Wage Earners' Plans: Chapter XIII

William E. McCarty

Follow this and additional works at: http://scholarship.law.marquette.edu/mulr

Part of the Law Commons

Repository Citation
Available at: http://scholarship.law.marquette.edu/mulr/vol45/iss4/9

This Article is brought to you for free and open access by the Journals at Marquette Law Scholarly Commons. It has been accepted for inclusion in Marquette Law Review by an authorized administrator of Marquette Law Scholarly Commons. For more information, please contact megan.obrien@marquette.edu.
WAGE EARNERS' PLANS—CHAPTER XIII

Recently there has arisen serious concern over the rising number of straight bankruptcy petitions. In the fiscal year 1952, total filings were 34,873. In 1958 this number rose to 91,668 and in 1960 there were 110,034 petitions filed. What is even more interesting is that in 1952, 81.3% of the total bankruptcy petitions filed were by non-traders. In 1960 this percentage rose to a startling 88.8%.

The tragic fact is that these non-trader cases are either no-asset cases or cases with such few assets as to provide no dividend whatsoever to their multitudinous creditors.

One of the possibilities suggested to stem this upward spiral is an increase in the use of Chapter XIII of the Bankruptcy Act, often referred to as Wage Earners' Plans. In essence, Chapter XIII provides a method whereby a debtor can pay his debts out of future earnings while at the same time he is being protected by the court from garnishments and wage attachments. The fact that Chapter XIII is desirous from the creditor's viewpoint is illustrated by the following:

The Committee called attention to the value of the proceedings under Chapter XIII as reflected in the amounts paid to creditor's in Chapter XIII cases and in no-asset straight bankruptcy cases. During the fiscal year 1960, the unpaid liabilities scheduled in the 63,086 straight bankruptcy cases closed during the year were $469,865,567. During the same period the debts affected in the 5,920 Chapter XIII cases completed were $5,277,737 of which $5,168,251, or 98 per cent, was paid to creditors.

Chapter XIII developed from section 74, enacted in 1933. Because of the inadequacies of section 74, the Chandler Act, in 1938, added Chapter XIII to its general revision of the then existing bankruptcy legislation.

In practice Chapter XIII has not been as popular as its originators had hoped, although statistics show its popularity is increasing. A total of 8,670 Chapter XIII petitions were filed during fiscal 1953. The Fifth Circuit, composed of Alabama, Florida, Georgia, Louisiana, Mississippi and Texas accounted for 6,955 of these. The entire Seventh Circuit accounted for only 15 of the 8,670. In 1958 this figure rose
to 13,391, with the Fifth Circuit accounting for 8,322, and the Seventh Circuit for 297. In 1960 the total number of wage earners’ petitions remained about the same except that the number of petitions in the Seventh Circuit almost doubled over that of 1958, namely from 297 to 532. Various reasons have been advanced why Chapter XIII has not found greater acceptance with members of the Bar, but that which is usually given the greatest weight is the failure of the Bar generally to make themselves acquainted with the advantages of using Chapter XIII in appropriate cases.

I. DISTINCTION BETWEEN COMPOSITION AND EXTENSION

As previously mentioned, Chapter XIII attempts to present an efficient and effective method by which persons dependent on wages can effectuate a settlement with their creditors, either by effectuating a composition with their creditors or getting an extension of time to pay their debts, the latter being the predominate choice. The distinction between a composition and an extension was clearly presented in In re Thompson wherein the court stated:

But it is evident that the statute intended a distinction between the terms ‘composition’ and ‘extension’; and that the difference is between a proceeding wherein a debtor settles his indebtedness in an agreed amount less than the amount owed and a proceeding wherein he merely obtains an extension of time within which to pay in full.

Once the choice is made between a “composition” or “extension,” great liberty is left to the drawer of the plan in regards to the terms thereof and the other specifics.

II. INDIVIDUALS AFFORDED RELIEF BY CHAPTER XIII

The use of Chapter XIII was originally limited to individuals whose wages did not exceed $3600. In 1950 this figure was raised to $5000 and in 1959 the definition of a wage earner was amended and presently reads “‘wage earner’ shall mean an individual whose principal income is derived from wages, salary or commissions.” Because of the great number of people earning over $5000 per year the proposers of the amendment felt that by eliminating this limitation the plan would be available to a greater number of people. In order to obtain the protection of the Act, the debtor must be “insolvent or unable to pay his debts as they mature” and also state that he desires

---

10 Annual Report, supra note 9, 1958, at 226-228.
11 ANNUAL REPORT, supra note 9, 1960, at 336.
13 Id. at 14.
to effect a composition or extension out of his future earnings. The debtor should file his original petition in the court which would have jurisdiction if the debtor were filing a straight bankruptcy petition. If a bankruptcy petition is pending and the debtor wishes to convert it to a Chapter XIII proceeding he has only to file a wage earner's petition in the same court that he filed the bankruptcy petition.

III. CLAIMS AFFECTED BY CHAPTER XIII

The plan filed by the debtor applies to all claims, whether "secured or unsecured, liquidated or unliquidated, fixed or contingent" except claims secured by estates in real property or chattels real. This section is of great importance to the debtor because combined with section 1014 it gives to the court the power to shield the debtor from garnishments or wage attachments. It is important to note that although the plan applies to all claims except those secured by estates in real property or chattels real, this concept must be distinguished from the claims actually involved in the plan. A creditor is affected by the plan if his interest will be materially and adversely affected by it.

IV. POWERS OF REFEREE

When the petition is originally filed with the district court, the clerk, unless the district judge directs otherwise, refers the petition to the referee in bankruptcy. Generally, bankruptcy courts possess powers of both law and equity. The referee possesses wide power over the wage earner's plan, the most important being control over the debtor's future earnings during the continuation of the plan. The referee also has "exclusive jurisdiction of the debtor and his property, wherever located," power to permit rejection of executory contracts; to enjoin the continuation of any suit and enjoin any proceeding to enforce a lien upon the property of a debtor, and to extend upon cause shown any time limit previously fixed. When these powers are considered in their totality it is easily seen that the

---

18 The Bankruptcy Act, 11 U.S.C. §1022 (1958). A person filing an ordinary bankruptcy petition files it in the court wherein the debtor has had his principal place of business, resided or been domiciled within the territorial jurisdiction of such court for a longer period of the preceding six months than in any other jurisdiction. The Bankruptcy Act, 11 U.S.C. §11 (1958).
receptiveness of the referees towards Chapter XIII proceedings can do much to further or restrict their popularity. The provisions of Chapters I to VII of the Bankruptcy Act apply to Chapter XIII proceedings insofar as they are not inconsistent with the provisions of the latter chapter. Also, because of the similarity between Chapters XI and XIII of the Bankruptcy Act, what the courts have said with respect to general bankruptcy provisions in Chapter XI proceedings furnish a guide as to the applicability of such provisions in Chapter XIII proceedings. Having stated that the debtor is insolvent, the petition should also contain a statement of the executory contracts of the debtor and the necessary schedules and statement of affairs, unless for some good reason it cannot be presently filed. In such case a debtor need only file a petition plus a list of his creditors and their addresses and a summary of his assets and liabilities and then ten days later file the schedules and statement of affairs. One leading authority suggests that this is one of the reasons why Chapter XIII is not used more often.

V. EFFECT OF FILING OF WAGE EARNER'S PETITION

There is no requirement that the debtor submit his plan when he files his petition, but by so doing the plan will be sent to the creditors before the first meeting of the latter and it has been suggested that to do so promotes the efficient operation of the chapter. When the petition is filed the debtor is required to pay $15 although it is payable in installments.

The effects of filing a Chapter XIII petition are important:

The filing of the Chapter XIII petition carries with it numerous important consequences. One is that a constructive adjudication in bankruptcy results, with these effects, (1) it gives creditors and all other persons the same rights, duties and liabilities with respect to the debtor’s property that they would have after an adjudication in an ordinary proceeding; (2) it gives the officers of the court the same rights, duties and powers, and gives the debtor the same rights, privileges and duties that both possess after an adjudication in an ordinary bankruptcy proceeding and (3) it gives the court the same jurisdiction, powers and duties

30 27 Ref. J. 69 (1953).
34 Supra note 8, at 424. "In other words, an original Chapter XIII petition entails all the clerical work and providing of copies of documents incident to a voluntary bankruptcy petition, which explains, without need for further comment, why embarrassed debtors and their attorneys have shown so little enthusiasm about the relief munificently tendered under Chapter XIII, notwithstanding the bargain filing fees.” Cf., 28 Kan. B. J. 165, at 169 (1959).
35 26 Minn. L. Rev. 775 (1942).
that the court possesses after an ordinary bankruptcy adjudications, which includes exclusive jurisdiction of the debtor and his property, where ever located, and of his earnings and wages in the period during the filing of the petition and confirmation of the plan.

Another consequence is that upon the filing of a Chapter XIII petition section 614 confers injunctive relief in two broad situations: (1) the court may, without giving notice, enjoin or stay the commencement or continuation of suits other than suits to enforce liens on the debtor's property, until a final decree is entered, and (2) the court may, upon notice and for cause shown, enjoin until final decree any act or the commencement or continuation of any proceeding to enforce a lien upon the debtor's property. . . . 37

VI. CONTENTS OF PLAN

The provisions of the Chapter itself do not provide any specific guides to determine what the actual contents of the plan should be. On the contrary, section 104638 lays out only general guides:

A plan under this chapter —

(1) shall include provision dealing with unsecured debts generally, upon any terms;

(2) may include provisions dealing with secured debts severally, upon any terms;

(3) may provide for priority of payment during the period of extension as between the secured and unsecured debts affected by the plan;

(4) shall include provisions for the submission of future earnings or wages of the debtor to the supervision and control of the court for the purpose of enforcing the plan;

(5) shall provide that the court may from time to time during the period of extension increase or reduce the amount of any of the installment payments provided by the plan, or extend or shorten the time for any such payments, where it shall be made to appear, after hearing upon such notice as the court may designate, that the circumstances of the debtor so require;

(6) may include provisions for the rejection of executory contracts of the debtor; and

(7) may include any other appropriate provisions not inconsistent with this chapter.

It can readily be seen that three of these provisions are mandatory and four are optional. The first mandatory provision is that unsecured debts must be dealt with generally, on any terms. What this means is that a wage earner's plan must "(a) encompass all and not less than all his unsecured creditors, and (b) treat them generally, in one and only one class, as a group and on an equal basis. All must be

treated proratably and alike. Obviously the drawer of the plan possesses a large degree of discretion as to how the unsecured creditors will be dealt with. However, two points to keep in mind are (1) that the plan will have to be approved by the requisite number of creditors and (2) that the plan will have to be in the best interests of creditors and also feasible. The second mandatory provision of section 1046 is that the debtor must submit his future earnings or wages to the control of the court. The third mandatory provision is that the plan must give to the court the power to raise or lower the amount of any installment payments. This provision can work to the benefit of either the debtor or his creditors, depending on the particular facts. If the debtor incurs unexpected sickness or job lay-off, he can apply to the court for a reduction in payments. If the debtor's financial condition improves unexpectedly, his creditors can use this provision to increase the installments provided for by the plan. In both instances either the debtor or creditor must petition the court for the relief desired.

Probably the most important optional provision in the plan is that dealing with secured creditors. A plan cannot deal with debts secured by estates in real property or by chattels real, but can deal with debts otherwise secured. The position of a secured creditor dealt with by a wage earners' plan is rather unique. A secured creditor cannot be dealt with by the plan unless he consents to it. If he does consent, he must be dealt with individually and not as a member of a class. But the real problem when speaking of secured creditors under a Chapter XIII petition is not how the consenting secured creditors will be dealt with but rather how the non-consenting secured creditors will be handled. In re Duncan held that where the debtor had a substantial equity in a refrigerator and the secured creditor had acquiesced in previous defaults and the debtor was able to pay the original monthly installments, the referee in bankruptcy had a right to deny the reclamation petition of the secured creditor. Note the particular facts of the case: That the debtor had substantial equity, that the secured creditor had acquiesced and that the debtor could pay the original monthly installments under his plan. In 1960 the Circuit Court of Appeals for the Seventh Circuit, in In re Clevenger, held substantially

39 Nadler, the Law of Debtor Relief 532 (1954).
41 The Bankruptcy Act, 11 U.S.C. §1, (28), defines a secured creditor as a creditor "who has security for his debt upon the property of the bankrupt of a nature to be assignable under this Act or who owns such a debt for which such indorser, surety, or other person secondarily liable from the bankrupt has such security upon the bankrupt's assets."
43 In re Clevenger, 282 F. 2d 756 (7th Cir. 1960).
the same as the Duncan\textsuperscript{44} decision. In 1961, the District of Kansas\textsuperscript{45} held that a secured creditor who has elected to reject the plan can successfully oppose its confirmation although approved by the unsecured creditors, when the proposed plan provides for installment payments lesser in amount than the terms of the instrument creating the debt. The court stated:

It is my opinion that a plan proposed under Chapter XIII which does not provide for assumption of executory contracts by the trustees or otherwise make provision for the payment of the claims of secured creditors according to the terms of the instrument creating the debt, does deal with such claims. A plan without such provisions should not be confirmed unaccepted by the secured creditors.\textsuperscript{46} Note that the court concludes that the secured creditor is actually dealt with by the plan and therefore can object to its confirmation when the trustee does not assume executory contracts or when the plan does not provide for payments to the secured creditor in an amount at least as great as the original contract creating the debt. In his discussion of the rights of secured creditors under a Chapter XIII petition, Nadler says: "Their acceptance or rejection of the proposal does not affect its subsequent confirmation, although it is obvious that the rights of each secured creditor cannot be affected unless each of them is willing to agree thereto."\textsuperscript{47} Earlier in the same section he states that a secured creditor "cannot be compelled to accept any proposal that modifies or alters his position."\textsuperscript{48} Therefore, Nadler seems to reason that the secured creditors cannot be forced to accept any plan that modifies their position but that their rejection should not affect the subsequent ratification of the plan. However, this conflict becomes predominantly academic because it can be solved simply by providing that the plan provide monthly payments to the secured creditor in an amount equal to the original contract creating the debt. If the non-consenting secured creditor tries to foreclose his lien in the state court, the debtor can petition the bankruptcy court for an injunction prohibiting any further action by the creditor.\textsuperscript{49} The secured creditor could also file a reclamation petition in the bankruptcy court. It would seem that it should be denied where the debtor has a substantial equity in the property and also where it is in the best interests of the debtor, for example, where it is necessary for a debtor to have a car in order to retain his employment.

\textsuperscript{44} \textit{In re} Duncan, supra note 42.
\textsuperscript{46} \textit{Id.} at 391.
\textsuperscript{47} \textit{Id.} at 391.
\textsuperscript{48} \textit{Id.} at 391.
The second optional provision of the plan is that it may provide for priority between the secured and unsecured creditors. This section is realistic in that it allows the debtor to retain some of his encumbered chattels by providing larger installment payments to those secured creditors than to his general creditors. In Alabama, a state where Chapter XIII is used often, the usual practice is for the debtor to propose a periodic payment and leave the disposition of the payment to the referee's suggestions. The referee then calculates appropriate specific payments to secured creditors, with the balance of the periodic payments to go to the unsecured creditors.\textsuperscript{50}

The third optional provision of the plan is that it may include provisions for the rejection of executory contracts of the debtor. The importance of this provision should be emphasized. Nadler says:

Furthermore, and perhaps a most important provision of the law is the right given to the debtor to disaffirm and cancel all such executory contracts, chattel mortgages and conditional contracts on automobiles, appliances, jewelry, leases, etc., as have now become burdensome to the debtor, such creditors being relegated to unsecured creditors for such amount as the Court finds to be damages for the rejection of such executory agreements.\textsuperscript{51}

The final provision of section 1046 allows for any other provision not inconsistent with the chapter. "This 'catch-all' provision makes it possible for the debtor to tailor-make an arrangement that best suits his factual situation, so long as any of such proposals do not conflict with the purposes and provisions of Chapter XIII."\textsuperscript{52}

Another principle that should be kept in mind when drawing a Chapter XIII petition is that there is no statutory limitation as to the length of time that the plan can run. The only provision of the Act relating thereto is section 1061\textsuperscript{53} which provides that a debtor may be discharged three years after confirmation of the plan, even though not all debts have been paid, if the court is satisfied "that the failure of the debtor to complete his payments was due to circumstances for which he could not be justly held accountable. . . ." But as a result of this provision most plans are set up so that they will be completed in approximately three years.

\textbf{VII. THE MEETING OF CREDITORS}

After the petition has been referred to the referee, it is his duty to "promptly call a meeting of creditors, upon at least ten days notice by mail to the debtor and his creditors."\textsuperscript{54} As to the requirements of the notice, section 1015\textsuperscript{55} states:

\textsuperscript{50} 27 \textsc{Ref. J.} 68 (1943).
\textsuperscript{52} \textsc{Nadler, supra} note 39, at 537.
Whenever notice is to be given under this chapter the court shall designate, if not otherwise specified hereunder, the time within which, the persons to whom, and the form and manner in which the notice shall be given. Any notice to be given under this chapter may be combined, whenever feasible, with any other notice or notices under this chapter.

All notices required by this chapter may be given by mail, unless otherwise directed by the court.

The debtor may submit his plan at the first meeting of creditors or he may submit it when he files his petition. If he chooses to do the latter, the plan may be sent out with the notice to creditors. In such cases the debtor should submit a copy of the plan for each creditor, the district director of internal revenue for the district in which the court is located and three additional copies for the referee's files. It has been suggested that a copy of the plan be sent to the county treasurer and the state income tax department. The notice of the first meeting of creditors may also be accompanied by a temporary restraining order, a blank form of agreement to accept the plan and a blank form to be used in filing proofs of debt.

At the first meeting of creditors:

(1) the judge or referee shall preside, receive proofs of claim, and allow or disallow them, and examine the debtor or cause him to be examined and hear witnesses on any matter relevant to the proceeding.

Each creditor filing a claim has the burden of showing that such claim is free from usury as defined by the laws of the state where the debt was contracted. If any creditor waives his right to participate in the plan, the debtor must submit an affidavit stating the absence of any special inducements for the waiver.

Once the claims are allowed, and the plan is filed, the court shall receive the written acceptances of the creditors, which acceptances may be obtained before or after the filing of the wage earner's petition. Chapter XIII provides a choice of two methods by which a wage earners' petition may be accepted by the creditors involved. The first method is where the plan is unanimously accepted in writing by all creditors affected by it, whether or not their claims have been proved, if in the court's judgment the plan is made in good faith and without any means forbidden by the Act. Since unanimous consent is probably

---

58 26 Minn. L. Rev. 775 (1942).
59 Ibid.
rare, the Act provides an alternative plan of approval, namely ap-
proval by a majority in number of all unsecured creditors “whose
claims have been proved and allowed” before the conclusion of
the first meeting of creditors, “which number shall represent a majority
in amount of such claims, and by the secured creditors whose claims
are dealt with by the plan.” The operation of this section is illustrated
by the following:

Thus, the extreme importance of the filing and proving of
claims and of the filing of the written consents becomes ap-
parent since the fate of the plan depends not upon obtaining the
majority in number and amount of all the creditors of, and
scheduled by, the debtor but only upon obtaining the majority
in number and amount of such, and only such of the creditors
as have filed, proved and had allowed their respective claims
and have filed their written acceptances at any time up to the
concluded meeting of creditors. In other words, the computation
is made on the basis of those creditors who actually exercised
their right of franchise and not on the basis of those who have
but did not exercise this right of franchise. As a result thereof,
it generally can and does happen that the debtor can “put
through” his plan by the acceptances of much less than the
actual majority in number and amount of his affected creditors.
Thus, even though the debtor, for example, may schedule 50
affected creditors whose claims total $10,000 and only 5 of them
with claims totaling $3000 have filed their written acceptances
and have had their respective claims filed, proved and allowed at
the conclusion of the meeting of creditors or any adjournment
thereof, the debtors' plan has been “accepted” when not less than
3 of such 5 creditors have assented provided that the total
of such assenting claims is not less than $1500.01 of such
total of $3000.

VIII. FILING OF CLAIMS

Must a creditor file a claim within six months of the meeting of
creditors in order to be paid dividends from the trustee? The answer
to this question depends on whether section 57n of the Bankruptcy
Act is thought to be controlling. Most authorities hold that 57n is
applicable and that a claim must be filed for a creditor to participate
in dividends paid by the trustee. The District Court of Minnesota
reasoned that since 57n is made expressly applicable to Chapters X and
XII, it is reasonable to assume that if Congress had not intended 57n
to apply to Chapter XIII, it could have easily done so. In addition,

67 NADLER, supra note 39, at 507-508.
70 In re Heger, supra note 69.
the court lists a number of practical reasons for its holding: (1) In many instances the only records that show the balance owed by the debtor are those of the creditor; (2) requiring claims to be proved will help to eliminate trivial and nuisance claims; and (3) no undue hardship is placed on the creditor by requiring him to prove his claim.11 At the meeting of the National Bankruptcy Conference in November, 1958, the Drafting Committee was instructed to prepare the necessary amendment to Chapter XIII so as to specifically provide that 57n is applicable and that claims must be filed.7

However, if the plan is not confirmed and an order is entered that bankruptcy be proceeded with, a creditor who has not filed his claim has another opportunity to file his claim in the ensuing bankruptcy proceeding. He must do so within six months "from the date of mailing of notice to creditors of the entry of the order directing that bankruptcy be proceeded with; otherwise they (i.e. creditors) are 'out in the cold' for all purposes, similar to straight bankruptcy."73 However, there is no obligation on a creditor to file his claim a second time when it was first filed in an original bankruptcy that was subsequently converted to a Chapter XIII proceeding.74

IX. APPOINTMENT OF TRUSTEE

Once the plan is accepted by the requisite number of creditors, the court appoints a "trustee to receive and distribute, subject to the control of the court, all monies to be paid under the plan."75 The trustee of a wage earner's plan should not be confused with the traditional concepts of a trustee under a straight bankruptcy petition. His main function under a Chapter XIII proceeding is to act as a distributing agent. "He is appointed by the court and the creditors have no voice in his selection."76

However, the concept of a trustee of a Chapter XIII proceeding acting only as a distributing agent is not entirely accurate. In 1956 it was held that a Chapter XIII trustee has the rights of a lien creditor under section 70c of the Bankruptcy Act.77 In this case the bank was the owner of an installment note secured by a chattel mortgage on a television set. The mortgage was not filed and the debtor had waived his exemptions, thereby giving the court control over all his property. The bank did not consent to the Chapter XIII plan and sought to reclaim the television set, or to participate as a secured creditor. The bank conceded that in an ordinary bankruptcy pro-

71 Id. at 150-151.
73 Nadler, supra note 39, at 521.
74 Nadler, supra note 39, at 522.
76 Nadler, supra note 39, at 553.
77 City National Bank v. Oliver, 230 F. 2d 686 (10th Cir. 1956).
ceeding the trustee could have avoided the unrecorded chattel mortgage under section 70c of the Bankruptcy Act. It argued that since the purpose of Chapter XIII was to allow the insolvent wage earner to discharge his debts without liquidating his assets, to give to the trustee the rights of a lien creditor would not be in the spirit of Chapter XIII because one would, in effect, be giving the trustee the power to deal with the assets of the debtor. However, the court reasoned that section 1041, which gives creditors in a Chapter XIII proceeding ordinary bankruptcy rights, and section 1011, which gives the court jurisdiction over the debtor's property when not inconsistent with the provisions of this chapter, clearly indicate that Chapter XIII is concerned with the debtor's assets as well as his future earnings. The fact that an unsuccessful wage earner's proceeding may be followed by liquidation of those assets in straight bankruptcy is an added indication that Chapter XIII is concerned with assets. The second argument advanced by the bank was that "even if the trustee is vested with the rights of a lien creditor, he cannot avoid the unrecorded mortgage because the mortgaged property is not utilized for the benefit of general creditors."

The court pointed out that although this would be true if the plan were completed, it would not be true if the debtor defaulted on his Chapter XIII payments and then consented to a transformation of a wage earner's proceeding into a straight bankruptcy, in which case it is in the interests of general creditors to preserve the assets of the debtor. It should be noted that the court expressly limited its holding to 70c and refused to consider the possible application of 70a, which gives title to the trustee to all the debtor's property as of the date of filing.

Most authorities strongly urge that only one trustee be appointed in each industrial area. General Order 55(2) excepts from application in wage earners' proceedings the provision set forth in General Order 14 that "no official trustee shall be appointed by the court, nor any general trustee to act in classes of cases." The reasons advanced why only one trustee should be appointed are: (1) All parties concerned have just one office to contact; (2) one trustee can adopt more efficient methods of operation and (3) communications between a single trustee and the referee's office are more effective.

---

80 City National Bank v. Oliver, supra note 77, at 689.
81 City National Bank v. Oliver, supra note 77, at 690.
84 NADLER, supra note 39, at 491; 27 Ref. J. 68, (1953).
86 General Orders in Bankruptcy, order 14 (1958).
87 17 Ref. J. 68 (1953).
X. Confirmation

After the plan has been accepted and the trustee appointed, the last item dealt with at the first meeting of creditors is the matter of confirmation. Unless already included in the notice of the first meeting or unless the plan is unanimously accepted by the creditors, the court will fix a time for the filing of applications to confirm the plan and for a hearing on the confirmation or on the objections to confirmation thereof. Although this requires the setting of two dates, the only event that need take place in the interval is the payment of the $15.00 filing fee by the debtor. Therefore, the “span of time required between the filing of and hearing on the confirmation can be as short as half an hour.”

The court will confirm the plan if it is satisfied that the requirements of section 1056 have been met. The first of these is that the “provisions of this chapter have been complied with.” Therefore, the court could not confirm a plan if the debtor refused to submit his future earnings to the control of the court or if the plan was not accepted by the requisite number of creditors.

The second requirement for confirmation is that the plan must be in the best interests of creditors and must be feasible. What is for the best interests of creditors depends on the facts in each case. The fact that creditors accepted the plan should be one indication that they consider it to be in their best interests. Prior to 1952, section 1056 required a finding by the court that in addition to being in the best interests of creditors, the plan must also be “fair and equitable.” Because a composition or extension can never be truly fair and equitable, and because of the judicial treatment of this phrase, it was eliminated, and the term “feasible” added:

Feasible need no longer be considered as conjunctive with ‘fair and equitable.’ This is the avowed purpose and effect of amending section 656 through the elimination of its former 3rd clause and adding “and is feasible” to its second clause. And in order to definitely show that Chapter XIII is not intended to be governed by the ‘fixed principle’ of Chapter X, the amendment added that ‘confirmation of a plan shall not be refused solely because the interest of a debtor will be preserved under the plan.’ No longer does a court have to consider whether

90 NADLER, supra note 39, at 555.
a plan is 'fair and equitable.' No longer can a court deny confirmation of a plan which provides for benefits and preserves equities for the debtor. The effect of this 1952 amendment is a true and realistic implementation of the philosophy of Chapter XIII proceedings. So long as the plan is for the best interests of the creditors and is feasible it can be confirmed. . . .

Presumably, feasible means "workable" in an economic sense. Wage earners' plans usually provide that between ten to twenty per cent of the debtor's future earnings will be turned over to the trustee for the benefit of creditors, but rarely do they provide for a greater than twenty-five per cent turnover. Although there is no requirement that the plan be completed within three years, this length of time seems to be a general guide in determining the economic feasibility of a wage earner's plan.

The third requirement for confirmation is that the debtor must not be guilty of any acts that would be a bar to the discharge of a bankrupt. Section 14, clause 5 provides that if a debtor has received a discharge from a wage earner's plan by way of "composition" within six years prior to the date of the filing of the petition, this prior discharge will be a bar to a confirmation of a later wage earner's plan. Therefore, where a debtor has received a discharge from a Chapter XIII proceeding by way of "extension," such discharge should not be a bar to the confirmation of a wage earner's plan brought within six years from the date of filing the original petition, whether the later plan be a composition or extension. However, a recently decided case casts some doubt on the validity of the previous statement. Here the court decided that a debtor was barred from securing confirmation of a wage earner's plan brought within six years after receiving a discharge from a previous wage earner's plan. The problem arises because the court neglected to state whether the first Chapter XIII proceeding was by way of composition or an extension. The court reasoned that debtors should not be allowed to use Chapter XIII to stop the accrual of interest on the principal debt and to prevent secured creditors from reclaiming their security, within six years after receiving a discharge under a prior Chapter XIII proceeding. If the previous Chapter XIII proceeding had been by way of composition the facts would have fallen squarely within section 14(c)(5), and

---

98 Nadler, supra note 39, at 565-566.
100 Nadler, supra note 39, at 565.
103 Nadler, supra note 39, at 551.
because of this, the court's failure to mention this section casts doubt
on the proposition that the previous Chapter XIII proceeding was a
composition. If this assumption is correct, this would appear to be the
first reported case holding a prior discharge from a wage earner's
plan by way of extension is a bar to a confirmation of a later Chap-
ter XIII proceeding brought within six years. In re Mahaley also
dealt with the problem of previous discharge as a bar to confirmation
of a wage earner's plan. However, in this case the debtor filed a
Chapter XIII petition by way of extension within six years after
receiving a discharge in ordinary bankruptcy. Faced with the proposi-
tion that a literal reading of sections 1056(a)(3) and 14(c)(5) would
deny the confirmation, the court reasoned that 14(c)(5) was so inconsis-
tent with the underlying principles of Chapter XIII that the latter was not applicable in this case, citing section 1002.

The fourth and last requirement of a wage earner's plan is that
the plan has been proposed and accepted in good faith and not procured
by any means forbidden by the Act. Obviously this would preclude
fraud and would prevent the giving of any secret advantages.

When confirmed, the plan is binding on the debtor and all his
creditors, "whether or not they are affected by the plan or have ac-
tcepted it or have filed their claims, and whether or not their claims
have been scheduled or allowed or are allowable." The effect of
section 1057 is that all creditors are barred from attacking the provi-
sions and the confirmation collaterally in any subsequent proceed-
ing.

Once the plan is confirmed, the court obtains control over the future
earnings of the debtor. To enforce this control, the court may issue
orders directed to any employer of the debtor. Experience has taught
that this is one of the most important sections of the Act:

The court may, if it wishes, rely on the voluntary promise of
the debtor to make regular payments, which is almost invariably
a mistake. At the opposite extreme it may order the employer
to make a necessary deduction or even to forward the debtor's
entire check to the trustee and it has full power to enforce its
order. It may issue its restraining order prohibiting the debtor

to VII, inclusive, of this Act shall, insofar as they are not inconsistent or in
conflict with the provisions of this chapter, apply in proceedings under this
chapter,...” [Emphasis added.].
113 NADLER, supra note 39, at 577.
from endorsing his check to anyone other than the trustee or cashing it anywhere except at the office of the trustee and if necessary, enforce its order through contempt of court action.116

Subsequent to confirmation the debtor starts making his agreed payments to the trustee. Before the creditors are paid anything, the requirements of section 1059117 must be fulfilled. Only when these payments have been met are the creditors entitled to be paid.

XI. DISCHARGE

The Act provides two methods by which a debtor may be discharged. The first is that the debtor has made all the payments provided for in the plan.118 In such cases the debtor is discharged from all his debts and liabilities provided for by the plan, "excluding such debts as are not dischargeable under section 17 of the Act held by creditors who have not accepted the plan."119 The Act also provides that a debtor may be discharged if, at the expiration of three years after confirmation, the debtor has not made all the payments provided for by the plan, but the court is satisfied that his failure to do "was due to circumstances for which he could not be justly held accountable."120 When a final discharge order is entered, the court also enters a decree discharging the trustee, closing the estate and making such other orders as may be equitable.121

If the debtor defaults in his payments or the plan is not confirmed for any of the various other reasons listed in 1066,122 the court has the power to set aside the proceedings and order that bankruptcy be proceeded with if the proceeding was originally converted from a straight bankruptcy petition to a Chapter XIII petition.123 If the original proceeding was under Chapter XIII, the court may either dismiss the Chapter XIII proceeding or with the debtor's consent, adjudge him a bankrupt.124

Two miscellaneous provisions worthy of mention are (1) all statutes of limitation affecting claims under this chapter are suspended "while a proceeding under this chapter is pending and until it is finally dismissed,"125 and (2) a debtor is not subject to taxable gain by reason of reduction of his indebtedness unless one of the principal purposes of the plan was to evade income tax.126

---

The costs of a Chapter XIII petition are naturally important. The following is an example of the average costs of a Chapter XIII proceeding. Debtor having income of $400 a month owes debts totaling $3000 which he desires to liquidate over a period of thirty months, at the rate of $100 per month. The average legal fee is $150 to $200; for purposes of example let us assume the higher fee of $200 is allowed. Since the trustee's commission (5% of $3000) is $150 and the average expenses of the trustee will total $90 and the referee's commission of one per cent is $30, the balance of the cost to the debtor equals $270. Therefore, the total cost of the average Chapter XIII proceeding is around $500, all, with the possible exception of $15 of the filing fee, payable out of the future earnings of the debtor.

XII. ADVANTAGES OF A CHAPTER XIII PROCEEDING

Practically, two requirements must be met before a debtor may take advantage of a Chapter XIII proceeding. First, the debtor must sincerely desire to pay his debts and be willing to sacrifice to do so and second, the debtor must not be so far in debt that a wage earner's plan would not be economically feasible. Some people have no desire to pay their debts; others, and I think the majority, have no desire to file bankruptcy and will do all they possibly can in order to avoid the stigma connected therewith. "We should always be careful not to let the small percentage of those who are dead beats, crooks or professional bankrupts distort our regard for the large majority who are honest." In addition, many people unable to resist highpowered advertising, high pressure sales tactics and loose consumer credit are often so far in debt that an attempt to pay off their debts in three to five years would be impractical.

Assuming the previous requirements are met, what can Chapter XIII do for a sincere debtor who is unable to meet his obligations as they mature? The single most important benefit obtained by the debtor is that when he files his Chapter XIII petition the court will enjoin the continuation of any and all garnishment proceedings against him. Since it is common knowledge that garnishments are the most potent weapon for driving debtors into bankruptcy, the importance of any measure that can stop them cannot be overemphasized. Secondly, the bankruptcy court may also stay any proceeding to enforce a lien upon the property of the debtor. This allows the debtor to keep badly needed chattles, such as his automobile or furniture. As previously mentioned, this has been used to enjoin a secured creditor from repossessing a chattel sold to a debtor under a conditional

sales contract where the debtor had a substantial equity in the property.\textsuperscript{130} Thirdly, Chapter XIII allows the debtor to reject executory contracts, including unexpired leases of real property,\textsuperscript{131} that he now feels are burdensome, the injured creditor being entitled to damages for the breach thereof. "Not only are leases on real estate included but also all other types of installment-contract purchases such as radios, autos, jewelry, clothing, etc."\textsuperscript{132} A fourth advantage of a Chapter XIII proceeding is that it is advantageous to the creditors because they will eventually receive what is due them. "All creditors with claims that will not stand the light of close examination dislike Chapter XIII and want no part of it."\textsuperscript{133} Lastly, Chapter XIII encourages debtors to pay their obligations and yet avoid the stigma of bankruptcy. A Chapter XIII proceeding that has been carried to a successful conclusion results in a double service to the community; the debtor has been financially rehabilitated and the business community has been saved a financial loss.

\textbf{Conclusion}

It has been the purpose of this article not to encourage the indiscriminate use of Chapter XIII in all no asset straight bankruptcy situations but rather to call attention to the use, manner and advantages of the chapter in appropriate cases.

\textit{William E. McCarty}

\textsuperscript{130} \textit{In re} Duncan, \textit{supra} note 42.
\textsuperscript{132} \textit{Nadler}, \textit{supra} note 39, at 767.
\textsuperscript{133} 33 \textit{Ref. J.} 51, 52 (1959).