reorganized debtor performing his obligations under a plan:

> The bankruptcy court's reasons for adopting a narrow reading of § 1141(d)(2) in *Mercado* are consistent with the bankruptcy policy favoring a fresh start for the debtor, while giving appropriate protection to the rights of creditors. This interpretation encourages flexibility for debtors attempting to reorganize, and may serve as an incentive to pursue confirmation of a plan instead of liquidation. At the same time, creditors, including those holding nondischargeable claims, are protected by the confirmation standards. In practice, as here, nondischargeable claims are paid in full, while other creditors also receive a benefit. An interpretation of § 1141(d)(2) that an individual debtor's plan can in no fashion modify the rights of a creditor holding a claim excepted from discharge would effectively grant that creditor a veto over the reorganization process. If a creditor holding a nondischargeable claim could not be temporarily prevented by a plan from pursuing collection, even where the creditor will be paid in full over time, that creditor is "in a position to undercut a debtor's attempt to reorganize, possibly harming other creditors who might benefit from the proposed plan."[22]

Section 105(a) of the Bankruptcy Code[23] provides further support for these types of collection injunctions. The bankruptcy court in *In re Mercado* invoked its equitable powers under section 105 of the Bankruptcy Code to sustain a plan injunction against collection of nondischargeable debts.[24] The *Mercado* court found that even if the provisions of Chapter 11 do not expressly authorize the imposition of a collection injunction in a Chapter 11 plan, section 105(a) provides ample statutory authority for the bankruptcy court's approval of such an injunction, provided a proper showing is made by the plan proponent to support such relief.[25]

Under the new law, it is not clear whether a similar collection injunction will be necessary, since holders of nondischargeable claims are barred from collecting their claims until the end of the plan term.[26] As is dis-

cussed below, the new law provides that a debtor does not receive a discharge upon confirmation of its plan, but only upon completion of the payments required under the plan.[27] The automatic stay that prohibits collection of a debt that arose before the commencement of the case stays in force until a discharge is "granted or denied."[28] These provisions could be read to prevent the holder of nondischargeable claims from collecting or enforcing its claims until the debtor either completes its plan payments or defaults on its plan. Thus, the need for a collection injunction has been eliminated and effectively strips the holder of a nondischargeable claim in an individual Chapter 11 case of any better rights than the holder of a dischargeable claim. This result may not be what was intended by the legislation, because it also delays the holder of a nondischargeable claim from pursuing exempt property and personal earnings not contributed to fund a plan.[29] Thus, until some law develops in the area, it might be prudent for Chapter 11 debtors to seek either a collection injunction or a determination of the impact of their plan on nondischargeable claims. Such injunctions should be granted almost universally under the reasoning of *Brotby* and *Mercado*, because in light of the disposable-income requirement, collection of a nondischargeable claim from the few non-estate assets the debtor has to live on (a debtor's "non" disposable income), would almost certainly frustrate the reorganization.

D. REJECTING PERSONAL SERVICE CONTRACTS

Under the old law, one of the benefits to individual debtors who were in financial distress was the ability to reject a personal services contract that was considered oppressive, enter into a new employment contract, and keep the earnings free of creditor claims. This was the quintessential "fresh start." Nothing in the new bankruptcy law restricts a debtor's ability to reject a personal services contract. But the benefits that flow from that rejection have been almost entirely stripped away. Under the new law, a debtor's earnings from a new employment contract are property of the estate—the debtor must devote them to pay creditor claims unless creditors are paid full. Because the rejection of the old contract will create a damage claim, the rejection will increase the pool of claims significantly. So unless the old contract is a long-term employment contract (longer than the term of the Chapter 11 plan) or is significantly more lucrative than the old employment contract, there may be little more than leverage gained by rejecting an old employment contract and entering into a new one.

Rejection alone does not always end the debate about employment contracts. Once rejection of a personal services contract is permitted, one of the key issues the individual debtor faces under both the old and the new law is the effect of the rejection on the nondebtor party's ability

to enforce "noncompete" and "exclusivity" provisions in the rejected employment contract.

1. The Effect of Rejection of an Employment Agreement

There are two lines of argument regarding the effect of rejection of an employment agreement on noncompete and exclusivity-type provisions.[30] One argument is that the rejection relieves the debtor of *all* future obligations under the contract. The other is that the critical question is not whether the contract has been rejected, but whether the debtor's discharge prevents the creditor from enforcing the contract.

a. Rejection May Free the Individual From All Future Obligations

A seminal case in this area, the Third Circuit's decision in *Matter of Taylor*,[31] has been widely cited for the proposition that rejection of a personal services contract relieves the debtor of all obligations under such contract. However, the issue was never squarely before the *Taylor* court.[32]

In *All Blacks, B.V. v. Gruntruck*,[33] the United States District Court for the Western District of Washington confronted the issue directly and denied the request of a record company to dismiss a rock music band's bankruptcy petition and enforce the terms of a recording contract between the band and the record company. Reinforcing the holding in *Taylor*, the *Gruntruck* court noted Supreme Court precedent consistent with the view that rejection was needed to give the debtor a "fresh start" and relieve the debtor from all prepetition obligations.[34] In refusing to allow the other party to enforce the recording contract, the *Gruntruck* court found that "the cases cited suggest that allowing [the record company] to achieve its goals [of enforcing the contracts] would contravene the primary purpose of the Bankruptcy Code."[35] Thus, in allowing the debtor to reject the recording contract, the court found that the obligations under the contract could not thereafter be enforced by the nondebtor parties.

b. A Discharge May Free an Individual of Future Obligations Under a Personal Services Contract

A more technical reading of Bankruptcy Code section 365 leads to the conclusion that the critical question with regard to the enforcement of noncompete or exclusivity clauses is not whether the contract was rejected but whether the debtor's discharge prevents a creditor from seeking equitable relief enforcing the injunction. To answer this question, a court must determine whether the equitable right to seek an injunction constitutes a dischargeable "claim."

The Bankruptcy Code discharges a debtor from "debts" that arose before the commencement of the bankruptcy case.[36] A "debt," in turn, is defined as "liability on a claim."[37] A "claim" is defined extremely broadly in the Bankruptcy Code, and encompasses a right to an equitable remedy for breach or performance if such breach gives rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured.[38] The critical issue is whether the definition of a "claim" encompasses an injunction to enforce a noncompetition or exclusivity provision.

In *Ohio v. Kovacs*,[39] the Supreme Court examined a prepetition judgment entered against Kovacs arising from his violations of various environmental laws. The judgment included a provision enjoining Kovacs from further polluting and requiring him to clean up the site. The judgment also included a damages component of $75,000. When Kovacs failed to comply, the State of Ohio obtained the appointment of a receiver over Kovacs's assets. Kovacs then commenced a Chapter 11 bankruptcy case, which he later converted to one under Chapter 7 of the Bankruptcy Code.[40]

The State of Ohio sued Kovacs in bankruptcy court on the grounds that his obligation to clean up the disposal site did not constitute a "claim," and therefore was not subject to the bankruptcy discharge. The Supreme Court determined that by obtaining the appointment of a receiver, the state had chosen to seek damages (as opposed to initiating criminal prosecution or other remedies) and now sought monetary compensation for its own clean-up costs, not Kovacs's performance pursuant to the injunction, thereby effectively converting its clean-up order into a claim for money damages.[41]

While the Court noted that Kovacs's discharge would not protect him from criminal prosecution arising from his violation of environmental laws or failure to comply with the terms of the judgment, the Court left open the issue of whether the injunctive provisions in the judgment were affected by the discharge, leaving room for debate as to whether the Supreme Court's holding would have varied had the State of Ohio pursued its equitable remedies exclusively without seeking monetary recoveries from Kovacs.[42]

The exact nature of the remedy sought by the creditor was also the focal point in *In re Udell*.[43] Udell was employed by Carpetland pursuant to an employment contract. The employment contract contained a three-year covenant not to engage in any business similar to Carpetland within fifty miles. The covenant provided that in the event of "Udell's actual or threatened breach of the provisions of this paragraph 11, Carpetland shall be entitled to an injunction restraining Udell as well as reimburse-

ment for reasonabl[e] attorneys fees incurred in securing said judgment and stipulated damages in the sum of $25,000.00."[44] After leaving his employment with Carpetland, Udell acquired a local carpet store and sued Carpetland in state court for breach of the employment agreement arising from allegedly unpaid commissions and other compensation. Carpetland counterclaimed for damages and sought an injunction pursuant to the provision reproduced above. The state court granted Carpetland a preliminary injunction. Soon thereafter, Udell commenced a Chapter 13 bankruptcy case. In order to enforce its preliminary injunction in state court, Carpetland moved for relief from the automatic stay, arguing that the injunction sought did not constitute a "claim" dischargeable in bankruptcy.[45] The bankruptcy court granted Carpetland's motion, but the district court reversed.

On appeal to the Seventh Circuit Court of Appeals, the court, looking to *Kovacs* for guidance, held:

> [A] right to an equitable remedy for breach of performance is a "claim" if the same breach also gives rise to a right to payment "with respect to" the equitable remedy. If the right to payment is an "alternative" to the right to an equitable remedy, the necessary relationship clearly exists, for the two remedies would be substitutes for one another.... [R]elationships other than outright substitution may also suffice. For example, the right to foreclose on a mortgage, though not strictly an "alternative" to the right to the proceeds from the sale of the debtor's property, nonetheless gives rise to a corollary right to payment (and may in fact be considered as an alternative to money in the sense that the debtor can stop the foreclosure by paying the full debt). The two remedies are sufficiently related that the Supreme Court classified the right to foreclose [as] a "claim."[46]

Applying its rule to the noncompetition provision in the Kovacs-Carpetland contract, the *Udell* court examined Indiana law to determine whether Carpetland's right to an injunction necessarily gave rise to a right of payment. Recognizing that Indiana law allowed for the imposition of an injunction in addition to an award of liquidated damages, the court held that Carpetland's pursuit of its injunction was not a barred "claim," because "Udell [could not] escape the restrictive covenant by paying $25,000 in liquidated damages."[47] By contrast, in *Kovacs*, the injunction sought was simply an order to pay money, either directly to a waste cleaning service or to the state to reimburse it for its cleaning costs.[48]

The decisions in *Kovacs* and *Udell* do not end the debate regarding the interplay between a creditor's right to injunctive relief and the definition of a dischargeable "claim" under the Bankruptcy Code. A different analysis of whether a noncompetition provision—this time, within an entertainment contract—constitutes a dischargeable "claim" is found in *In re Brown*.[49] Immediately after the commencement of his bankruptcy case,

Brown sought to reject certain management, recording, publishing, and production contracts between Brown and Death Row Records[50] and various entities and individuals associated with Death Row. Although the bankruptcy court authorized Brown's motion to reject, it declined to issue a declaration requested by Brown that none of the rejected contracts could be enforced against him and that Brown could seek new employment without fear of liability under the rejected contracts. Brown appealed to the district court the bankruptcy court's refusal to grant all the relief Brown requested.

Reaffirming the preclusive effect of rejection, the district court in *Brown* focused on the requirement that an equitable remedy "give[] rise to a right to payment" in order to be considered a claim. Applying a Third Circuit test for determining whether an award of damages constituted "an adequate substitute for specific performance," the district court looked to California law to determine the appropriate remedy for breaches of a covenant not to compete.[51] Concluding that California law permitted a court to impose an equitable remedy to enforce a covenant not to compete only where the performer was a "celebrity," the court found that Brown was not a "star" at the time he entered into the contracts with Death Row, and held: "Death Row has no right under California law to a purely equitable remedy to enforce against Brown the covenants not to compete. Because Death Row has no such right, all obligations and burdens under the executory contracts were discharged when Brown rejected them."[52]

As the case law discussed above evidences, there is no clear method for evaluating injunctive relief in the context of the Bankruptcy Code's definition of a "claim." As such, although under the new law the likelihood of rejection of a personal service contact is reduced, in the event that a debtor does reject such a contract, he or she will still face the question of whether noncompete clauses and other equitable relief that may be sought by an employer may be discharged in the bankruptcy case.

III. THE 2005 BANKRUPTCY AMENDMENTS TOOK MANY OF THESE ISSUES OFF THE TABLE

The wide-sweeping changes to the consumer provisions of the Bankruptcy Code captured most of the attention of the press and commentators when the BAPCPA amendments were enacted. But while no one was paying much attention, Congress also made significant changes to Chapter 11 for individual debtors. Although the full impact of the changes will not be evident for years to come, it is likely that the changes will encourage individuals that would have otherwise restructured their debts under Chapter 11 to opt for a Chapter 7 liquidation and a more meaningful fresh start.

This section will discuss each of the relevant changes to individual Chapter 11 cases. It will also discuss what types of issues will now be faced by individual Chapter 11 debtors and hypothesize about what type of individual will be the most likely candidate for Chapter 11 relief in light of these changes.

A. THE CHANGES

1. Postpetition Earnings are Property of the Estate—Section 1115

The BAPCPA amendments added Bankruptcy Code section 1115, which supplements an individual Chapter 11 estate with two categories of assets: assets acquired after the commencement of the case and postpetition earnings.[53] New section 1115 is virtually identical to Bankruptcy Code section 1306, which is only applicable in Chapter 13 cases. The addition of postpetition earnings to property of the estate assures that those assets are devoted to funding a plan of reorganization and that they are protected by the automatic stay.[54] It also ends the debate about allocating personal earnings from a sole proprietorship between an estate and an individual.

As a practical matter, this provision will likely cause great consternation for individual debtors and their advisors. Where previously individual Chapter 11 debtors could use earnings as they saw fit, now that earnings are property of the estate, presumably the debtor must obtain bankruptcy court approval to use those assets for personal living expenses. Congress, however, failed to provide any framework or standards for approval of such expenses. Although the Bankruptcy Code provides that the "actual, necessary costs and expenses of preserving the estate"[55] are administrative expenses and can be paid in the ordinary course, there is no provision that addresses personal living expenses for an individual Chapter 11 debtor.

Does a Chapter 11 individual debtor have to get approval for all personal living expenses? Or can these be considered "ordinary course"? Many everyday expenses would not be technically "necessary" to preserve the estate. Is going out to dinner or a movie necessary to preserve estate assets? What about clothing and vacations? Without any guidance in the law, individuals risk having the courts and creditors micromanage their discretionary expenditures.

One might argue that to the extent that the individual's earnings are necessary (and required) to fund a Chapter 11 plan, "preservation of the estate" includes preserving and maintaining a lifestyle consistent with those earnings. After all, we live in a reward-based society. It is only the rare altruistic soul who works tirelessly but is content with not reaping any of the financial rewards of that hard work. If a debtors are going to

have the same objective standard of living no matter how hard they work, it may be difficult to encourage a hardworking debtor to continue and not simply take it easy for some period of time.

Absent a practical interpretation of these provisions, they will most likely disincentivize individuals from maximizing their earning potential. A percentage contribution would have been more easily administered and would have incentivized the individual to work harder, earn more, and pay off debts faster. If an individual was certain he or she could retain a certain percentage of earnings, creditors would also benefit. Instead, the law as currently drafted provides little encouragement for individuals to maximize their earnings and lacks predictability.

And to make matters more complicated, when Congress amended the Bankruptcy Code to modify the definition of property of the estate, it did not make modifications to the tax laws and the "separate entity rule" to accommodate these changes. Thus, until the Tax Code is appropriately amended, tax consultants will have to struggle with how to account for the income from earnings paid over the estate and any funds for living expense paid back to the individual.[56]

2. Confirmation Requirements

a. Devoting Earnings to Fund a Plan—Section 1123(a)(8)

BAPCPA added section 1123(a)(8), which requires a debtor that is an individual to "provide for the payment to creditors under the plan of all or a portion of earnings from personal services performed by the debtor after the commencement of the case or other future income of the debtor as is necessary for the execution of the plan."[57] This section would appear to address the concern that was raised by the cases[58] discussed earlier that held that unless an individual debtor is contributing postpetition earnings to fund a plan, the plan might not satisfy the good faith standard of Bankruptcy Code section 1129(a)(3).

It is unclear, however, how this section is intended to work with new Bankruptcy Code section 1129(a)(15), which requires that "disposable income" be devoted to fund a plan unless unsecured creditors are to be paid in full.

b. Pay Claims in Full or Devote "Disposable Income"—Section 1129(a)(15)

In an effort to address the Absolute Priority Rule problem, BAPCPA added a new subsection to Bankruptcy Code section 1129 (Confirmation of a Plan) that is only applicable to individual Chapter 11 debtors. Bankruptcy Code section 1129(a)(15) provides that a plan may only be con-

firmed in a case in which the debtor is an individual and where the holder of any allowed unsecured claim objects if:[59]

> (A) the value as of the effective date of the plan, of the property to be distributed under the plan on account of such claim is not less than the amount of such claim; or
>
> (B) the value of the property to be distributed under the plan is not less than the projected disposable income of the debtor (as defined in section 1325(b)(2)) to be received during the 5-year period beginning on the date that the first payment is due under the plan or during the period for which the plan provides payments, whichever is longer.[60]

Unless creditors are paid in full, if there is a sole objecting creditor, this new section of the Bankruptcy Code appears to require individual debtors to contribute all of their disposable income to fund a plan, and the plan term can be no shorter than five years. However, if you read the language carefully and interpret it literally, that is not the requirement. The requirement in section 1129(a)(15) is that "the value of property" distributed be equal to the disposable income. The requirement is not that "the disposable income" be contributed directly. Thus, in a case where a debtor has substantial assets that can be liquidated to fund a plan, it could be argued that if the value of those assets equals the projected disposable income, then Bankruptcy Code section 1129(a)(15)(B) would be satisfied even if no disposable income is contributed. What then, does Bankruptcy Code section 1123(a)(8)'s requirement that earnings "necessary for execution of the plan" be contributed add? If the confirmation requirement contained in 1129(a)(15) is met, it is hard to imagine how further earnings are necessary for the "execution of the plan."

Although it is hard to predict how courts will interpret these new sections, most likely section 1123(a)(8) will be used to bolster a lack of good faith argument in the event that a debtor appears to be abusing the process by living a lavish lifestyle while paying creditors only a fraction of their claims.

c. Other Confirmation Requirements

Two additional confirmation requirements for individuals were added by BAPCPA. In accordance with Bankruptcy Code section 1129(a)(14), individual debtors are required to have their domestic support obligations current as of confirmation.[61] In addition, pursuant to a section of BAPCPA that was not incorporated into the Bankruptcy Code, individual debtors must establish that they have provided all tax information requested prior to confirmation.[62]

In addition, Bankruptcy Code section 1125 was amended to require a disclosure statement to contain a meaningful discussion of the federal tax consequences of a Chapter 11 plan. This provision applies equally to individual and corporate debtors and means that individuals will have to engage a tax professional to provide a careful tax analysis that applies the specific facts of the particular case to the tax law. It is unlikely that general boilerplate tax discussion will be acceptable.[63]

3. Delayed Discharge—11 U.S.C.A. § 1141(d)(5)

Under the old law, a Chapter 11 debtor, whether an individual or business, received its discharge upon confirmation (or the effectiveness) of its Chapter 11 plan. This has dramatically changed under the new law. BAPCPA added a new provision that provides that, unless ordered otherwise for cause, the discharge does not occur until the court grants a discharge on completion of all payments under the plan.[64] However, there is some flexibility in the new law, because another new provision of the Bankruptcy Code provides bankruptcy courts with flexibility to grant a discharge to a debtor that has not completed its payments under the plan, as long as the creditors have received at least as much as they would receive in a Chapter 7 liquidation and modification of the plan[65] is not "practicable."[66]

The delayed discharge provision has other consequences, because the granting or denial of a discharge is tied to the date that the automatic stay is lifted. Thus, as was mentioned previously,[67] holders of nondischargeable claims will be subject to the automatic stay until the plan payments are completed or a discharge is otherwise granted or denied.

4. Plan Modifications

Presumably because it was recognized that an individual's earnings capacity is not always stable and that personal circumstances can change over time, BAPCPA added a new provision dealing with the modification of a confirmed plan in an individual's Chapter 11 case. Bankruptcy Code section 1127(e) provides that if the debtor is an individual, the plan can be modified any time after confirmation on the request of the debtor, trustee, United States trustee, or the holder of an unsecured claim to increase or decrease payments or to alter the amount of payments.[68] Although this provision must have been designed to address changed circumstances or newly discussed facts, it does not require such a showing and includes no standard for approval of a plan modification other than that the other confirmation requirements have to be met.

Taken to its extreme, this could mean that even if a debtor files a plan within its exclusivity period and confirms that plan, a single creditor could

turn around and immediately file a request for a plan modification increasing the payments and the term. In an effort to provide finality, the author is hopeful that bankruptcy courts will be strict in considering postconfirmation plan modifications absent a strong showing of changed circumstances.

B. ARE THESE CHANGES CONSTITUTIONAL?

The changes to individual Chapter 11 may run afoul of the constitutional prohibition on involuntary servitude. One commentator has surmised that the "rush by the drafters of BAPCPA to have individual chapter 11 parallel chapter 13 in order to achieve creditor access to postpetition earnings form services, combined with (at best) inadvertent or (at worst) cynical failure to replicate the Chapter 13 protections against involuntary servitude, will surely result in a constitutional challenge to the 'new' individual chapter 11."[69]

Under the new law, not only are postpetition earnings property of a Chapter 11 estate, but a debtor is compelled to use those earnings to fund a Chapter 11 plan. The amendments do not take into account the fact that an individual can be placed into Chapter 11 involuntarily and that an individual has no absolute right to dismiss or convert its Chapter 11 case.[70] An individual debtor could then forced to comply with a Chapter 11 plan where the payment amounts and term can be increased on creditor motion. While the problem is heightened in an involuntary case, it is also present in a voluntary case where a creditor plan is proposed or a debtor plan is modified by motion of a creditor. Robert J. Keach argues that the inclusion of an individual's earnings as property of the estate, in certain circumstances, can result in "legal coercion" that offends the Thirteenth Amendment.[71] The problem is not solved by a debtor simply quitting his or her job. Never mind the practical problem that most debtors cannot survive without earnings, Keach notes that a debtor, even an involuntary debtor, is a fiduciary to the estate as to his or her earnings and therefore cannot simply "abandon them without consequence."[72]

A case decided under the old law is instructive. In *Matter of Noonan*,[73] a musician and songwriter, Robert A. Noonan (more popularly known as "Willie Nile"), sought to extricate himself from an 18-month exclusive recording contract with Arista Records, Inc. that Arista, according to the contract terms, had opted to extend for another 18-month term. Noonan commenced a Chapter 11 bankruptcy case and moved to reject the recording contract. Faced with "vehement opposition" and the prospect of "all out war" waged by Arista, Noonan then exercised his absolute right to convert his Chapter 11 case to one under Chapter 7,[74] admittedly "to take advantage of the automatic rejection of executory contracts given by 11 U.S.C.A. § 365(d)(1)."[75] The court noted:

> Noonan quite properly sensed that his bankruptcy trustee could not assume the Arista contract, for while he might force Noonan to the recording studio, he could not make him sing or play. Noonan also understood that the Arista contract is not the kind of contract capable of assignment by the trustee after assumption. As there could be no assumption or assignment, the trustee would either reject or the Arista contract would be deemed rejected. 11 U.S.C. § 365(d)(1) is clear as to this synergism.[76]

Arista responded swiftly and innovatively, asking the court to reconvert Noonan's case to an involuntary Chapter 11 case and offering to fund a plan (in the form of royalty advances to be recouped later) giving Noonan's creditors more than they could expect to receive in a Chapter 7 liquidation. Of course, the plan would be dependent upon Noonan's assumption of his recording contract with Arista.

Predictably, the court expressed grave concerns regarding the lynchpin of Arista's proposed plan. Citing case law invoking the Thirteenth Amendment's prohibition on involuntary servitude,[77] the court remarked:

> It is a longstanding rule that courts of equity will not order specific performance of personal service contracts… These considerations are the indices of a mature, democratic society. And hand in hand with their reaffirmation is recognition that *where problems have arisen in a contractual relationship calling for the performance of purely personal services, the termination of that relationship terminates the problems… It follows from all these generalities that Noonan cannot be compelled to abide by his contract with Arista but that it must be rejected* for it cannot be assumed unless Noonan wants it so.[78]

Because Arista's efforts to reconvert Noonan's case back to one under Chapter 11 were predicated on Noonan's assumption of his recording contract, the court denied Arista's motion.[79]

Noonan would be decided differently under the new law because new Bankruptcy Code section 707(b)(3) requires debtor consent for conversion from Chapter 7 to Chapter 11. The *Noonan* court's concerns about involuntary servitude are instructive, though. As caselaw develops under the "new" individual Chapter 11, the issue about the constitutionality of these provisions is sure to be one of the central issues that will need to be addressed.

C. WHO IN THEIR RIGHT MIND WOULD COMMENCE AN INDIVIDUAL CHAPTER 11 CASE NOW? WHO WOULDN'T?

In light of the expense related to administering a Chapter 11 case, Chapter 11 has been primarily used for individuals with substantial assets or earning capabilities. For these individuals, notwithstanding the fact that the changes to Chapter 7 are designed to force debtors to file Chapter 13 or 11, Chapter 7 may still be a viable alternative. This is

because the "means test" found in Bankruptcy Code section 707(b) applies only to debtors with "primarily consumer debts."[80]

Thus, the presumptions of substantial abuse based on income as set forth in section 707(b)(2)(A) do not apply. In light of the sweeping and significant changes to Chapter 11, we are left with the question of what type of individual would opt for Chapter 11 rather than Chapter 7 (to the extent it is available)? As discussed below, even with the modifications to the new law, there are a number of circumstances where individuals would benefit from Chapter 11 reorganization.

1. Individuals With Large Nondischargeable Claims and Assets to Protect

An individual who has large tax debts or other nondischargeable debts could find many benefits in Chapter 11. Because the Chapter 11 discharge is delayed until completion of plan payments, the holder of a nondischargeable claim is stayed from enforcing its claim against the debtor or the assets of the estate. Thus, even a debtor's exempt assets would be off-limits until the case was closed or dismissed or a general discharge was granted or denied. In that case, a Chapter 11 plan would have to provide for the full payment of the nondischargeable claim, but the debtor could make those payments over time without forfeiting assets to the creditor(s) holding a nondischargeable claim. For an individual who has the earning capacity or assets that can be orderly liquidated to pay the non-dischargeable claims over time, Chapter 11 would provide them with the breathing space to do so.

2. Buying Time—Individuals Facing Execution on a Judgment That Is on Appeal

Certain individuals have historically filed Chapter 11 when they were facing execution on a judgment and did not have sufficient assets to stay that judgment while an appeal proceeds. These individuals would also be more likely to file Chapter 11 than Chapter 7 in order to retain control of the litigation. In that case, the individual would have to balance the inconvenience and lifestyle adjustments attendant to the new Chapter 11, with the risk of permitting a Chapter 7 trustee to control significant litigation.

3. Individuals With Significant Assets—But Facing Short-Term Liquidity Problems—Who Can Benefit From Some Time to Restructure Their Debts

An individual with substantial assets may also be more likely to file Chapter 11 than Chapter 7 in order to protect the value of those assets, particularly if a timely liquidation of the assets could satisfy the estate's

obligations without the need to contribute personal earnings. Perhaps the debtor holds an asset that will not generate its empirical value in a quick sale through Chapter 7. The debtor could commence Chapter 11, file a plan that provides for a timely and orderly sale of the asset and a repayment plan for the outstanding debt from the asset. This would, in many cases, be preferable to an immediate "fire sale" of the asset by a Chapter 7 trustee.

4. An Individual With an Oppressive Employment Contract and Significant Postpetition Earning Potential Might Opt for Chapter 7 (and Face the Risk of an Involuntary Conversion)

By contrast, an individual who has an oppressive employment contract and the ability to generate substantial earnings postfiling[81] would generally fare better in a Chapter 7 case where the recovery on the claim by the employer for breach of the employment contract would be limited to the assets of the Chapter 7 estate. Of course, the debtor could face a motion to dismiss its case.

IV. CONCLUSION

The criticisms of the new Chapter 11 provisions include unconstitutionality, lack of coordination with the federal Tax Code, and overall inequity. As a result of the changes, Chapter 11 individual debtors no longer receive a "fresh" start and receive even fewer protections and benefits than are afforded Chapter 13 debtors. Among other things, the coveted discharge is delayed for what could be five or more years, and until it is granted, individuals risk having their confirmed plans modified on the request of a single creditor at any time. There is little finality in individual Chapter 11 cases, and some may be unconstitutional. Thus, it is likely that fewer debtors will opt for Chapter 11, and to the extent that Chapter 7 is available, many will be more likely to opt for a meaningful "fresh start."

Research References:

Bankr. Desk Guide §§ 1:46, 1:49, 6:4, to 6:6; Norton Bankr. L. & Prac. 2d §§ 18:9, 76:2, 84A:1

West's Key Number Digest, Bankruptcy ⚿ 2221 to 2223

1. Toibb v. Radloff, 501 U.S. 157, 111 S. Ct. 2197, 115 L. Ed. 2d 145, 21 Bankr. Ct. Dec. (CRR) 1296, 24 Collier Bankr. Cas. 2d (MB) 1179, Bankr. L. Rep. (CCH) P 73994 (1991).

2. Because Chapter 11 is considerably more expensive than Chapter 7, Chapter 11 has been generally limited to an elite group of individuals, often actors, athletes, and (previously) successful business people whose assets or earnings can bear the legal costs associated with a protracted Chapter 11 case. Among the high-profile individuals that have filed Chapter 11 are: Tia Carrere, Kim Basinger, Zsa Zsa Gabor, Vanessa Redgrave, Burt Reynolds, Toni Braxton, MC Hammer, Mike Tyson, Debbie Reynolds, Wayne Newton, Suge Knight, and Anna Nicole Smith.

3. Pub. L. No. 109-08, 119 Stat. 23 (2005).

4. Keach, Robert J., Dead Man Filing Redux: Is the New Individual Chapter Eleven Unconstitutional? 13 Am. Bankr. Inst. L. Rev. 483 (Winter 2005).

5. Roland v. Unum Life Ins. Co. of America, 223 B.R. 499 (E.D. Va. 1998) (bankruptcy court had no authority to prevent a debtor from using postpetition earnings to pay criminal attorney); see also Matter of Hargis, 887 F.2d 77, 19 Bankr. Ct. Dec. (CRR) 1664 (5th Cir. 1989), decision clarified on reh'g, 895 F.2d 1025 (5th Cir. 1990) (no authority to order disgorgement of earnings); In re Andrews, 80 F.3d 906, 28 Bankr. Ct. Dec. (CRR) 1117, 35 Collier Bankr. Cas. 2d (MB) 811, Bankr. L. Rep. (CCH) P 76993 (4th Cir. 1996).

6. See 11 U.S.C.A. § 541(a)(6).

7. See, e.g., In re Brotby, 303 B.R. 177, 42 Bankr. Ct. Dec. (CRR) 91, 51 Collier Bankr. Cas. 2d (MB) 677 (B.A.P. 9th Cir. 2003); Matter of Clark, 891 F.2d 111, 115, 19 Bankr. Ct. Dec. (CRR) 1875, Bankr. L. Rep. (CCH) P 73171 (5th Cir. 1989); In re Prince, 127 B.R. 187, 192 (N.D. Ill. 1991), decision aff'd, 85 F.3d 314, 29 Bankr. Ct. Dec. (CRR) 196, 36 Collier Bankr. Cas. 2d (MB) 149, 35 Fed. R. Serv. 3d 201 (7th Cir. 1996); In re Millerburg, 61 B.R. 125, 14 Collier Bankr. Cas. 2d (MB) 1405 (Bankr. E.D. N.C. 1986); In re Lundeen, 207 B.R. 604, 610 (Bankr. S.D. Ind. 1997); In re Powell, 187 B.R. 642, 27 Bankr. Ct. Dec. (CRR) 1145, 34 Collier Bankr. Cas. 2d (MB) 514, Bankr. L. Rep. (CCH) P 76683 (Bankr. D. Minn. 1995); In re Attanasio, 218 B.R. 180, 221-23 (Bankr. N.D. Ala. 1998). But see In re Harp, 166 B.R. 740, 30 Collier Bankr. Cas. 2d (MB) 1164 (Bankr. N.D. Ala. 1993) (a heavily criticized case that held that all postpetition wages must be used to satisfy creditor claims).

8. In re FitzSimmons, 725 F.2d 1208, 11 Bankr. Ct. Dec. (CRR) 799, 10 Collier Bankr. Cas. 2d (MB) 73, Bankr. L. Rep. (CCH) P 69754, 76 A.L.R. Fed. 845 (9th Cir. 1984); In re Cooley, 87 B.R. 432, 17 Bankr. Ct. Dec. (CRR) 903, Bankr. L. Rep. (CCH) P 72320 (Bankr. S.D. Tex. 1988); In re Herberman, 122 B.R. 273, 24 Collier Bankr. Cas. 2d (MB) 1105 (Bankr. W.D. Tex. 1990); In re Altchek, 124 B.R. 944 (Bankr. S.D. N.Y. 1991); In re Keenan, 195 B.R. 236, 28 Bankr. Ct. Dec. (CRR) 1289 (Bankr. W.D. N.Y. 1996) (citing In re Bradley, 185 B.R. 7, 10 (Bankr. W.D. N.Y. 1995)).

9. See 11 U.S.C.A. § 1115.

10. See 11 U.S.C.A. § 707(b)(1) (conversion only with "debtor's consent").

11. See discussion supra at section III B. See, e.g., In re McDonald, 213 B.R. 628, 630-31 (Bankr. E.D. N.Y. 1997) (dismissing Chapter 7 case because debtors might have had available disposable income for Chapter 13 plan, which would compromise Chapter 13's voluntary nature); In re Farrell, 150 B.R. 116, 119 (Bankr. D. N.J. 1992) (citing Congress' primary

concern that debtors not be compelled to work for benefit of creditors in violation of Thirteenth Amendment).

12. 11 U.S.C.A. § 1129 (b).

13. See Norwest Bank Worthington v. Ahlers, 485 U.S. 197, 108 S. Ct. 963, 99 L. Ed. 2d 169, 17 Bankr. Ct. Dec. (CRR) 201, 18 Collier Bankr. Cas. 2d (MB) 262, Bankr. L. Rep. (CCH) P 72186 (1988).

14. In re Hendrix, 131 B.R. 751, 22 Bankr. Ct. Dec. (CRR) 121 (Bankr. M.D. Fla. 1991); Matter of Yasparro, 100 B.R. 91, 95, 19 Bankr. Ct. Dec. (CRR) 745, Bankr. L. Rep. (CCH) P 72886 (Bankr. M.D. Fla. 1989) (rejected by, In re Henderson, 321 B.R. 550, 54 Collier Bankr. Cas. 2d (MB) 65 (Bankr. M.D. Fla. 2005)); In re Ashton, 107 B.R. 670, 674 (Bankr. D. N.D. 1989); see also In re Davis, 262 B.R. 791, 46 Collier Bankr. Cas. 2d (MB) 401 (Bankr. D. Ariz. 2001); In re Fross, 220 B.R. 405, 39 Collier Bankr. Cas. 2d (MB) 1419 (Bankr. D. Kan. 1998), judgment rev'd, 233 B.R. 176 (B.A.P. 10th Cir. 1999); In re Bolton, 188 B.R. 913, 28 Bankr. Ct. Dec. (CRR) 240, Bankr. L. Rep. (CCH) P 76773 (Bankr. D. Vt. 1995); In re East, 57 B.R. 14, 19 (Bankr. M.D. La. 1985).

15. See 11 U.S.C.A. § 1129(a)(3).

16. See In re Gardner, 2003 BANKR. LEXIS 250, *12-15, (Bankr. S.D.N.Y. March 14, 2003) (Gropper, J.) (debtor had no "reasonable likelihood of reorganization" where debtor could only contribute $15,000 to effectuate a plan of reorganization and had debt in excess of $8 million).

17. See In re Weber, 209 B.R. 793, 798, 30 Bankr. Ct. Dec. (CRR) 1305, 38 Collier Bankr. Cas. 2d (MB) 405 (Bankr. D. Mass. 1997) (determining that individual Chapter 11 debtor's plan funded out of future earnings failed to satisfy good-faith requirement of section 1129(a)(3), where debtor lived lavishly using same postpetition income).

18. See 11 U.S.C.A. § 1141(d)(2).

19. See Brotby, 303 B.R. 177; In re Mercado, 124 B.R. 799, 801-03, 21 Bankr. Ct. Dec. (CRR) 700, 24 Collier Bankr. Cas. 2d (MB) 1895 (Bankr. C.D. Cal. 1991). Such an injunction was also issued in the Southern District of New York in the Michael G. Tyson Chapter 11 case. Michael G. Tyson, et al., case no. 03-41900.

20. Brotby, 303 B.R. at 188.

21. Brotby, 303 B.R. at 189 (citing Mercado, 124 B.R. at 804).

22. Brotby, 303 B.R. at 189-190 (quoting Mercado, 124 B.R. at 804).

23. 11 U.S.C.A. § 105(a).

24. Mercado, 124 B.R. at 803 ("the bankruptcy court has the power to find that an injunction in the plan is appropriate should it be necessary for the success of the plan).

25. The Brotby court followed the Mercado court's reasoning:

> Under the equitable analysis implicated by §105(a), to establish the propriety of a collection injunction, the debtor must prove that it is necessary to allow the debtor to successfully reorganize and to perform the terms of the Chapter 11 plan. The injunction must also be tailored in duration and scope to afford the necessary relief to the debtor while not placing unnecessary restrictions on the target creditor's rights. In this regard, the debtor must demonstrate that the injunction does not prevent, but merely postpones, the creditor's collection of the nondischargeable claim in full pending debtor's performance of the plan. In addition, the injunction should be effective only as long as the debtor is properly performing and complying with the terms of the plan. If the debtor fails to make plan payments or engages in conduct that unfairly frustrates the rights of the creditor to collect its claim (e.g. by improperly conveying away assets), the creditor should be allowed relief from the collection injunction.

Brotby, 303 B.R. at 190.

26. 11 U.S.C.A. § 362(c)(2) provides that:

> the stay of *any other act* under subsection (a) of this section continues until the earliest of—
>
> (A) the time the case is closed;
>
> (B) the time the case is dismissed; or
>
> (C) if the case is case under chapter 7 of this title concerning an individual or a case under chapter 9, 11, 12 or 13 of the title, the time the discharge is granted or denied.

11 U.S.C.A. § 362(c) (emphasis added).

Subsection (a) of section 362 includes "any act to collect, assess or recover a claim against the debtor that arose before the commencement of the case under this title. 11 U.S.C.A. §362(a)(6).

27. See 11 U.S.C.A. § 1141(d)(5)(A). As is discussed infra at Section III A 3, under certain circumstances, a discharge can be issued earlier.

28. See 11 U.S.C.A. § 362(c).

29. Holders of nondischargeable claims may seek relief from the automatic stay to pursue exempt assets.

30. Because is it often difficult to enforce noncompete provisions in individuals' employment contracts, many contracts include what is termed an "exclusivity provision" that provides the individual will work exclusively for the employer for a period of time.

31. In Matter of Taylor, 913 F.2d 102, 20 Bankr. Ct. Dec. (CRR) 1515, 23 Collier Bankr. Cas. 2d (MB) 1035, Bankr. L. Rep. (CCH) P 73606 (3d Cir. 1990), James Taylor, a member of the band "Kool and the Gang," was subject to a contract that required him to record seven albums. After completing only one album, he commenced a Chapter 11 bankruptcy case and sought to reject the contract. The record company urged the court not to consider section 365 of the Bankruptcy Code in a vacuum, but instead to "take into account other provisions of the Bankruptcy Code, most notably § 541(a)(6)…," reasoning that "[s]ince an executory contract for the debtor's personal services is not part of the estate… such a contract is not within the 'jurisdiction' of the trustee, and the trustee simply has no power to deal with such a contract." Matter of Taylor, 913 F.2d at 106. The Third Circuit dismissed the argument as "rest[ing] upon some fundamental misconceptions" and distinguished Carrere. Matter of Taylor, 913 F.2d at 106-107 (emphasis added).

32. At the close of its opinion, the court remarked:

> Since we are dealing with a personal-services contract which could not be assumed without the parties' consent, and which would therefore, sooner or later, be deemed rejected in the absence of such consent, the debtor-in-possession was confronted with an extremely limited choice: he could reject the contract, or he could defer decision pending formulation of a plan of reorganization… We have no hesitation in concluding that no useful purpose would have been served by delaying the rejection decision. Indeed, *the task of formulating a successful reorganization plan is undoubtedly aided by promptly clarifying the potential availability of some or all of the revenues from the debtor's post-petition creative efforts.*

Matter of Taylor, 913 F.2d at 107 (emphasis added).

33. All Blacks B.V. v. Gruntruck, 199 B.R. 970 (W.D. Wash. 1996).

34. The Supreme Court has stated that:

> [o]ne of the primary purposes of the bankruptcy act is to "relieve the honest debtor form the weight of oppressive indebtedness and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortunes.

Local Loan Co. v. Hunt, 292 U.S. 234, 244, 54 S. Ct. 695, 78 L. Ed. 1230, 93 A.L.R. 195 (1934) (quoting Williams v. U.S. Fidelity & Guaranty Co., 236 U.S. 549, 554-55, 35 S. Ct. 289, 59 L. Ed. 713 (1915)).

35. Gruntruck, 199 B.R. at 975.

36. See 11 U.S.C.A. §§ 542, 727, 1141.

37. 11 U.S.C.A. § 101(12).

38. 11 U.S.C.A. § 101(5).

39. Ohio v. Kovacs, 469 U.S. 274, 105 S. Ct. 705, 83 L. Ed. 2d 649, 12 Bankr. Ct. Dec. (CRR) 541, 11 Collier Bankr. Cas. 2d (MB) 1067, 21 Env't. Rep. Cas. (BNA) 2169, Bankr. L. Rep. (CCH) P 70163, 15 Envtl. L. Rep. 20121 (1985).

40. Kovacs, 469 U.S. at 707.

41. Kovacs, 469 U.S. at 710.

42. See Kovacs, 469 U.S. at 711-12.

43. Matter of Udell, 18 F.3d 403, 30 Collier Bankr. Cas. 2d (MB) 1192, Bankr. L. Rep. (CCH) P 75752 (7th Cir. 1994) (rejected by, Glass v. Prcin, 3 S.W.3d 135 (Tex. App. Amarillo 1999)).

44. Udell, 18 F.3d at 405.

45. Udell, 18 F.3d at 404-405.

46. Udell, 18 F.3d at 408 (emphasis added; footnote omitted).

47. Udell, 18 F.3d at 409.

48. Courts and commentators following Udell analysis: In re Printronics, Inc., 189 B.R. 995, 28 Bankr. Ct. Dec. (CRR) 333, 35 Collier Bankr. Cas. 2d (MB) 84 (Bankr. N.D. Fla. 1995); In re May, 141 B.R. 940 (Bankr. S.D. Ohio 1992); In re Hughes, 166 B.R. 103, 30 Collier Bankr. Cas. 2d (MB) 2010, 10 I.E.R. Cas. (BNA) 221, Bankr. L. Rep. (CCH) P 75912 (Bankr. S.D. Ohio 1994); see, generally, Erin McMahon, Covenants Not to Compete: Bankruptcy Issues, 4 J. Bankr. Law & Prac. 115 (1995); see also In re Ward, 194 B.R. 703, 28 Bankr. Ct. Dec. (CRR) 1197 (Bankr. D. Mass. 1996). Dismissing the holding in Kovacs first, the Ward court noted that the Court curiously gave great significance to the state's actively seeking reimbursement for environmental clean-up costs and the fact that the debtor's compliance with the state court's decree required an expenditure of money, whereas the statutory definition of "claim" merely requires that the breach giving rise to the equitable remedy also give rise to a "right" to payment Ward, 194 B.R. at 710. Turning to Udell, the Ward court noted that the court's first test for determining that an equitable remedy constitutes a "claim"—that is, if payment arises from the exercise of the remedy—is virtually "unpassable," since "equitable remedies are typically designed to provide nonmonetary relief." Ward, 194 B.R. at 714. The Ward court found the second test articulated in Udell similarly unwieldy, since it requires *all* payments awarded for breach to be an alternative to the equitable remedy in order for the equitable remedy to constitute a claim: The test ignores the likely existence of a right to payment arising from damages other than the possible future harm to be alleviated by the equitable remedy, e.g., the nondebtor party may be entitled to compensation for damages already suffered as a result of the debtor's wrongful competition, in addition to (perhaps liquidated) damages for future harm—the impetus for the requested injunction. Because the injunction considered in Udell was a substitute remedy for future monetary damages, the injunction actually constituted a "claim." Ward, 194 B.R. at 714.

49. In re Brown, 31 Bankr. Ct. Dec. (CRR) 1055, 1997 WL 786994 (E.D. Pa. 1997).

50. Marion "Suge" Knight, the principal of Death Row Records, commenced an individual Chapter 11 case on April 4, 2006, and Death Row filed a Chapter 11 case the next day. Knight's Chapter 11 case is one of the first high-profile individual Chapter 11 cases filed

since BAPCPA was enacted and will therefore be watched closely to see how some of the questions raised by this article and other commentators are addressed.

51. Brown, 1997 WL 786994 at *4 ("The Court of Appeals for the Third Circuit considered the meaning of 'gives rise to a right of payment' in *Continental* [In re Continental Airlines, 125 F.3d 120, 31 Bankr. Ct. Dec. (CRR) 579, 156 L.R.R.M. (BNA) 2193, Bankr. L. Rep. (CCH) P 77557 (3d Cir. 1997)]. The dispute in that case arose from Continental's acquisition of Eastern Airlines which subsequently declared bankruptcy. Eastern Pilot Association claimed its collective bargaining agreement provided for integrating the seniority status of Eastern's pilots with the status of Continental's current pilots… Continental sought a declaration that the pilots' claims were, at best, unsecured claims compensable by a monetary award. The Court of Appeals agreed, holding that the pilots' demands could be satisfied through a monetary award instead of specific performance [of integrating seniority status]. Eschewing a specific formula, the court instead relied on various factors to determine that damages were an adequate substitute for specific performance. In accordance with the analysis in *Continental*, we must consider the remedial purpose, practicality and feasibility of issuing an injunction to enforce the covenants not to compete. The interpretation and enforceability of contracts such as these are dictated by state law.") (citation omitted).

52. Brown, 1997 WL 786994 at *6.

53. New Bankruptcy Code § 1115 provides:

> 1115. Property of the Estate
>
> (a) In a case in which the debtor is an individual, property of the estate includes, in addition to the property specified in section 541—
>
> (1) all property of the kind specified in section 541 that the debtor that the debtor acquires after the commencement of the case but before he case is closed, dismissed or converted to a case under chapter 7, 12, or 13, whichever occurs first; and
>
> (2) earnings from services performed by the debtor after the commencement of the case but before the case is closed, dismissed or converted to a case under chapter 7, 12, or 13, whichever occurs first.

11 U.S.C.A. § 1115.

54. As discussed previously, now that a Chapter 11 individual's discharge is delayed, the automatic stay remains in place after plan confirmation.

55. Bankruptcy Code section 503(b) provides that an administrative expense will be allowed for the "actual and necessary costs and expenses of preserving the estate." 11 U.S.C.A. § 503(b).

56. For a thorough discussion of the tax consequences of postpetition income as property of the estate, see Williams, Jack F. & Jacob L. Todres, Tax Consequences of Post-Petition Income as Property of the Estate in Individual Debtor Chapter 11 Case and Tax Disclosure in Chapter 11, 13 Am. Bankr. Inst. L. Rev. 701 (Winter 2005).

57. 11. U.S.C.A. § 1123(a)(8).

58. See discussion, supra, at Section II B.

59. This provision also modified one of the fundamental precepts of Chapter 11—the ability to bind dissenting members of an accepting class. It allows a single creditor holding an unsecured claim to trigger the requirements of section 1129(a)(15) even if the creditor's class has accepted the plan.

60. 11 U.S.C.A. § 1129(a)(15).

61. 11 U.S.C.A. 1129(a)(14).

62. BAPCPA § 1228(b).

63. 11. U.S.C.A. § 1125(a)(1). See also Williams, Jack F. & Jacob L. Todres, Tax Consequences of Post-Petition Income as Property of the Estate in Individual Debtor Chapter 11 Case and Tax Disclosure in Chapter 11, 13 Am. Bankr. Inst. L. Rev. 701 at 54 (Winter 2005).

64. 11 U.S.C.A. § 1141(d)(5)(A).

65. See discussion below.

66. 11 U.S.C.A. § 1141(d)(5)(B).

67. See discussion at Section II C.

68. 11 U.S.C.A. § 1127(c).

69. See Keach, Robert J., Dead Man Filing Redux: Is the New Individual Chapter Eleven Unconstitutional? 13 Am. Bankr. Inst. L. Rev. 483 (Winter 2005).

70. Revised Bankruptcy Code § 707(b) does required debtor consent for conversion from Chapter 7 to 11. See 11 U.S.C.A. § 707(b)(3)

71. See U.S. Const. amend XIII, § 1 ("Neither slavery nor involuntary servitude, except as a punishment for crime whereof the party shall have been duly convicted, shall exist within the United States, or any place subject to their jurisdiction.").

72. See Keach, Robert J., Dead Man Filing Redux: Is the New Individual Chapter Eleven Unconstitutional? 13 Am. Bankr. Inst. L. Rev. 483 (Winter 2005).

73. Matter of Noonan, 17 B.R. 793, 8 Bankr. Ct. Dec. (CRR) 919, 5 Collier Bankr. Cas. 2d (MB) 1536, Bankr. L. Rep. (CCH) P 68841 (Bankr. S.D. N.Y. 1982).

74. With limited restrictions, section 1112(a) of the Bankruptcy Code affords a debtor-in-possession the absolute right to convert its Chapter 11 case to one under Chapter 7.

75. Noonan, 17 B.R. at 795, 796.

76. Noonan, 17 B.R. at 796.

77. The court also expressed its concern more narrowly regarding the impact of Noonan's compelled assumption of his contract with Arista:

> If the debtor could be compelled to assume the [recording] contract, he would leave this bankruptcy court subject to at least $300,000 for indebtedness, which [the record company] could recoup from his future earnings… As the full measure of the debtor's fresh start flowing from the bankruptcy process is vital to Congress' mission in enacting the Code, anything which would frustrate this mission must be scrutinized carefully.

Noonan, 17 B.R. at 800 (citations omitted).

78. Noonan, 17 B.R. at 798, 799 (emphasis added).

79. The court also downplayed Arista's apocalyptic warnings regarding the impact of the court's decision on the music industry:

> This court is not moved by Arista's argument that this is a test case for the industry that requires, in the big picture, that it succeed. That Arista believes that the future of both the record industry and budding performance artists may be affected by a decision adverse to it may be a valid concern for record companies and the contractual exclusivity of their artists. However, this court is well aware that any business might be adversely affected by someone else's bankruptcy—the record industry is not unique to this plight.

Noonan, 17 B.R. at 796 n.9.

80. See 11 U.S.C.A. § 707(b).

81. This presumes the individual is otherwise eligible for bankruptcy relief and is not filing solely for the purpose of rejecting a contract that would likely be held to be in bad faith. See In re Integrated Telecom Express, Inc., 384 F.3d 108, 43 Bankr. Ct. Dec. (CRR) 175, Bankr. L. Rep. (CCH) P 80168 (3d Cir. 2004), cert. denied, 125 S. Ct. 2542, 162 L. Ed. 2d 286 (U.S. 2005).