Chapter 11 for Individual Consumer Debtors: Fresh Start or False Start?

At the end of every seven years thou shalt make a release. And this is the manner of the release; every creditor shall release that which he hath lent unto his neighbor; he shall not exact it of his neighbor and his brother; because the Lord's release hath been proclaimed.¹

INTRODUCTION

The "fresh start" doctrine dates back to biblical times, when every seven years all debts were cleared. No schedules were filed, no exemptions were determined, and most importantly, no decision was required as to which remedy would be used. Therefore, the debtor's pursuit of a fresh start was essentially guaranteed.

Today, however, the pursuit of debt relief through the Bankruptcy Code ("Code") has become much more complex. The individual consumer debtor ("consumer debtor") who would normally have the choice between chapter 7 liquidation⁴ or chapter 13 adjustment of debt⁵, now has the additional option of reorganization under

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2. A legislative purpose behind the Bankruptcy Code is to provide "to the honest but unfortunate debtor who surrenders for distribution the property which he owns at the time of bankruptcy, a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt." Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934). Traditionally, the "fresh start" concept was observed within the spectrum of dischargeability for consumer debtors under chapter 7. However, the "fresh start" doctrine has also been applied to chapter 13 consumer debtors. See In re Belt, 106 B.R. 553 (Bankr. N.D. Ind. 1989). In Belt, the court looked to the legislative history which explained "that [t]he purpose of Chapter 13 [was] to enable an individual, under court supervision and protection, to develop and perform under a plan for the repayment of his debtors over an extended period. This theory [was] to provide the debtor with effective relief and a fresh start." Id. (citing H.R. REP. No. 595, 95th Cong., 1st Sess. 118 (1977), reprinted in 1978 U.S.C.C.A.N. 5787, 6078-79). For an in-depth discussion of the "fresh start" concept, see Charles G. Hallinan, The "Fresh Start" Policy in Consumer Bankruptcy: A Historical Inventory & an Interpretive Theory, 21 U. RICH. L. REV. 49 (1986).


5. Id. §§ 1301-1330.
chapter 11. At first glance, the expansion of bankruptcy relief to include chapter 11 appears to advocate the policy of providing a fresh start to the consumer debtor. But in reality, the 1991 Supreme Court decision in Toibb v. Radloff, where the Court adhered to the position that chapter 11 was not solely reserved for businesses, threatened the consumer debtors' pursuit of a fresh start.

Despite this freedom of choice for remedies under the Bankruptcy Code, this ruling is a trap for those unwary consumer debtors, leading them away from a fresh start into a false start. This ruling will deceive consumer debtors into believing that chapter 11 will be their saving grace, instead of facing the reality that the only practical solution is to not even attempt the chapter 11 option. The Toibb ruling places the consumer debtors' pursuit of a fresh start in jeopardy. Moreover, it also raises the issue of whether legislative action should be taken to rewrite the Code to provide the necessary flexibility within chapter 13, so the consumer debtor will not have to turn to chapter 11.

This comment begins in section I by comparing and contrasting the two sections of the Bankruptcy Code, chapter 11 and chapter 13, which evidence markedly different approaches to debt restructuring. After demonstrating why chapter 11 is inappropriate for the consumer debtor, section II analyzes the Supreme Court's decision in Toibb v. Radloff. The Supreme Court discarded the importance of legislative history by relying on the plain meaning of the chapter 11 eligibility provision to hold that consumer debtors are permitted to file under chapter 11. Section III explores the theoretical and practical implications of having chapter 11 available to consumer debtors by analyzing the relevant case law and bankruptcy concepts. By exploring the implications, this section will illustrate how the consumer debtor will receive a false start by trying to obtain bankruptcy relief through chapter 11. Section IV concludes with specific recommendations for amending the Code to assure that a fresh start sought by the consumer debtor will not be a false start.

6. Id. §§ 1101-1174.
9. A false start occurs for the consumer debtor after he or she files a petition under chapter 11, because it is his or her only hope to save certain assets, like a home. Then, the court dismisses the case for other valid reasons, dashing the consumer debtor's hope for relief.
I. CHAPTER 11 & CHAPTER 13: THE REORGANIZATION CHAPTERS

The first step a typical consumer debtor must take in commencing a bankruptcy proceeding is to determine which chapter will provide him or her with the sought-after relief. Before *Toibb*, chapter 7 generally provided the relief sought by the consumer debtor trying to obtain his or her fresh start. Whereas, chapter 11 was an alternative for consumer debtors only within specific circuits. After *Toibb*, chapter 11 reorganizations became a generally recognized alternative for all consumer debtors. Since both chapters focus on reorganization of debt, an exploration of their respective approaches to reorganization will prove that Congress never intended chapter 11 to be

10. A chapter 13 adjustment of debt provides the consumer debtor with the opportunity for rehabilitation by permitting the debtor to create a plan where the creditors will receive payments usually derived from future income over a three to five-year period. Gross, *supra* note 10, at 65. For a comprehensive explanation of chapter 13 adjustment of debt, see *Sommer, supra* note 10, §§ 4.1-4.8.


13. For purposes of this comment, chapter 11 and chapter 13 are central and, therefore, only these chapters will be discussed in detail. While chapter 11 and chapter 13 involve reorganization of a debtor's debt, chapter 7 generally relieves the debtor of his or her assets through liquidation before a discharge is granted.
used by anyone other than business debtors,\(^{14}\) while chapter 13 solely concentrated on the consumer debtor.\(^{15}\) Not only is regular income required in a chapter 13 proceeding, but the consumer debtor may have to apply his or her future disposable income to the reorganization plan.\(^{16}\) The disposable income requirement generally occurs if a creditor objects to the plan. The objection will commit the consumer debtor's future disposable income to all creditors.\(^{17}\) Therefore, both the regular income and the future disposable income requirements under chapter 13 help to ensure that creditors will receive an equitable distribution. It is hard to envision a consumer debtor attempting to complete a repayment plan when no income is available to fund the

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\(^{14}\) The business focus of chapter 11 was evident in chapter 11's predecessors in the Bankruptcy Act of 1898, chapters X, XI, and XII. The consolidation of these chapters occurred in the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (1978). Congress's express intent in merging the chapters was to simplify the law for business reorganizations by "eliminating unnecessary differences in detail that are inevitable under separately administered statutes." S. REP. No. 989, 95th Cong., 2d Sess. 9 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5795. Therefore, through the reorganization, "a chapter 11 debtor is given breathing room and powerful tools to rescale its operations and, in time, to modify both the debt and equity portions of its capital structure." GEORGE M. TREISTER ET AL., FUNDAMENTALS OF BANKRUPTCY LAW § 9.01 (3d ed. 1988 & Supp. 1992).

\(^{15}\) 11 U.S.C. § 109(e) provides that: "Only an individual with regular income that owes, on the date of filing of the petition, noncontingent, liquidated, unsecured debts of less than $100,000 and noncontingent, liquidated, secured debts of less than $350,000 . . . may be a debtor under chapter 13 of this title." 11 U.S.C. § 109(e) (1988). For example, a consumer debtor with credit card debt of $102,000 or a mortgage of $357,000 would not be eligible for chapter 13. The purpose behind the dollar limitations is to stop potential abuse of the system by preventing "sole proprietors with large businesses from abusing creditors by avoiding chapter 11." H.R. REP. No. 595, 95th Cong., 1st Sess. 119 (1977), reprinted in 1978 U.S.C.C.A.N. 5787, 6080. The $350,000 limit for secured claims was the compromise between the House's proposal of $500,000 and the Senate's $200,000. 124 CONG. REC. S17,407 (daily ed. Oct. 6, 1978) (statement of Sen. DeConcini); 124 CONG. REC. H11,091 (daily ed. Sept. 28, 1978) (statement of Rep. Edwards).

\(^{16}\) If the trustee or the holder of an allowed unsecured claim objects to confirmation of the plan . . . (B) the plan provides that all of the debtor's projected disposable income to be received in the three-year period beginning on the date that the first payment is due under the plan will be applied to make payments under the plan.


\(^{17}\) 11 U.S.C. § 1325(b)(1)(B) (1988). However, if the creditor would not receive anything under chapter 7, the creditor is not entitled to receive anything under chapter 13, regardless of an objection. Id. § 1325(a)(4). The other available option for the objecting creditor would be to receive full payment of their claim. Id. § 1325(b)(1)(A).
plan. Yet, under chapter 11, even though regular income is not required, some means must be available to effectuate the reorganization plan.

After examining the eligibility issues, the consumer debtor should consider the complexity of creating the plan under both chapters. The development of a chapter 13 reorganization plan is a less time consuming quest, where the consumer debtor exerts more control over the proceeding. The reason behind this premise is that under chapter 13 only the debtor may file a plan. Furthermore, chapter 13 calls for a simplified process, necessitating only court approval. Creditors may defeat the plan by successful objection to confirmation, but other than objecting, creditors have little power over the consumer debtor's decisions in a chapter 13 proceeding. In contrast, chapter 11 allows any party in interest to file a plan after the debtor's exclusivity period.

18. Therefore, this eligibility requirement which may be viewed as a deterrent to the consumer debtor, only helps the consumer debtor to comply with the plan and work towards his or her fresh start. Whereas chapter 11, which states no eligibility requirement when filing a petition, will then not confirm a plan because the consumer debtor has no means to effectuate the reorganization. This is an example of how the unwary consumer debtor will receive a false start by filing under chapter 11. See generally Drake, supra note 16 (discusses the concept of regular income under chapter 13).

19. Rabea J. Zayed, Individual Consumer Debtors are Eligible for Chapter 11 Relief, 1988 U. Ill. L. Rev. 785, 787. Unfortunately, some courts concede that periodic inflow of income is sufficient when determining whether there are sufficient means to reorganize. See In re Moog, 774 F.2d 1073, 1075 (11th Cir. 1985).

20. 11 U.S.C. § 1321 (1988). A plan under chapter 13 usually is three years, but if cause is shown, the plan can extend to five years. Id. § 1322(c). The duration of a chapter 11 plan is not restricted. See 11 U.S.C. § 1123 (1988).

21. § 1325(a)(1) states that the "court" shall confirm the plan when the specified requirements are met. 11 U.S.C. § 1325(a)(1) (1988).

22. Id. § 1325(b). In the event that an unsecured creditor objects to the plan, the objecting unsecured creditor will either receive full payment of the claim, or all the consumer debtor's disposable income will be applied to the plan. Id. § 1325(b)(1). With respect to the objecting secured creditor, the consumer debtor's plan can still be confirmed if the creditor retains the lien securing the claim, and the value of the property to be distributed is not less than the allowed amount of the claim, otherwise the consumer debtor will ultimately have to surrender the property securing the lien to the creditor. Id. § 1325(a)(5).

23. Any party in interest includes: "the debtor, the trustee, a creditors' committee, an equity security holders' committee, a creditor, an equity security holder, or any indentured trustee . . . ." 11 U.S.C. § 1121(c) (1988).

24. 11 U.S.C. § 1126(a) (1988). Therefore, chapter 13 provides the consumer debtor with a less complicated procedure which he or she can control.
Since the outcome of the bankruptcy proceeding is to obtain a discharge, the consumer debtor must seriously consider the limitations within both chapters’ discharge provisions. Both chapters have exceptions to discharge, but the exceptions under chapter 13 are more closely identified with the individual. The chapter 13 exceptions to discharge are: (1) allowed claims not provided for in the plan; (2) long term obligations that extend beyond the length of the plan; (3) alimony and child support; (4) educational loans; and (5) debts for drunk driving.25 Furthermore, a hardship discharge is available under chapter 13 for the debtor who can prove that circumstances beyond his or her control prevent continued payments to the plan, even if the plan is modified.26 In contrast, the exceptions to discharge under chapter 11 not only encompass the exceptions for chapter 13, but also include tax debts, fines, and penalties or forfeitures payable to and for the benefit of governmental units.27 Also, no equivalent hardship provision is within the chapter 11 provisions. The only benefit of chapter 11’s discharge provision is that discharge results upon confirmation of the plan, whereas chapter 13’s discharge is not granted until plan completion.28 Therefore, chapter 13’s discharge provision not only provides the consumer debtor with the option to dismiss the case at any time before completion of the plan,29 the broader discharge and the hardship option will help to ensure the consumer debtor with a fresh start.

The consumer debtor must also understand that before granting a discharge, the possibility of having a case converted to chapter 7 or dismissed for cause is always a possibility. When a case is dismissed under these circumstances, the court is concluding that the debtor did not file the petition in good faith. Before granting the conversion or dismissal, the court examines the statutory grounds set forth under each chapter.30 Most importantly, in a chapter 11 case one of the causes for conversion or dismissal is the inability to effectuate a

26. Id. § 1328(b).
27. Id. §§ 523(a), 1141(d)(2). Chapter 11’s exceptions to discharge emphasize the business nature of the relief. Not many private individuals are fined by governmental units in comparison with businesses and corporations. See § 523(a) to view the complete list of exceptions from discharge for chapter 11 debtors.
28. Id. § 1141(d). Since the discharge occurs before payments to the plan begin, dismissal is harder to obtain.
29. Id. § 1328(a). This is known as the absolute right to dismissal.
30. The two sections which list the statutory grounds for conversion to chapter 7 or dismissal are § 1112(b) and § 1307. 11 U.S.C. §§ 1112(b), 1307(c) (1988). See infra note 110 for the 10 statutory grounds listed in chapter 11.
Even though chapter 13 shares many of the same provisions to permit dismissal or conversion, the clause pertaining to ability to effectuate a plan is not present under the chapter 13 provision. This indicates that broad discretion has been granted to the court in making a determination as to whether the debtor will be able to effectuate a plan under chapter 11 — making dismissals or conversions more probable.

The consumer debtor must examine the differences between each chapter's approach to modifying the rights of claim holders. The chapter 13 plan may modify the rights of holders of secured and unsecured claims and cure or waive any defaults. The modification within a chapter 13 is limited to those secured creditors "other than one whose sole collateral is a mortgage or other security interest on the debtor's home," whereas, in chapter 11, a plan may "impair" any class of claims. Therefore, chapter 13's treatment is different because "Congress intended Chapter 13 to be the primary tool of wage earners to save their homes." Moreover, chapter 13 supplies

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31. Id. § 1112(b)(2). Courts appear to interpret the applicable chapter 11 clause broadly to include an ongoing business requirement. More specifically, if the consumer debtor did not have an ongoing business, the question was raised as to whether the consumer debtor could effectuate a reorganization plan. See infra notes 103-18 and accompanying text for a discussion involving courts' use of cause to circumvent the *Toibb* decision permitting consumer debtors to file chapter 11 petitions.


34. 11 U.S.C. § 1322(b)(1988). Specifically, the debtor can cure a default and reinstate terms on a home mortgage even if the debt is accelerated, as long as the foreclosure is not completed before the petition. In re Glenn, 760 F.2d 1428, 1442 (6th Cir. 1985). However, this right is limited. In re Wilks, 123 B.R. 555, 561 (Bankr. W.D. Tex. 1991). Even though a debtor may cure defaults on its home mortgage under 11 U.S.C. § 1322(b)(2), the debtor is explicitly precluded from lien stripping the mortgage debt down to the property's current value. Id. No comparable section is available within chapter 11. *Id.*

35. TREISTER, supra note 15, at 339.

36. Under 11 U.S.C. § 1123(b)(1) (1988), "a plan may (1) impair or leave unimpaired any class of claims, secured or unsecured, or of interests." Impairment indicates the rights of a class of claims has been affected by the reorganization plan. TREISTER, supra note 15, at 401-09.

safeguards for the creditor to obtain an equitable distribution, while permitting the consumer debtor to modify those applicable claims and defaults so as to better meet their mortgage requirements.

Lastly, procedural differences need to be considered. The filing fee for a chapter 11 debtor is $600.00, opposed to the $150.00 fee for a chapter 13 filing.\textsuperscript{38} Preparation in chapter 11 is more complex, starting with the need for a disclosure statement.\textsuperscript{39} Furthermore, chapter 11 requires the appointment of an unsecured creditors committee.\textsuperscript{40} These procedural aspects increase the cost of chapter 11 to the consumer debtor, where chapter 13 does not require these added preparations.

The preceding explores the differences between the two chapters, evidencing the nature of chapter 11 as serving the business debtor. Even though certain chapter 11 aspects, like the lack of eligibility criteria or the option to create a plan exceeding five years, seem advantageous to the unwary consumer debtor, a careful analysis indicates that a consumer debtor does not belong within the provisions of chapter 11.

II. \textit{Toibb v. Radloff}: Freedom to Choose a False Start, Not a Fresh Start

Freedom of choice was the foundation of the Supreme Court decision in \textit{Toibb v. Radloff}.\textsuperscript{41} The Supreme Court held that chapter 11 of the Bankruptcy Code did not contain an "ongoing business" requirement, allowing individuals not engaged in business to file for relief under that chapter.\textsuperscript{42} The Supreme Court based its decision on a narrow statutory interpretation of the Code, paying little deference to the legislative history, structure, or policy considerations behind chapter 11.\textsuperscript{43} Therefore, individuals now have the freedom to choose among three options of relief when filing for bankruptcy.\textsuperscript{44} Even though chapter 11 was not expressly forbidden to consumer debtors

\textsuperscript{39} 11 U.S.C. § 1125 (1988). The disclosure statement allows information to be revealed which will help determine the feasibility of the plan. This section was not available under the Bankruptcy Act of 1898.
\textsuperscript{40} 11 U.S.C. § 1102(a) (1988).
\textsuperscript{41} 111 S. Ct. 2197 (1991).
\textsuperscript{42} \textit{Id.} at 2202.
\textsuperscript{43} \textit{Id.} at 2197.
\textsuperscript{44} The three options available are chapter 7 liquidation, chapter 13 adjustment of debt for individuals with regular income, and chapter 11 reorganization.
prior to this decision, the action of the Court conferring this absolute right for consumer debtors will undoubtedly become a trojan horse to the unwary. By opening chapter 11 to the consumer debtor this freedom of choice will become a trap to those not literate with the concepts of bankruptcy relief. Now consumer debtors have the opportunity to walk into a chapter 11 with visions of a fresh start, only to be caught in the web of false hopes and disillusionment.

A. PROCEDURAL HISTORY: THE IMPORTANCE OF LEGISLATIVE HISTORY

Sheldon Baruch Toibb, an independent consultant, initially filed for bankruptcy under chapter 7. Upon learning that he owned stock of substantial value, he converted his chapter 7 liquidation into a chapter 11 reorganization to preserve the value of the stock.

The bankruptcy court, district court and the court of appeals each held that Toibb did not qualify for relief under chapter 11 because he was not engaged in business. Each of these courts relied on Wamsganz v. Boatmen's Bank of De Soto, wherein the Eighth Circuit thoroughly examined the legislative history of chapter 11 in support of the theory that chapter 11 should be limited to non-consumer debtors.

In concluding that consumer debtors could not seek relief under chapter 11, the Wamsganz court first viewed the legislative history as a whole. In examining the legislative history, the court pointed to

45. See supra note 13 for cases permitting consumer debtors to file under chapter 11.

46. Toibb was an attorney who after gaining expertise in the area of energy law, marketed a business plan which eventually was formed into a hydroelectric generation corporation by entrepreneurs. Along with obtaining 24% of the stock in the corporation, Toibb also executed a consulting agreement to be an independent contractor with the corporation. See generally Joint Appendix, Toibb v. Radloff, 111 S. Ct. 2197 (1991) (No. 90-368), available in LEXIS, Genfed Library, Supreme Court Briefs File [hereinafter Joint Appendix].

47. Toibb, 111 S. Ct. at 2198.

48. Id. at 2198. The debtor owned 24% of company stock of a company he organized, yet was subsequently terminated.

49. Id. at 2197. As indicated in Toibb, while this case was in the bankruptcy court, the debtor had attempted to demonstrate that he had a business to reorganize. Id. at 2198-99. See generally Joint Appendix, supra note 49 (presenting and documenting that the debtor was engaged in business).

50. 804 F.2d 503 (8th Cir. 1986).

51. Id. at 505.

52. Id.; see, e.g., In re Ponn Realty Trust, 4 B.R. 226, 229-30 (Bankr. D. Mass. 1980) (reemphasizing the necessity of examining the whole legislative history of the Bankruptcy Code to determine whether the "court [was] within the intended purpose of Chapter 11.")
specific references made within Senate and House reports supporting its position.\textsuperscript{53} The Senate report cited in \textit{Wamsganz} referred to chapter 11 as the "single chapter for all business reorganizations."\textsuperscript{54} While the House report reemphasized the business purpose by referring to chapter 11 as "a consolidated chapter for all business reorganizations."\textsuperscript{55}

\textit{Wamsganz} further supported the legislative history analysis of its decision by relying on \textit{In re Ponn Realty Trust},\textsuperscript{56} which also delved into the legislative history of chapter 11. The \textit{Ponn} court also cited Senate and House reports which illustrated the business purpose behind chapter 11.\textsuperscript{57} The Senate report stated the purpose of chapter 11 as "the reorganization of a financially distressed business enterprise, providing for its rehabilitation by adjustment of its debt and equity interest."\textsuperscript{58} While the House report expressed a similar intent for chapter 11, stating "the purpose of a business reorganization case . . . is to restructure a business's finances so that it may continue to operate, provide its employees with jobs and pay its creditors . . . . If the business can extend or reduce its debts, it often can be returned to a viable state."\textsuperscript{59} Moreover, the \textit{Ponn} court supplemented the legislative history rationale with statements made by "legislative leaders."\textsuperscript{60}

Aside from legislative history, \textit{Wamsganz} also relied on earlier cases\textsuperscript{61} which explored specific Code provisions that were more "con-

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\item \textsuperscript{53} \textit{Wamsganz}, 804 F.2d at 505.
\item \textsuperscript{56} 4 B.R. 226 (Bankr. D. Mass. 1980).
\item \textsuperscript{57} \textit{Id.} at 230.
\item \textsuperscript{60} \textit{Ponn}, 4 B.R. at 230. Comments included those by Senator DeConcini, "it has been the experience of the great majority of those who have testified . . . that a consolidated approach to business rehabilitation is warranted." 124 CONG. REC. S17,406 (daily ed. Oct. 6, 1978) (statement of Sen. DeConcini); Hon. Don Edwards remarked that chapter 11 "will protect the investing public, protect jobs, and help save troubled businesses." 124 CONG. REC. H11,089 (daily ed. Sept. 28, 1978) (statement of Rep. Edwards).
\item \textsuperscript{61} \textit{In re Little Creek Dev. Co.}, 779 F.2d 1068 (5th Cir. 1986); \textit{In re Winshall Settlor’s Trust}, 758 F.2d 1136 (6th Cir. 1985); \textit{In re Ponn Realty Trust}, 4 B.R. 226 (Bankr. D. Mass. 1980). Even though these cases did not directly address the issue
sistent with application to business enterprises than to individual consumers." The court in *In re Ponn Realty* reviewed section 1102 which provided the guidelines to create a committee of unsecured creditors, and section 1103 which explained the purpose of the 1102 committee, which was to "investigate the operation of the debtor's business and the desirability of the continuance of the business." The court in *In re Winshall Settlor's Trust* explored the ongoing business requirement, which was implied by the court through section 1112(b) of the Bankruptcy Code. The court stated that if the debtor had no ongoing business to reorganize, the debtor in effect did not have the means to effectuate a reorganization, which would have provided the court with the proper rationale to dismiss the case for lack of good faith.

The *Wamsganz* opinion set forth the significant evidence from the legislative history and the Code provisions which support the view of whether an individual consumer debtor was eligible to file under chapter 11, all three cases provided an in-depth analysis of the purpose behind chapter 11 and the issue of good faith. A fourth case discussed in *Wamsganz* was *In re Mogul*, 17 B.R. 680 (Bankr. M.D. Fla. 1982), which was the only case which dealt with chapter 11 eligibility and its real focus was good faith versus eligibility.

66. *In re Ponn Realty Trust*, 4 B.R. 226, 231 (Bankr. D. Mass. 1980); *cf. In re Wamsganz*, 54 B.R. 759, 762 (Bankr. E.D. Mo. 1985), aff'd, 804 F.2d 503 (8th Cir. 1986) (The *Wamsganz* court pointed to § 1108 which permitted the debtor to retain his or her property and operate the business, and § 1113 which allowed debtors to reject collective bargaining agreements, as evidence of Code provisions that confirm chapter 11's business character.).
67. 758 F.2d 1136 (6th Cir. 1985).
68. *Winshall*, 758 F.2d at 1137. § 1112(b) permitted the court after notice and hearing to convert a chapter 11 case to a chapter 7 or to dismiss the chapter 11 for "cause" including inability to effectuate a plan. 11 U.S.C. § 1112(b)(2) (1988).
69. *Winshall*, 758 F.2d at 1137. The court came to this conclusion by first looking to § 1123(a)(5) which required the debtor to have adequate means to execute the plan in order to obtain plan confirmation. *Id.; cf. In re Little Creek Dev. Co.*, 779 F.2d 1068, 1073 (5th Cir. 1986) (stating the purpose of chapter 11 reorganization was to provide the "breathing" space necessary to get the business back into an operating state, which coincides with the courts' requirement of an on-going business factor within good faith to succeed successfully under chapter 11). The *Winshall* analysis now appears to be a method of circumventing the eligibility aspect of § 109(d) permitting the consumer debtor to file under chapter 11. See *infra* notes 103-18 for a detailed analysis of this premise.
that chapter 11 is not suitable for the consumer debtor. The lower courts in *Toibb* correctly regarded this precedent when deciding that the consumer debtor should not engage in a chapter 11 proceeding. The overwhelming evidence used by the lower courts clearly indicated the importance of the legislative history used to ultimately protect the consumer debtor from the hurdles of chapter 11. However, the Supreme Court granted certiorari because the lower courts’ holding, barring chapter 11 from consumer debtors, conflicted with *In re Moog*,70 which permitted consumer debtors to file under chapter 11.71

B. **TOIBB: SETTING THE TRAP**

The Supreme Court in *Toibb* based its decision to permit consumer debtors to file under chapter 11 on what it perceived to be the plain language of the Bankruptcy Code.72 The Court relied on a basic canon of statutory construction in which the court looks to the legislative history to determine congressional intent only when the statutory language is ambiguous.73

The statutory provision at issue was section 109(d) of the Bankruptcy Code.74 While section 109 set out the eligibility requirements as to who may have been a debtor, section 101(41) defined person to include “individuals,”75 entitling individuals to file under chapter 11. Moreover, a debtor who was entitled to be a debtor under chapter 7, automatically qualified to be a debtor under chapter 11.76 Despite the

70. 774 F.2d 1073 (11th Cir. 1985); see infra notes 119-35 and accompanying text.
72. *Id.* at 2199.
73. *Toibb*, 111 S. Ct. at 2200. *But see* Public Citizen v. United State Dept. of Justice, 491 U.S. 440 (1989) (despite the acknowledgement of the plain meaning rule, the Court held that “where the literal reading of a statutory term would 'compel an odd result' we must search for other evidence of congressional intent to lend the term its proper scope.” *Id.* at 454 (quoting Green v. Bock Laundry Machine Co., 490 U.S. 504, 509 (1989)).
74. “Only a person that may be a debtor under Chapter 7 of this title, except a stockbroker or a commodity broker, and a railroad may be a debtor under Chapter 11 of this title.” 11 U.S.C. § 109(d) (1988).
76. 11 U.S.C. § 109(d) (1988). Also § 109(b) set out who can be a debtor under chapter 7: “A person may be a debtor under Chapter 7 of this title only if such person is not — (1) a railroad; (2) a domestic insurance company, bank, . . .; or (3) a foreign insurance company, bank, . . . engaged in such business in the United States.” 11 U.S.C. § 109(b) (1988).
enumerate list of exceptions, the Court stated that to exclude certain classes of individuals from chapter 11 would not make sense. Therefore, the Court concluded that since no ambiguities existed within section 109(d), a review of the legislative history was unnecessary.

This use of the plain meaning rule seems to more firmly entrench the doctrinal analysis purported by Justice Scalia, that the Court's "only legitimate source for interpretive guidance is the statutory text at issue, the structure of the statute as a whole, or other related provisions of statutory law." However, since there are conflicting "rules" of statutory interpretation, to ignore the vast amount of legislative history to the contrary is an injustice. Moreover, the Court's unwillingness to use legislative history to supplement statutory interpretation leaves Congress with the excessive burden of finding language that means the exact same thing to millions of people. Therefore, until the Court creates a definitive set of rules on how to interpret statutes, legislative history, especially in a case such as Toibb where it overwhelmingly contradicts the "plain meaning," should be considered in the statutory interpretation.

The Court, despite its acceptance of the plain meaning surrounding section 109(d), indicated that even if it were to consider the legislative comments to exclude consumer debtors from chapter 11, the Court maintained that the remarks did not suggest a clear legislative intent contrary to the plain language. The Court pointed to

77. The only exceptions listed under § 109(d) are stockbrokers, commodity brokers and railroads. 11 U.S.C. § 109(d) (1988).
78. Toibb, 111 S. Ct. at 2199.
79. Toibb, 111 S. Ct. at 2200. However, Justice Stevens in the dissent felt that the word "only" within § 109(d) provided the ambiguity necessary to explore the legislative history. Id. at 2202 (Stevens, J., dissenting). For a discussion about the abolition of the plain meaning rule in the courts, see W. David Slawson, Legislative History & the Need to Bring Statutory Interpretation Under the Rule of Law, 44 Stan. L. Rev. 383, 413 (1992).
81. See generally Slawson, supra note 82 (discussing the reasons why statutory interpretation should come under rules of law).
82. The Justices on the Supreme Court still conflict as to the importance of legislative history in statutory interpretation. For example, in Wisconsin Public Intervenor v. Mortier, 111 S. Ct. 2476 (1991), a case decided only a week following Toibb, Justice White and Justice Scalia disagreed over the use of legislative history in statutory interpretation. See John Choon Yoo, Marshall's Plan: The Early Supreme Court & Statutory Interpretation, 101 Yale L.J. 1607 (1992).
83. Toibb, 111 S. Ct. at 2200. The Court inferred that the legislative history
the presence of contradictory statements from House and Senate reports, but failed to read the reports in context.14

The Court then rejected the contention that since other Code provisions within chapter 11 were geared toward businesses, the relief should only be available to businesses.5 The Court did acknowledge Code provisions directed toward business entities,8 6 but suggested that these provisions, although having a business overtone, were not sufficient in themselves to restrict chapter 11 eligibility beyond the requirements of section 109(d).87

Furthermore, the policy arguments set forth by the amicus curiae, suggesting that chapter 11 was prohibited to consumer debtors, did not persuade the Supreme Court88 for several reasons. First, the Court held that chapter 11’s purpose was not solely to rehabilitate and revitalize businesses to preserve and protect investors.89 Second, the

pertaining to this issue was sparse. But cf. Wamsganz v. Boatmen’s Bank of De Soto, 804 F.2d 503 (8th Cir. 1986) (noting that the legislative history strongly supported the proposition that chapter 11 was not applicable to consumer debtors).

84. Toibb, 111 S. Ct. at 2200. A question could be raised as to whether the statements suggested by the Court were contradictory. The House report indicated that if consumer debtors would not have received relief under chapter 13, then the only remedy would have been a straight liquidation. H.R. Rep. No. 595, 95th Cong., 1st Sess. 125 (1977), reprinted in 1978 U.S.C.C.A.N. 5787, 5795. Then the Court relied on a portion of the Senate report which stated: “Chapter 11, Reorganization, is primarily designed for businesses, although individuals are eligible for relief under the Chapter. The procedures of Chapter 11, however, are sufficiently complex that they will be used only in a business case and not in the consumer context.” S. Rep. No. 989, 95th Cong., 2d Sess. 3 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5789. The contradiction appeared when the Senate report mentioned that chapter 11 could have been used by individuals. However, when reading the Senate report in context, it was important to note the second sentence which stated that chapter 11 was available to consumers, however it would only have been used in a business case. This viewpoint was strengthened when the dissent in Toibb pointed to the House report which “unambiguously states that a Chapter 7 liquidation is ‘the only remedy’ for ‘consumer debtors’ [who] are unable to avail themselves of the relief provided under Chapter 13.” Toibb v. Radloff, 111 S. Ct. 2197, 2203 (1991) (Stevens, J., dissenting).

85. Toibb, 111 S. Ct. at 2200.

86. Id. The two Code sections cited were 11 U.S.C. § 1102 (1988), which authorized the appointment of an equity security holders’ committee, and § 1104(a)(1), which permitted the appointment of a trustee if mismanagement of the affairs of the debtor occurs by current management. Id.

87. Id. at 2200.


89. Toibb, 111 S. Ct. at 2201. The Court noted one of the general purposes
Court did not agree that "allowing a consumer debtor to proceed under chapter 11 would permit debtors to shield both disposable income and non-exempt personal property." Third, the Court rejected as an unfounded fear that opening chapter 11 to consumer debtors would flood the courts with unworkable plans, reasoning that the cost and complexity alone would dissuade most consumers from using this section, and stated that courts already had the power under chapter 11 to dismiss unwarranted petitions. The Court also found that chapter 11 provided no increased threat of involuntary bankruptcy by the creditor of a consumer debtor, because the plan from either side must have the cooperation of the debtor. To force a debtor to work for the benefit of the creditors would have been an impermissible violation of the involuntary servitude provision of the Thirteenth Amendment.

The preceding rationale led the Court to provide the consumer debtor with the additional option of filing under chapter 11. This freedom of choice resulting from the *Toibb* decision conflicts not only behind the Code was to maximize the value of the bankruptcy estate. In certain circumstances a chapter 11 reorganization brought more value to the estate than a chapter 7 liquidation.

90. *Id.* at 2200-01. The Court held that despite legislative history stressing that protection provided under chapter 13 and chapter 7 should not extend by filing under chapter 11, the plain language of § 109(d) superseded the legislative intent and permitted consumer debtors to file under chapter 11. Moreover, it also reflected Congress's acknowledgement that different approaches to a variety of reliefs under the Bankruptcy Code were available.

91. *Id.* at 2201. The Court takes a very limited view of this situation. The *Toibb* ruling did not indicate that consumer debtors would provide a successful chapter 11 proceeding. The Court should have looked beyond the cost barriers and considered the number of people who should liquidate because they do not have the funds to effectuate a plan; or those who have excessive mortgages and will attempt this option instead of none at all. This is where the false start commences, and courts should be ready to handle an increased number of cases that were misguided into chapter 11.

92. *Id.*

93. *Id.* at 2202.

94. *Id.* at 2201. Although not discussed by amicus, a related issue that the Court addressed was the creditor's position in a consumer debtor chapter 11 filing. The Court indicated that creditors would not be negatively affected, because the creditor's power to reject the debtor's plan insured that the creditors would receive their sought after compensation. *Id.* Interestingly, the *Toibb* court adopts the same reasoning that has been used to bar involuntary petitions in chapter 13. See supra note 26. Therefore, the Court appears to want to give the consumer debtor the protections of chapter 13, and the benefits of chapter 11, which would go against the goal of equitable distribution for the creditor.
with the legislative history stressing the business character of chapter 11, but also with the consumer debtor’s desire to not be caught in a web of potential disillusionment, where only a false start will be granted.

III. IMPLICATIONS OF TOIBB: A TRAP FOR THE UNWARY

The Commission Report for the Bankruptcy Reform Act of 1978,95 reiterated two of the internal goals of the bankruptcy process as a fresh start for debtors and equality of distribution among creditors.96 In Toibb v. Radloff, the door was opened to another avenue of relief for the consumer debtor. However, this new avenue became an unrealized danger, because many consumer debtors shouldered the expense of a chapter 11, only to learn that eligibility for chapter 11 hardly secured a successful proceeding and a fresh start.

Moreover, the relationship between the consumer debtor and the creditor has been altered. The Toibb ruling placed an increased burden on the pursuit of the goal of equitable distribution for the creditor. The following relevant case law and concepts present the potential scenarios that strengthen the proposition that changes to the Bankruptcy Code are necessary, because the Toibb ruling created a trap for the unwary consumer debtor whose pursuit for a fresh start will likely become a false start if pursued under chapter 11.

A. DEBTORS WILL NOT RECEIVE A FRESH START UNDER CHAPTER 11

The consumer debtor has to overcome a considerable number of hurdles to achieve a successful fresh start. Bankruptcy concepts such as cause,97 conversion to chapter 7 liquidation98 or a chapter 11 liquidation99 could block the consumer debtor’s passage to a brighter future. Moreover, upon commencing a chapter 11 proceeding, the consumer debtor could experience the danger of finding foreclosure on a residence permissible because the residence was not necessary for an effective chapter 11 reorganization. In addition, the issues of the pro se debtor and the involuntary petition emerge as other

96. REPORT ON THE COMM’N ON THE BANKRUPTCY LAWS OF THE U.S., H.R. Doc. No. 137, pt. 1, 93d Cong., 1st Sess. 75 (1973), reprinted in COLLIER ON BANKRUPTCY (App. 2) [hereinafter COMM’N REPORT]. A third internal goal was the economical administration of the entire bankruptcy process.
97. “Cause” or “good faith” are interrelated concepts which permit the court to dismiss or convert a chapter 11 petition under 11 U.S.C. § 1112(b). See infra notes 103-18 and accompanying text.
99. Id. § 1123(b)(4).
potential problems created by the availability of chapter 11 to the consumer debtor.

1. Circumvention of Eligibility Through the "Good Faith" Doctrine: A "Cause" for Alarm

Chapter 11's cause provision permits courts to circumvent the eligibility issue surrounding section 109 and to dismiss a consumer debtor's petition for cause. Since courts have used cause in cases both where eligibility was and was not an issue, this strengthens the proposition, that cause can override eligibility concerns.

The debtor in First Jersey National Bank v. Brown, a housewife who co-owned three parcels of land, filed under chapter 11 with the purpose of stopping foreclosure proceedings against the property. In dismissing the petition because the debtor was not engaged in business, the court went beyond the issue of eligibility and addressed whether the court had the power to dismiss the case for cause even if individuals were allowed to file under chapter 11.

100. The eligibility issue essentially being whether consumer debtors are considered debtors for chapter 11 based on the eligibility provision § 109(d).

101. See supra notes 33-35 and accompanying text for general discussion about cause; See infra note 110 for a list of factors that would permit a court to dismiss for cause under chapter 11.

102. 127 B.R. 108 (Bankr. D.N.J. 1991). Brown was only one of several cases that addressed the issue of good faith as a subset of eligibility. Cf. In re Lange, 75 B.R. 154 (Bankr. N.D. Ohio 1987) (addressing the issue of eligibility not in terms of § 109(d), but using the criteria that no ongoing business was a sufficient reason to dismiss for lack of good faith); In re Bendig, 74 B.R. 47 (Bankr. D. Conn. 1987) (noting that a residence to save, when a lack of engagement in business was present, was not sufficient to stop a chapter 11 dismissal). But see In re McStay, 82 B.R. 763 (Bankr. E.D. Pa. 1988) (holding that when the sole reason for filing was to frustrate creditors, and the debtors although permitted to file under chapter 11 had no ongoing business, a lack of good faith was presumed).

103. Brown, 127 B.R. at 110. Three parcels of land were mortgaged so the debtor could obtain additional financing for a corporation in which she was a principal. It was not until the corporation failed and the liquidation of the assets were insufficient, that the bank tried to foreclose on the debtor's property. Id.

104. Id. at 113-15. In making this determination, the court reviewed In re Moog, 774 F.2d 1073 (11th Cir. 1985), but it relied on the precedents of In re Little Creek Dev. Co., 779 F.2d 1068 (5th Cir. 1986), In re Winshall Settlor's Trust, 758 F.2d 1136 (6th Cir. 1985), and Wamsganz v. Boatmen's Bank of De Soto, 804 F.2d 503 (8th Cir. 1986), in concluding that individuals not engaged in business were precluded from filing under chapter 11. Brown, 127 B.R. at 113.

105. For example, lack of good faith in filing a petition would have given the court sufficient cause to dismiss.

106. Brown, 127 B.R. at 113. A case could be dismissed for cause if a debtor
When reviewing the issue of cause, the court noted that section 1112(b) of the Code provided several factors in determining cause. The court's inquiry in cause analysis, specifically addressed lack of good faith by determining "whether there was a need and realistic ability to effectuate a reorganization." This inquiry revolved around the business nature of chapter 11 because the court equated the realistic ability to effectuate a reorganization with "whether there is a going concern to preserve and whether there is the possibility that the debtor 'will emerge from the chapter 11 proceeding in a rehabilitated condition — that is, ready to carry on with viable business operations.' The court concluded that the debtor was not an ongoing concern with employees, but rather an individual with no cash flow and a dispute with creditors. Therefore, the court would have been correct to dismiss for cause, because there was no ongoing business requirement even if eligibility under chapter 11 was not an issue.

Other courts have prevented individuals from successfully reorganizing under chapter 11 by finding that good faith was lacking. For example, the bankruptcy court in Florida addressed this issue in In re Bock. In Bock, the debtor had no business, no income and the sole asset consisted of an alleged claim against a former employer. The

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106. Brown, 127 B.R. at 113. A case could be dismissed for cause if a debtor could not effectuate a reorganization plan pursuant to § 1112(b). Therefore, the Toibb ruling could be considered meaningless, since the court still had another method to prevent consumer debtors from receiving relief from chapter 11.

107. Id. at 112. The Brown court also noted that the list is not exhaustive because Congress's purpose in not limiting the list to those 10 factors was to provide the court with the discretion to consider other factors that could arise under different circumstances. Id. The 10 factors listed under § 1112(b) are as follows:

1. continuing loss to or diminution of the estate and absence of a reasonable likelihood of rehabilitation; 2. inability to effectuate a plan; 3. unreasonable delay by the debtor that is prejudicial to creditors; 4. failure to propose a plan under section 1121 of this title within any time fixed by the court; 5. denial of confirmation of every proposed plan and denial of a request made for additional time for filing another plan or a modification of a plan; 6. revocation of an order of confirmation under section 1144 of this title, and denial of confirmation of another plan or a modified plan under section 1129 of this title; 7. inability to effectuate substantial consummation of a confirmed plan; 8. material default by the debtor with respect to a confirmed plan; 9. termination of a plan by reason of the occurrence of a condition specified in the plan; or 10. nonpayment of any fees or charges required under chapter 123 of title 28.


109. Id. (quoting Carolin Corp. v. Miller, 886 F.2d 693, 701-02 (4th Cir. 1989)).

110. Id. at 114-15.


court acknowledged that individuals were allowed to file under chapter 11, but also stated that in determining good faith, the "fact that an individual debtor is not engaged in business is certainly a relevant factor to be considered when his or her right to maintain a chapter 11 is challenged." In evaluating the debtor's situation, the court concluded that the debtor could not have effectuated a reorganization under chapter 11; thus, the court was correct in dismissing the case for cause.

Evidence of the courts' use of cause indicates that the ongoing business requirement for chapter 11 might still be present. Since the Toibb ruling specifically dealt with the eligibility requirement under section 109(d), and did not address cause, courts will have a loophole to dismiss the consumer debtor's petition under chapter 11. Courts can look to precedent stating that since there is no ongoing business, the petition will be dismissed for having no means to effectuate a reorganization. Therefore, instead of eligibility being a barrier to chapter 11, it provided the consumer debtor with the deceptive entrance into a chapter that would later become restricted.

2. A Home to Save: Will Chapter 11 Provide the Sought-After Relief or is it Only an Illusion?

Chapter 13 has been known as the chapter to use when trying to save a home, so it was unusual for a consumer debtor to pursue the same result through chapter 11. Nevertheless, In re Moog involved a chapter 11 filing by a housewife with no regular income and a home subject to three mortgages. The case was filed under chapter 11 because no other chapters were available to her that would allow her to keep her home.

113. Id. at 378. The court appeared to be leaving itself broad discretion to determine whether or not the debtor should be permitted the relief sought. On one hand, the court purported to give the debtor the opportunity to seek rehabilitation under chapter 11, yet the court subjectively decided based on the facts of the case, whether the debtor should obtain that relief.
114. See supra note 77 and accompanying text for the Code provision which dealt with eligibility.
115. See supra notes 103-18 and accompanying text for a discussion of cause. When dismissing the petition, courts did not consider the amount of money expended by the consumer debtor on attorney's fees and other court costs, in some cases just to try to save a home.
117. In re Moog, 774 F.2d 1073 (11th Cir. 1985).
118. Id. at 1074.
119. Id. at 1075. The debtor was precluded from using chapter 13 because she had no regular income, and chapter 7 would force her to liquidate her home.
In concluding that chapter 11 was available to the debtor, the Eleventh Circuit reviewed the legislative history, the Code, and the prior Bankruptcy Act. The court began by stating that section 109 did not expressly preclude consumer debtors from eligibility under chapter 11. Although legislative history suggested chapter 11 was better used by businesses, the court noted that consumer debtors might be compelled to use this remedy under certain circumstances. The court further noted that under the previous Bankruptcy Act, consumer debtors did have an option for relief in a chapter that was eventually consolidated into the present chapter 11. Lastly, the court held that bankruptcy rule 1007(b) acknowledged chapter 11 use by consumer debtors, so it was evident that relief for them was available under this chapter. For all the foregoing reasons the Eleventh Circuit concluded that consumer debtors should not be barred from eligibility under chapter 11.

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120. Id.
121. See supra note 77 and accompanying text for the Code provision which dealt with eligibility.
122. Moog, 774 F.2d at 1074.
123. Id. at 1074-75. The court inferred that certain special circumstances, such as a consumer debtor with no regular source of income, should be allowed to turn to chapter 11 for relief, otherwise the home would be lost to liquidation. However, this stance by the court was almost contradictory. On one hand, the court permitted the debtor who had no regular source of income to file a chapter 11 which required regular plan payments. On the other hand, the court also inferred that a consumer debtor should only be permitted to file a chapter 11 under special circumstances, like not having a regular source of income. This raised the question of whether there was income to fund the plan in the first place.
124. See supra note 15 and accompanying text.
125. Moog, 774 F.2d at 1075. Chapter 11 was a consolidation of chapters X, XI and XII. The consumer debtor could obtain relief under chapter XII of the previous Bankruptcy Act. Id.
127. Moog, 774 F.2d at 1075. The court only pointed to one rule provision to support this proposition. The court stated that under Fed. R. Bankr. P. 1007(b), the debtor in a chapter 7 or chapter 11 case shall file a specific statement of financial affairs depending on whether the debtor was engaged in business. Therefore, the court maintained that this rule provision provided sufficient support to conclude that the consumer debtor could file under chapter 11.
128. Id. at 1074. Cases of similar factual circumstances had parallel outcomes. See In re Warner, 30 B.R. 528 (Bankr. 9th Cir. 1983) (holding that the debtors were qualified to be chapter 11 debtors under § 109(d)); In re Bock, 58 B.R. 374 (Bankr. M.D. Fla. 1986) (holding that where debtor had no business or assets, just a possible claim from a lawsuit, was still eligible under chapter 11); In re Martin-Amirault, 115 B.R. 10 (Bankr. D.N.H. 1990) (holding that the debtor who had no regular income and a house to save was eligible under chapter 11).
Interestingly, the court neglected to address whether the case could be dismissed for cause. The court permitted a consumer debtor who had no visible regular source of income to proceed under chapter 11, without questioning how this debtor could effectuate a reorganization. Moreover, since the chapter 11 petition had not been filed, the court decided that the issue of whether the petition would eventually be dismissed was not appropriate.

The Moog case did not result in a dismissal, but even worse, the case was converted into a chapter 7 liquidation. Such a result clearly shows how the consumer debtor's reliance on chapter 11 can easily turn into disillusionment.

Like Moog, the efforts of homeowners were also frustrated in In re Wilks. This was another case where the debtors' primary objective in filing under chapter 11 was to save their home. However, unlike Moog, where the case was eventually converted to a chapter 7, the debtors in Wilks had their efforts thwarted when the court granted a motion to lift stay permitting foreclosure on their home.

129. See supra notes 103-18 and accompanying text for a discussion about cause.

130. The debtors' counsel indicated that the debtor only had a "source of periodic income that might be sufficient to maintain a Chapter 11 reorganization plan." Moog, 774 F.2d at 1075 (emphasis added). The debtors' periodic source of income raised the question as to how someone with only sporadic influxes of income was supposed to keep a $160,000.00 mortgage current.

131. Moog, 774 F.2d at 1077 (Hill, J., concurring). The court could not look at the issue of good faith, unless the petition was filed. However, Judge Hill indicated that this case was not appropriate for a chapter 11 and was an imposition on the bankruptcy court.

132. The information stating that the case was converted to chapter 7 would be contained in case file number 84-03248, on file with the Federal Records Center in Georgia. Furthermore, even if the court had decided not to convert the case to a chapter 7, another danger would be a chapter 11 liquidation under 11 U.S.C. § 1123(b)(4). More specifically, § 1123(b)(4) provided that a chapter 11 plan might "provide for the sale of all or substantially all of the property of the estate, and the distribution of the proceeds of such sale among holders of claims or interests . . . ." Since creditor participation was more evident within a chapter 11, the creditors would have the opportunity to push for a liquidating plan. Therefore, the debtor could incur the expense of a chapter 11, only to end with the unanticipated relief of asset liquidation.


134. In re Wilks, 123 B.R. 555 (Bankr. W.D. Tex. 1991). The debtors' sole objective under the chapter 11 plan was to reduce the current lien amount on their home to the property's current market value. Id. This procedure is commonly known as lien stripping.

135. Id. at 562. The debtors in Wilks were eligible for chapter 13, yet they elected chapter 11 in order to lien strip, an option not available under chapter 13. Id. at 558-59.
Instead of examining the issue of cause, the Wilks court chose to examine the crucial issue of whether the consumer debtor's home was "such an integral asset to the estate that it [was] necessary for Debtor's effective reorganization." The court set out several factors in determining whether saving a home was sufficient to warrant a chapter 11 filing. Applying a number of the factors, the court concluded that the debtor's home was not essential for a reorganization. The court's rationale turned on whether the home was used or not used to produce income, and whether other suitable housing was available to the consumer debtors.

Furthermore, the court noted that chapter 13 was the chapter to choose when a debtor's primary reason for filing the petition was to save a home. In arriving at this conclusion the court examined the approach taken when the home was the sole motive for a chapter 13 reorganization. Since a primary purpose surrounding chapter 13 was to "allow wage earner, non-business debtors to retain their homes by curing defaults on their home mortgage debt," courts have been reluctant to grant a motion to lift a stay to foreclose if the reorganization plan feasibly showed full payment of the mortgage. Apparently, courts applied a different standard when examining whether

136. Id. at 558. Before examining this issue, the court did address the issue of eligibility under chapter 11, by setting out the same reasoning as was given in Moog as to why the debtors were eligible for chapter 11 relief. Id. at 557-58.

137. The factors included:
   (a) the nexus between the residence and the debtor's generation of income;
   (b) the supply of other suitable housing in the area; (c) the length of time the debtor had been in Chapter 11; (d) whether the residence is a financial burden to the debtor; (e) whether the Chapter 11 was filed solely to stay foreclosure of the home; or (f) whether there is some special reason or circumstance for the debtor to maintain ownership of the residence.
   Id. at 559.
138. Wilks, 123 B.R. at 561.
139. The Wilks court noted that "if no nexus exists between the home and any business operation to be reorganized, the home has been held not necessary for an effective reorganization." Id. at 559. The business character of this factor appeared to contradict the earlier expressed precept that consumer debtors were eligible to file under chapter 11. Instead, the statement further strengthened the proposition that chapter 11 should be reserved solely for businesses.
140. Id. at 561.
141. Id. "Congress intended Chapter 13 to be the primary tool of wage earners to save their homes." Id. at 562.
142. Id. at 561-62.
143. Wilks, 123 B.R. at 562. (citing In re Artishon, 39 B.R. 890 (Bankr. D. Minn. 1984)).
144. The Wilks court concluded that in determining whether a stay should be
a home was "necessary to an effective reorganization" in chapter 11 cases versus chapter 13 where saving the home was the favored outcome.145

Thus the Wilks court permitted the consumer debtor to utilize chapter 11, but the result of granting the relief from stay probably left the debtors discouraged and frustrated with the bankruptcy process supposedly designed to aid them. The Wilks case was dispositive of the fact that consumer debtors would rarely receive any type of relief from a chapter 11 proceeding. In this case, the very reason the debtors filed under chapter 11, to save their home, was deemed irrelevant.

Both Wilks and Moog further emphasized that the business purpose was relevant for a successful chapter 11 proceeding. Not only would cause be an efficient way to bar consumer debtors from the chapter 11 arena, but also conversion to chapter 7 and the courts’ ability to grant motions to lift stays were effective tools for the same outcome — not providing relief to consumer debtors under chapter 11.


The flexibility created in Toibb may have put the consumer debtor in another precarious position in relation to the creditor. The question could be raised as to whether the creditor could treat the consumer debtor as a proper chapter 11 entity.146 More specifically, since the consumer debtor was eligible for chapter 11 relief, the

lifted under chapter 11 rather than chapter 13, a much stricter standard would be applied to determine whether a home was essential to a successful reorganization. Id.

145. Id.; cf. Grundy Nat’l Bank v. Stiltner, 58 B.R. 593, 595 (Bankr. W.D. Va. 1986) (stating that the standard used in determining what was necessary for an effective reorganization in a chapter 11 filing where the property was used for business should be different when applied to the rehabilitative purpose of chapter 13); In re Thomas, 121 B.R. 94 (Bankr. N.D. Ala. 1990) (holding that a residence was considered essential to a successful reorganization when the debtor and her children lived in the home for a number of years). The applicable Code provision interpreted was § 362(d)(2)(B) which stated that a motion to lift stay would be granted if “such property [was] not necessary to an effective reorganization.” 11 U.S.C. § 362(d)(2)(B) (1988 & Supp. 1991).

146. See In re Canion, 129 B.R. 465, (Bankr. S.D. Tex. 1989). The court in Canion addressed the issue of what guidelines the court should follow when debtors who were barred from chapter 13 utilized chapter 11. The court stated that the “same rules that govern business debtors must also govern individual debtors.” Id. at 468-69.
creditor should also be permitted to force the consumer debtor into a chapter 11 proceeding.\(^\text{147}\) Presently, only one case, \textit{In re Amburgey}, stated that involuntary petitions would not be invoked against consumer debtors.\(^\text{148}\) The court indicated that ""[a]s a matter of policy, this court now determines that a bankruptcy court should not entertain involuntary petitions under chapter 11 against individuals who do not own a business or significant property which could be administered by a trustee.""\(^\text{149}\)

However, as the number of bankruptcies reach alarming rates — ""one in every 106 American households filed for bankruptcy in 1991""\(^\text{150}\) — creditors may lose their lackadaisical attitude of the past and aggressively participate in bankruptcy proceedings involving consumer debtors.\(^\text{151}\) If this becomes a trend, involuntary petitions may become a reality for a number of consumer debtors, and the protections of a chapter 13\(^\text{152}\) will become less effective, as more consumer debtors can be forced into a chapter 11.

Another cause for alarm involves the potential pro se debtor. Currently, pro se debtors who file under chapter 13 have not met with much success.\(^\text{153}\) Therefore, it is logical to assume that the pro se debtor who chooses a chapter 11 filing, which is more complicated, will meet with much less success and much more damage to his or her already precarious financial position.

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\(^{147}\) Under chapter 13 involuntary petitions are prohibited. 11 U.S.C. § 303(a) (1988).


\(^{149}\) \textit{Id.} at 774. This is a prime example of why there is a need for a Code revision. The bankruptcy courts at their discretion, appear to be changing the Code to accommodate debtors under chapter 11, without remembering that one of the goals of bankruptcy is equitable distribution to creditors.


\(^{151}\) As creditors begin to realize more of a loss from consumer debtors, they may pursue the involuntary petition in order to receive some type of relief, rather than wait and see if the consumer debtor chooses the bankruptcy process or worse becomes a judgment proof debtor.

\(^{152}\) Under chapter 13, the debtor has a higher probability of receiving plan confirmation, obtaining a broader discharge and being protected from involuntary petitions.

\(^{153}\) For example, in the District of New Hampshire in 1990, of the 22 pro se debtors who filed under chapter 13, only one received a discharge, 15 were dismissed and six were still open. In 1991, of the 13 that filed under chapter 13, six were still open and seven were dismissed. U.S. Bankruptcy Court, District of New Hampshire, July 1992.
The preceding reasons help support the rationale that a fresh start for consumer debtors is illusory through the use of chapter 11. Even though there is evidence that the cost and complexity behind a chapter 11 filing will discourage many debtors from using that remedy, others will initially turn to it if their amount of debt bars them from the most suitable remedy. These consumer debtors approach a chapter 11 as their only hope of saving their homes, yet fall into a situation where the chapter 11 proceeding turns into an unnecessary burden, more often considered a false start.

B. CREDITORS AFTER TOIBB: WHAT HAPPENS?

Not only are consumer debtors detrimentally affected by the Toibb decision, but creditors are now in danger of receiving less of a payment. "When a consumer [debtor] uses chapter 11 rather than chapter 13, the creditors lose the ability to force the debtor to pay over his disposable income merely by objecting to the confirmation of the plan." The consumer debtor now, at the most, only has to make payments over the life of the plan. Therefore, the danger is that the creditor under a chapter 11 will only receive the equivalent of what would have been generated by a chapter 7 liquidation. This example shows one way the creditor is disadvantaged by the Toibb ruling.

Furthermore, under chapter 11, a creditor will potentially receive considerably less, because consumer debtors can negotiate a plan to prevent paying over their future disposable income. Mortgage holders will be negatively affected in a chapter 11, because a debtor could modify the rights of secured creditors whose sole collateral is a principal residence.

155. For example, a consumer debtor who has unsecured debt of $100,500 will be barred from a chapter 13. If this consumer debtor does not want to choose the prudent option of liquidating, the only option available is chapter 11.
156. 11 U.S.C. § 1325(b)(1)(B) (1988); see also Michael J. Herbert, Consumer Chapter 11 Proceedings: Abuse or Alternative?, 91 COM. L.J. 234, 246 (1986). Essentially, the debtor will end up paying less to creditors. Id.
157. 11 U.S.C. § 1129(a)(7)(A)(ii) (1988). Even though this concept was similarly shared in chapter 13, a restriction occurred because if a creditor objected to the plan, the debtor had to commit their future disposable income to the plan.
158. See Toibb v. Radloff, 111 S. Ct. 2197, 2204 (Stevens, J., dissenting).
159. Herbert, supra note 159, at 244. This was unlike a chapter 13, where if one creditor objected to the plan, the consumer debtor's future income practically guaranteed the creditor an equitable distribution.
Since there was no time limit on a chapter 11 plan, not only would the creditor receive less, but it would take longer for the creditor to receive less. The dissent in Toibb pointed out that the creditor could be adversely affected because “it takes time and money to determine whether a plan will provide creditors with benefits equal to those available through liquidation and still more time and money to find out whether such a predictive decision turns out to be correct or incorrect.” 161 Consequently, creditors would be compelled to aggressively pursue the consumer debtor, 162 increasing litigation costs until they were satisfied. Not only would the creditor be put at a disadvantage, but the creditor’s aggressive pursuit would undeniably make the debtor’s quest for a fresh start more difficult.

In order to conform to the internal goals of equitable distribution among creditors and a fresh start for debtors, as expressed in the Bankruptcy Commission Report, it is clearly necessary to review and revise the current provisions of the Bankruptcy Code. Not only will a revision address the needs of the consumer debtor, but the court system will also be relieved of the duty of turning away debtors who really need a fresh start.

IV. A RECOMMENDATION TO RENEW THE SPIRIT OF THE “FRESH START”

On November 19, 1991, the Senate introduced the Omnibus Bankruptcy Reform Legislation (“Bankruptcy Reform Legislation”). 163 Part of the purpose of the Bankruptcy Reform Legislation was to establish a “National Bankruptcy Review Commission (‘Commission’) to aid Congress in identifying and addressing problems

162. See supra notes 150-55 and accompanying text for a discussion of the involuntary petition.
163. OMNIBUS BANKRUPTCY REFORM LEGISLATION, S. Doc. No. 279, 102d Cong., 2d Sess. 25 (1992). Even though the legislation does contain an option for consumer debtors by expanding the debt limitation for chapter 13, the creation and importance of the Review Commission should not be overlooked. The number of bankruptcies have skyrocketed since the Commission was created for the Bankruptcy Reform Act of 1978. In the area of consumer bankruptcies, the statistics show that in 1946 there were 8566 non-business filings compared to 191,729 in 1967. COMM’N REPORT, supra note 99, at 33. For the 12-month period ended June 30, 1992, the total number of non-business filings was 899,840. DIRECTOR OF THE ADMIN. OFFICE OF U.S. COURTS, 1992 ANNUAL REPORT (Table F-2). It is through the proposed Review Commission that the problems for the consumer debtor, in relation to chapters 11 and 13, can be properly addressed.
found in the bankruptcy field." The bill was necessary because almost fifteen years had passed since the enactment of the Bankruptcy Reform Act of 1978, a sufficient number of years for the Code "to fully impress itself on bench, bar and citizenry." Not only did the bill suggest the creation of a Commission, it also proposed specific changes to chapter 13 to expand eligibility, by raising the debt limits of "those debtors who seek to use chapter 13 of the Code . . . ." Therefore, the bill could be viewed a necessary response to the unresolved issue of whether the consumer debtor should be permitted to file under chapter 11. The provisions contained within the bill provide a remedy for those consumer debtors who turn to chapter 11 because of the chapter 13 debt limitations.

The Bankruptcy Reform Legislation specifically proposed changes to the dollar limitations for secured and unsecured debt which forced many debtors to pursue chapter 11. The proposed changes are as follows: (1) raise the dollar limitation from $350,000 to $1,000,000; (2) remove distinctions regarding secured and unsecured debt; and (3) allow "a debtor to file a chapter 13 case with noncontingent, liquidated debts which are higher than $1,000,000." The Senate proposed these changes because it wanted to break down "unnecessary barriers," while providing flexibility to courts and debtors in choice of remedy.

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164. OMNIBUS BANKRUPTCY REFORM LEGISLATION, S. Doc. No. 279, 102d Cong., 2d Sess. 25 (1992). The establishment of the Commission would not only update the Code, but would also "provide a rational framework from which future changes may evolve." Id.


166. REHNQUIST SPEECH, supra note 153, at S7396. Chief Justice Rehnquist noted the following statistics in emphasizing the need for bankruptcy reform. "Since the implementation of the new Bankruptcy Code in 1979, over six million bankruptcy cases have been filed." Id. Moreover, in 1992, one million bankruptcy cases were expected to be filed, which is tremendous when only 250,000 civil cases and 50,000 criminal cases were estimated. Id.


168. Id. at 38.

169. Id.

170. Id.

171. Id. This loophole would provide consumer debtors with the ability to prove that chapter 13 was their best form of relief aside from the debt restrictions.

172. OMNIBUS BANKRUPTCY REFORM LEGISLATION, S. Doc. No. 279, 102d Cong., 2d Sess. 38 (1992). However, the issue of regular income had properly been left alone. Consumer debtors with lack of regular income should not be permitted to file under chapter 11. It is very difficult to envision a debtor with no regular income effectuating a successful reorganization. See supra note 133 and accompanying text.
This proposal suggested that Congress had recognized that the consumer debtor did not belong in chapter 11, but the limitations within chapter 13 gave him or her no other option. By raising the debt limitation to $1,000,000, consumer debtors, specifically those wishing to save their homes, would now have a reasonable option for relief under chapter 13.\footnote{173}

The Committee's proposal to change the eligibility requirements supports the theory that chapter 11 only benefits the business debtor. Further evidence was the Committee's proposal to "create a pilot program in eight judicial districts to provide an expedited method for reorganizing small businesses."\footnote{174} The Committee pointed out that current chapter 11 filings ranged from the large corporate entity down to the small mom-and-pop grocery store.\footnote{175} The Committee was concerned about the uniform application of chapter 11 upon these two distinct entities as only creating "problems and inefficiencies in the handling of individual bankruptcy cases."\footnote{176}

Ironically, the legislature expressed concern about the suitability of chapter 11 for small businesses, yet the Toibb ruling made chapter 11 available to the consumer debtor. If the uniform application of chapter 11 on small businesses creates problems and inefficiencies, it is logical to conclude that a consumer debtor will experience similar, if not greater, problems and create more inefficiencies for the bankruptcy court system.

The Committee should enact the Bankruptcy Reform Legislation in order to clarify the purpose behind chapter 11.\footnote{177} Even though the Toibb ruling states that the consumer debtor should not be barred from seeking relief under chapter 11, a tremendous amount of evidence still suggests that chapter 11 is a business reorganization chapter. Moreover, since section 109(d) does not specifically state that consumer debtors are not barred from chapter 11, this could mean "that Congress never seriously considered the hypothetical of a consumer

\footnote{173}{The proposed legislation is only one option. Another option would be to have the consumer debtor sell the encumbered home and move into a less expensive home. This would also provide the consumer debtor with a more manageable debt structure.}


\footnote{175}{\textit{Id.}}

\footnote{176}{\textit{Id.}}

\footnote{177}{The bill also wants to experiment with a separate method of reorganizing small businesses. \textit{Omni}}\textbf{bus Bankruptcy Reform Legislation}, S. Doc. No. 279, 102d Cong., 2d Sess. 26 (1992). This is another indication that there is a belief that chapter 11 should be reserved solely for businesses.
chapter 11, and thus never even thought about extending or restricting its availability to non-business debtors." 178

Currently, the Bankruptcy Reform Legislation met with the obstacle of an election year combined with the end of a congressional session. However, upon the reintroduction and reconsideration of legislation reforming the Bankruptcy Code,179 the Committee should strongly consider the following suggestion. An amendment to the eligibility provision should be devised stating that chapter 11 is unavailable to those consumer debtors not engaged in purposeful business activities. This amendment will not only rectify the Toibb decision, but also provide uncontradictory authority emphasizing the business nature of chapter 11.

The legislative solution will provide the flexibility to the consumer debtor who was ineligible due to the dollar limitation under the current chapter 13. However, it must be noted that increasing the debt limitation may only be an equitable solution for certain debtors. For example, a plan to restructure a million dollars of debt over a three-year period could be infeasible. Although harsh, the other solution would be to leave the limitations within chapter 13 the same, and inform the consumer debtor that their only option is a chapter 7 liquidation.180

Sufficient evidence exists both within the case law and the proposed Bankruptcy Reform Legislation to state that chapter 11 is a business chapter and there is no room for the consumer debtor. Both the proposed expansion of the dollar limits for eligibility and the creation of the small business chapter support this proposition. However, even these measures may not be enough to ensure the consumer debtor with a fresh start. Perhaps the only judicious option will be to liquidate under chapter 7. Together, these options will achieve the three internal goals of bankruptcy articulated in 1978 — fresh start, equitable distribution, and economical administration.

CONCLUSION

Even though the Toibb ruling permits the consumer debtor to file under chapter 11, the legislative history and case law reinforce

178. Herbert, supra note 158, at 238.
179. In a recent article from the American Bar Association, the authors stressed the need for bankruptcy reform, and that S-1985 will provide a “benchmark for an analysis of creative resolutions to problems presented under current law.” David F. Bantleon & Kathy L. Kresch, A Bankruptcy Law for the 90’s, BUS. LAW TODAY, Jan.-Feb. 1993, at 25-26.
180. Based on the treatment of consumer debtors within the chapter 11 arena, this option will avoid both the upfront costs of a chapter 11 and the intangible costs of a false start.
the proposition that the business purpose behind chapter 11 prevents the consumer debtor from receiving a fresh start. Moreover, courts are circumventing *Toibb* by finding reasons to dismiss or convert chapter 11 filings by consumer debtors. Support for this premise occurs when courts declare that trying to save a home that is not producing income is insufficient to effectuate a chapter 11 reorganization, or else dismissing the petition for cause because the ongoing business requirement has not been satisfied. Consequently, consumer debtors expend time and money to file under chapter 11 only to find that the court will dismiss for cause or convert to a chapter 7 liquidation.

The proposed Senate bill, which would create a Commission to review the current Code, and more specifically, alter the eligibility for chapter 13, could provide the necessary legislation to update the Code to better suit the needs of today’s consumer debtors, rather than those of the early 1980s. It must be remembered that the consumer debtors of the 1990s need a fresh start, not a false start.

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