No. 11-6309

IN THE
UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

In re ARVIN E. STEPHENS AND KAREN J. STEPHENS
AND NINNEKAH QUICK MART, L.L.C.,
Debtors.

DILL OIL COMPANY, L.L.C. AND DANNY DILL
AND NANCY DILL,
Appellants
— v. —
ARVIN E. STEPHENS AND KAREN J. STEPHENS AND NINNEKAH QUICK MART, L.L.C.,
Appellees

ON CERTIFICATION FOR DIRECT APPEAL FROM THE BANKRUPTCY APPELLATE PANEL FOR THE TENTH CIRCUIT No. 11-29

BRIEF OF *AMICUS CURIAE* NATIONAL ASSOCIATION OF CONSUMER BANKRUPTCY ATTORNEYS IN SUPPORT OF DEBTORS-APPELLEES

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May 21, 2012

CORPORATE DISCLOSURE STATEMENT

Dill Oil Company v. Stephens, No. 11-6309

Pursuant to Rule 26.1 of the Federal Rules of Appellate Procedure *Amicus Curiae* the National Association of Consumer Bankruptcy Attorneys makes the following disclosure:

1) For non-governmental corporate parties please list all parent corporations.
NONE.

2) For non-governmental corporate parties please list all publicly held companies that hold 10% or more of the party's stock. **NONE.**

3) If there is a publicly held corporation which is not a party to the proceeding before this Court but which has a financial interest in the outcome of the proceeding, please identify all such parties and specify the nature of the financial interest or interests. **NONE.**

4) In all bankruptcy appeals counsel for the debtor or trustee of the bankruptcy estate must list: 1) the debtor, if not identified in the case caption; 2) the members of the creditors' committee or the top 20 unsecured creditors; and, 3) any entity not named in the caption which is an active participant in the bankruptcy proceedings. If the debtor or trustee is not participating in the appeal, this information must be provided by appellant.
NOT APPLICABLE.

/s/ Tara Twomey
Tara Twomey, Esq.

Dated: May 21, 2012

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

Legislative History

Other Sources

STATEMENT OF INTEREST OF *AMICUS CURIAE*

Incorporated in 1992, the National Association of Consumer Bankruptcy Attorneys (NACBA) is a non–profit organization consisting of more than 4,400 consumer bankruptcy attorneys nationwide.

NACBA's corporate purposes include education of the bankruptcy bar and the community at large on the uses and misuses of the consumer bankruptcy process. Additionally, NACBA advocates nationally on issues that cannot adequately be addressed by individual member attorneys. It is the only national association of attorneys organized for the specific purpose of protecting the rights of consumer bankruptcy debtors. NACBA has filed *amicus curiae* briefs in various cases seeking to protect the rights of consumer bankruptcy debtors. *See, e.g., Schwab v. Reilly*, 560 U.S. ___, 130 S.Ct. 2652 (2010); *Kawaauhau v. Geiger*, 523 U.S. 57 (1998).

NACBA members primarily represent individuals in bankruptcy cases. Individuals who are sole proprietors or who own businesses or rental properties are often are ineligible for chapter 13 because their debts exceed the limits set forth in 11 U.S.C. § 109(e). Once in chapter 11, many such individuals who want to reorganize are forced into liquidation because of the application of the absolute priority rule. In 2005, Congress made significant amendments to chapter 11 insofar as it applies to individuals, which gave individual debtors a realistic opportunity to reorganize while continuing to protect unsecured creditors. Although this issue is currently pending before the Fourth Circuit Court of Appeals, *In re Maharaj*, No. 11-1747, no circuit

court has yet rendered an opinion as to whether the 2005 amendments to the Bankruptcy Code abrogate the absolute priority rule for individual chapter 11 debtors. As such, it is of great importance to NACBA and its membership.

STATEMENT UNDER FED. R. APP. P. 29(c)(5)

(a) No party's counsel authored this Amicus Curiae Brief in whole or in part;

(b) No party or party's counsel contributed money that was intended to fund preparing or submitting this brief; and

(c) No person, other than the amicus curiae, it members, or its counsel, contributed money that was intended to fund preparing or submitting the brief.

SUMMARY OF ARGUMENT

Chapter 11 of the Bankruptcy Code is designed to facilitate reorganization rather than liquidation. Integral to the rehabilitation of the chapter 11 debtor is the plan of reorganization. Section 1129 sets forth in detail the substantive requirements that a reorganization plan must satisfy to be confirmed. If a class of creditors rejects the debtor's plan of reorganization, the plan may only be confirmed if it is "fair and equitable." With respect to unsecured creditors, "fair and equitable" includes the requirement that: (i) claims must be paid in full; or (ii) senior creditors are paid in full before any party with a junior claim or interest, including the debtor, receives or

retains any property on account of such claim or interest. This prohibition against the debtor retaining any property unless creditors are paid in full is referred to as the "absolute priority rule."

In 2005, Congress made significant changes to chapter 11 as it applies to individual debtors. Among these changes was the addition of section 1115, which redefines "property of the estate" for individual chapter 11 debtors, and an amendment to section 1129(b)(2)(B)(ii), which permits debtors to retain property of the estate under section 1115 notwithstanding the absolute priority rule. These amendments abrogate the absolute priority rule with respect to individual chapter 11 debtors.

The Bankruptcy Court correctly held that the absolute priority rule no longer applies to individuals in chapter 11. The plain language of the statute, the history of the absolute priority rule and the purpose of the 2005 amendments affecting individual chapter 11 debtors all demonstrate that Congress has abrogated the absolute priority rule as applied to individual debtors.

ARGUMENT

A. THE STATUTORY FRAMEWORK FOR CHAPTER 11 ENCOURAGES REORGANIZATION, RATHER THAN LIQUIDATION.

The principal purpose of the Bankruptcy Code is to grant a fresh start to the honest but unfortunate debtor. *See Marrama v. Citizens Bank of Mass.,* 549 U.S. 365, 367

(2007); *Kokoszka v. Belford,* 417 U.S. 642, 645 (1974). More specifically, chapter 11 of the Bankruptcy Code is designed to facilitate reorganization and rehabilitation of the debtor. *See In re Thirtieth Place, Inc.,* 30 B.R. 503, 504 (B.A.P. 9th Cir. 1983) ("Chapter 11 of the Bankruptcy Code has one purpose; the rehabilitation or reorganization of entities entitled by statute to its relief"); *see also Nat. Labor Relations Bd. v. Bildisco,* 465 U.S. 513, 527 (1984); S.Rep. No. 95-989, 9-10 (1978) ("Chapter 11 deals with the reorganization of a financially distressed business enterprise, providing for its rehabilitation by adjustment of its debt obligations and equity interests"). Chapter 11 is intended to avoid liquidations under chapter 7 because liquidations have a negative impact on jobs, suppliers to businesses and the economy as a whole, *see United States v. Whiting Pools,* 462 U.S. 198, 203 (1983), and because creditors necessarily receive more in a successful chapter 11 case than in a chapter 7 liquidation.

Integral to the rehabilitation of the chapter 11 debtor is the plan of reorganization. Section 1129 of the Bankruptcy Code sets forth in detail the substantive requirements that a reorganization plan must satisfy to be confirmed. 11 U.S.C. § 1129. A chapter 11 plan that meets the requirements of section 1129(a), including acceptance by all impaired[1] classes of creditors, must be confirmed by the

[1]Section 1124 defines impairment, which with some exceptions generally means that the treatment of the class of claims has been modified under the plan. Unimpaired creditors are deemed to accept the plan without voting. 11 U.S.C. § 1126(f). Impaired creditors have the right to vote, and for a class of creditors to accept a plan those voting must accept the plan by two-thirds in dollar amount and a majority in number. 11 U.S.C. § 1126(c).

bankruptcy court. By contrast, if there are impaired classes that have not accepted the plan, the plan must conform to the dictates of section 1129(b) in order to be confirmed.

Section 1129(b) permits a court to confirm a chapter 11 plan despite its rejection by impaired creditor classes "if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan." 11 U.S.C. § 1129(b). To be "fair and equitable," section 1129(b)(2)(B) requires that: (i) unsecured creditors receive the value of the allowed amount of the claim as of the effective date of the plan; or (ii) senior creditors are paid in full before any party with a junior claim or interest, including the debtor, receives or retains any property on account of such junior claim or interest. This provision is generally referred to as the "absolute priority rule."

In 2005, Congress made significant changes to chapter 11 as it applies to individual debtors. Among other provisions, Congress added section 1115, which states as follows:

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

> (b) Except as provided in section 1104 or a confirmed plan or order confirming a plan the debtor shall remain in possession of all property of the estate.

Congress, at the same time, amended section 1129(b)(2)(B)(ii) to provide that in individual cases, "the debtor may retain property included in the estate under section 1115, subject to the requirements of subsection (a)(14)," effectively excluding individual debtors from the operation of the absolute priority rule. In its stead, Congress added a projected disposable income test, similar to that in chapter 13, to the confirmation requirements for individual chapter 11 plans. *See* 11 U.S.C. § 1129(a)(15).

When read plainly, the amendments to chapter 11 with respect to individual debtors show that the absolute priority rule has been abrogated in favor of the projected disposable income test as the mechanism to protect unsecured creditors (along with the liquidation, or "best interests" test in 1129(a)(7)). The bankruptcy court below correctly held that the debtors need not satisfy the absolute priority rule, opting for an interpretation of the statute that avoids liquidation and allows the debtors to maintain their reorganization plan, thereby maximizing recovery for unsecured creditors.

B. THE PLAIN LANGUAGE OF SECTIONS 1129(B)(2)(B)(ii) AND 1115 DEMONSTRATES THAT THE ABSOLUTE PRIORITY RULE NO LONGER APPLIES TO INDIVIDUAL DEBTORS.

The starting point for the court's inquiry should be the statutory language of 11 U.S.C. §§ 1115 and 1129(b)(2)(B)(ii). *See Lamie v. U.S. Trustee,* 540 U.S. 526, 534, 124 S.Ct. 1023, 1030 (2004). It is well established that when a "statute's language is plain, the sole function of the court, at least where the disposition required by the text is not absurd, is to enforce it according to its terms." *Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.,* 530 U.S. 1, 6 (2000) (internal quotations omitted). A result will be deemed absurd only if it is unthinkable, bizarre or demonstrably at odds with the intentions of its drafters. *See In re Spradlin,* 231 B.R. 254, 260 (Bankr. E.D. Mich. 1999) (citing *Public Citizen v. Dept. of Justice,* 491 U.S. 440, 109 S. Ct. 2558, 105 L.Ed.2d. 377 (1989)).

Section 1129(b)(2)(B)(ii) permits the debtor to retain "property included in the estate under section 1115." Section 1115(a) provides that property of the estate of an individual Chapter 11 debtor includes the following:

1. The property specified in section 541;
2. All section 541-type property acquired post-petition; and
3. Earnings from post-petition services performed by the debtor.

The natural reading of the plain language demonstrates that section 1115 broadly defines property of the estate to include property specified in section 541 as

well as property acquired post-petition and earnings from services performed post-petition. *See SPCP Group, LLC v. Biggins*, 465 B.R. 316 (M.D. Fla. 2011); *In re Tegeder,* 369 B.R. 477 (Bankr. D. Neb. 2007); *In re Bullard,* 358 B.R. 541 (Bankr. D. Conn. 2007). The word "includes" is not limiting, but rather logically encompasses everything that follows. *See* 11 U.S.C. § 102(3); *see also Burgess v. U.S.,* 553 U.S. 124, 128 n.3 (2008) ("The word 'includes' is usually a term of enlargement, and not of limitation") (citing 2A N. Singer & J. Singer, *Sutherland on Statutory Construction* § 47:7, p. 305 (7th ed. 2007)); *Friedman v. P + P, L.L.C.,* 466 B.R. 471, 482 (B.A.P. 9th Cir. 2012) ("'Included' is not a word of limitation"). What follows in section 1115(a) is both the property specified in section 541 and a list of additional items that will be also be considered property of the estate.

Courts agreed that the exception to the absolute priority rule in section 1129(b)(2)(B)(ii) encompassed both pre-petition and post-petition property for individual debtors until the court in *In re Gbadebo,* 341 B.R. 222 (Bankr. N.D. Cal. 2010), reached the opposite result. Subsequently, several courts have followed *Gbadebo* in holding that the absolute priority rule still applies to individual debtors. *See, e.g., In re Kamell,* 451 B.R. 505 (Bankr. C.D. Cal. 2011); *In re Steedley,* 2010 WL 3528599 (Bankr. S.D. Ga. Aug. 27, 2010). However, as recently determined by the Bankruptcy Appellate Panel for the Ninth Circuit, a close analysis of *Gbadebo* demonstrates that this line of cases is based on faulty logic and an erroneous rewriting of the statutory language. *See Friedman*, 466 B.R. at 483 (reasoning in *Gbadebo* "fatally flawed").

In *Gdabedo,* the debtor, a licensed engineer and sole shareholder of his engineering firm, filed a chapter 11 plan that proposed to retain the debtor's equity interest in the estate, strip down judgment liens on real property and treat the underlying judgment debt as a general unsecured claim. *Id.* The plan proposed to pay approximately a 2.6% distribution to unsecured creditors over 60 months. *Id.* at 225. A judgment creditor controlled the voting of the unsecured class, rejected the plan and objected to confirmation. *Id.*

Before reaching the question of the absolute priority rule the court found that the debtor's plan was filed in bad faith because his car and house payments were unreasonable. *Id.* at 226. The *Gbadebo* court also concluded that the debtor did not satisfy section 1129(a)(15) because the debtor's financial information was not credible. Rather, the debtor's testimony persuaded the court that the debtor used his company as "his personal 'piggy bank,' drawing money from it or causing it to pay his personal expenses as needed and failing to maintain its corporate separateness." *Id.*

After finding the debtor's chapter 11 plan unconfirmable based on sections 1129(a)(3) and 1129(a)(15), the *Gbadebo* court nevertheless went on to consider the applicability of the absolute priority rule. The *Gbadebo* court inverted the statutory language of section 1115 to hold the absolute priority rule still applies to individual chapter 11 debtors and thereby added another proverbial nail to the coffin of this dishonest debtor. Specifically, the *Gbadebo* court stated that:

> Section 541 provides that, when a petition is filed, a bankruptcy estate is created, consisting of the debtor's pre-petition property. Section 1115 provides that, in an individual chapter 11 case, *in addition to the property specified in § 541,* **the estate includes the debtor's post-petition property.**

431 B.R. at 229 (emphasis added). The *Ghadebo* court read the phrase "in addition to the property specified in section 541" (italicized above) as preceding the phrase "the estate includes the debtor's post-petition property" (bold above). Under the statute as rewritten by the *Ghadebo* court, property of the estate in section 1115 does not "include" property specified in section 541. The *Ghadebo* court concluded that only property *added* to the bankruptcy estate by section 1115 may be retained by the debtor under the exception in section 1129(b)(2)(B)(ii). But, the language written by Congress is different from that rewritten and analyzed by the *Ghadebo* court.

First, section 1129(b)(2)(B)(ii) uses the phrase "property *included* in the estate under section 1115," not "property *added* to the estate by section 1115." "Included" does not mean "added." Something that is "added" may be included but the converse is not necessarily true. Limiting the word "included" to mean "added" as the *Ghadebo* court did is inconsistent with the Code, which uses "includes" expansively. *See* 11 U.S.C. § 102(3); *see also American Sur. Co. v. Marotta,* 287 U.S. 513 (1933) (in the bankruptcy context "'include' is frequently, if not generally, used as a word of extension or enlargement rather than as one of limitation or enumeration.").

Second, while inverting the order of the clauses in section 1115 may support the conclusion reached by the *Ghadebo* court, it is not the language used by Congress.

Congress used the words "property of the estate includes, in addition to the property specified in section 541—…" Here, section 1115 refers the superset of section 541(a) property and the debtor's post-petition service income. *See In re Shat,* 424 B.R. 854, 863 (Bankr D. Nev. 2010). Put another way, section 1115 entirely supplants section 541 by specifically incorporating it and then adding to it. *Id.* Section 1129(b)(2)(B)(ii), therefore, permits the debtor to confirm a plan and retain both pre-petition and post-petition property of the estate so long as the other requirements of section 1129(a), except (a)(8), are satisfied.

As explained by the Bankruptcy Appellate Panel for the Ninth Circuit, when the *Gbadebo* court went beyond the plain language of the statute it engaged in "speculative analysis that was fatally flawed." *Friedman*, 466 B.R. at 483. The *Friedman* court took issue with the *Gbadebo* court's identification of an "anomaly" under which, if the absolute priority rule were to be deemed abrogated, a creditor's "no" vote would become meaningless. The court in *Friedman* disagreed. Congress built in safeguards in the event that a creditor votes "no" that rendered the absolute priority rule unnecessary to protect the dissenting creditor's interest. As explained above, a plan may be confirmed despite an impaired creditor's vote against confirmation only where section 1129(a)(15)(B) is satisfied, and the plan is "fair and equitable" under section 1129(b)(1).

The plain language of the statute, as written, thus abrogates the absolute priority rule for individual chapter 11 debtors. *See Friedman*, 466 B.R. at 484. The fact

that Congress could have opted for another way to relieve individual chapter 11 debtors of the obligations imposed by the absolute priority rule does not permit courts to simply ignore the language as written or rewrite the language to support the court's conclusion. It is irrelevant whether the language used by Congress is the most efficient way to achieve the intended result. Courts that find the absolute priority rule still applies to individual debtors because Congress could have, or should have, written the law differently have missed the mark in applying the foundational rule of statutory construction. *See In re Karlovich,* 456 B.R. 677, 682 (Bankr. S.D. Cal. 2010) (if abrogation of the absolute priority rule for individual debtors was Congress' intent, it would simply have amended the statutory debt ceilings for chapter 13 cases[2]); *In re Mullins,* 435 B.R. 352, 360 (Bankr. W.D. Va. 2010) (it would have been much clearer, easier and more direct to abrogate the absolute priority rule with different statutory language[3]). The proper inquiry here is whether applying the plain language of the

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[2] While Congress could have indeed raised the Chapter 13 debt ceilings in 11 U.S.C. § 109(e), Congress presumably made the decision that a modified Chapter 11, incorporating a disposable income requirement as in Chapter 13, along with the disclosure and voting requirements and the rights under § 1111(b) of non-recourse secured creditors to be treated as having recourse and of secured creditors to elect treatment as fully secured, would be preferable to the Chapter 13 process when more is at stake.

[3] Significantly, while reference is made to abrogating the absolute priority rule for individual debtors, the amendments to § 1129(b)(2)(B)(ii) do that only with respect to the "equity interest" of individual debtors in their assets, and not with respect to the requirement to pay senior classes of creditors in full before paying junior classes of creditors, such as subordinated debt. Language that allows the debtor to retain property of the estate, rather than repealing the absolute priority rule in its entirety, properly leaves the rule in effect with respect to junior creditors and prevents a debtor

statute leads to a result that is unthinkable, bizarre or demonstrably at odds with the intentions of its drafters. *See In re Spradlin,* 231 B.R. 254, 260 (Bankr. E.D. Mich. 1999). In this case, the abrogation of the absolute priority rule is demonstrated by the language Congress used and the effect of that language.

C. TO THE EXTENT THIS COURT FINDS THE LANGUAGE OF SECTIONS 1129(B)(2)(B)(ii) AND 1115 AMBIGUOUS, THE HISTORY OF THE ABSOLUTE PRIORITY RULE AND THE 2005 AMENDMENTS TO THE CODE DEMONSTRATE THAT THE ABSOLUTE PRIORITY RULE DOES NOT APPLY TO INDIVIDUAL DEBTORS IN CHAPTER 11.

Though the plain language of sections 1129(b)(2)(B)(ii) and 1115 make the absolute priority rule inapplicable to individual chapter 11 debtors, some courts have found the meaning of these sections, as amended in 2005, to be ambiguous and open to multiple interpretations. *See, e.g., In re Gelin,* 437 B.R. 435 (Bankr. M.D. Fla. 2010); *In re Shat,* 424 B.R. 854, 863 (Bankr D. Nev. 2010). If this Court similarly concludes the language of these two sections is ambiguous, then it must look beyond the words on the page to the statutory cross-references, legislative history, and congressional intent to discern its meaning. *See Ratslaf v. United States,* 510 U.S. 135, 147-48 (1994). Here, the history of the absolute priority rule and the 2005 amendments to the Code demonstrate that the absolute priority rule no longer applies to individual chapter 11 debtors.

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from paying subordinated (often insider) debt to the detriment of senior classes of unsecured creditors.

The absolute priority rule itself predates the Bankruptcy Code. It developed under the previous Bankruptcy Act as a judicially created doctrine to protect unsecured creditors from unscrupulous management and shareholders in corporate reorganizations. *Friedman,* 466 B.R. at 478. Fairness and equity required that "creditors…be paid before the stockholders could retain [equity interests] for any purposes whatever." *Bank of Am. Nat. Trust and Sav. Ass'n v. 203 North LaSalle St. P'ship,* 526 U.S. 434, 444 (1999). The absolute priority rule was codified in the Bankruptcy Code as section 1129(b)(2)(B). The effect of the absolute priority rule was to make it almost impossible for equity holders to retain their interest in a reorganized debtor in the absence of a plan that paid 100% to creditors or had their support.

The judicial exception to the absolute priority rule that permits equity to retain an interest in the reorganized debtor by contributing "new value" has provided a mechanism for corporate shareholders to contribute new capital, but provides little relief to sole proprietors and other individual chapter 11 debtors. *See Norwest Bank Worthington v. Ahlers,* 485 U.S. 197 (1988); *In re East*, 57 B.R. 14, 19 (Bankr. M.D. La. 1985); *In re Yasparro*, 100 B.R. 91, 98-99 (Bankr. M.D. Fla. 1989). Because shareholders typically have other sources of capital to contribute to the enterprise, they may contribute new value from outside the corporation and effectively buy back their shares. The Supreme Court effectively approved of this in *203 North LaSalle*, 527 U.S. at 453-54, provided that the new value is market tested to ensure that it is fixed by the market and not just by the Court or plan proponent. *Id.* at 457-58.

For individual debtors, the "new value exception" proved largely illusory, as the individuals' assets were already property of the estate and already counted in the liquidation test. Further, individual debtors cannot count the promise of future services as new value. *Ahlers,* 485 U.S. at 204-05. Without substantial gifts from friends or family, there was in most cases no source for this new value. *See Yasparro,* 100 B.R. at 98; *East*, 57 B.R. at 19. Even where there were post-petition profits, their contribution would not count if they were proceeds of estate assets. *See In re Stegall*, 865 F.2d 140, 142-44 (7th Cir. 1989). Effectively, under the absolute priority rule the owner of an unincorporated business had no means by which to offer new value so that the business could remain a going concern.

In *Ahlers,* the Supreme Court invited Congress to revisit the issue: "Yet relief from current farm woes cannot come from a misconstruction of applicable bankruptcy laws, but rather, only from action by Congress." 485 U.S. at 209. Other courts also held that it was up to Congress, not the courts, to exclude individual debtors from the harsh effect of the absolute priority rule on such individuals. *See In re Witt,* 60 B.R. 556, 560 (Bankr. N.D. Iowa 1986).

In 2005, Congress made significant amendments to chapter 11, applicable only to individual debtors, to make the administration of their cases more similar to chapter 13 cases. These changes include:

- redefining property of the estate in chapter 11 under Section 1115 along the lines of property of the estate under Section 1306;

- changing the mandatory contents of a plan pursuant to Section 1123(a)(8) to resemble Section 1322(a)(1);
- adding the disposable income test of Section 1325(b) to Section 1129(a)(15);
- delaying the discharge until completion of all plan payments as in Section 1328(a);
- permitting discharge for cause before all payments are completed pursuant to Section 1141(d)(5), similar to the hardship discharge of Section 1328(b); and
- the addition of Section 1127(e) to permit the modification of a plan even after substantial consummation for purposes similar to Section 1329(a).

In re Shat, 424 B.R. at 862 (citing 5 Keith M. Lundin, *Chapter 13 Bankruptcy* § 368.1 at 368-1 to 368-5 (3d ed. 2000 & Supp. 2006)); *In re Roedemeier,* 374 B.R. 264, 275-76 (Bankr. D. Kan. 2007) (citing same). Taken together, these changes evidence Congress's intent to harmonize the treatment of individual debtors under both reorganization chapters, and, as part of that harmonization, remove the absolute priority rule as a factor for individual chapter 11 debtors. *Friedman*, 466 B.R. at 484; *Roedemeier,* 374 B.R. at 276.

Viewed in the context of BAPCPA as a whole, it makes perfect sense that Congress intended to avoid the absolute priority rule as an unnecessary and largely nonsensical impediment to plan confirmation. One of the principal goals of BAPCPA was to enact "means testing" for Chapter 7 debtors with primarily consumer debt, *see* 11 U.S.C. § 707(b); *Ransom v. FIA Card Services, N.A.*, 131 S.Ct. 716, 721 (2011), forcing those for whom Chapter 7 would be an "abuse" into the reorganization chapters, where they would be required to repay their creditors from disposable

income. But for this goal to work, Chapter 11 would not only need a disposable income requirement, but it would have to be made viable for individual debtors who are ineligible for Chapter 13. To do that, the absolute priority rule would have to give way so that plans could be confirmed over a rejecting unsecured class.

The "protection" offered to unsecured creditors by the absolute priority rule in individual chapter 11 cases has been supplanted by the addition of the projected disposable income test. According to Congress, fairness and equity for unsecured creditors is embodied in the projected disposable income test, or means test, enacted as part of BAPCPA for both chapter 13 debtors and individual chapter 11 debtors. *See Friedman*, 466 B.R. at 484 (Congress intended to create symmetry between chapter 11 and chapter 13). The disposable income test—which applies in chapter 11 only to individual debtors—permits the holder of an allowed unsecured claim to object to confirmation of the debtor's plan if the plan fails to pay that creditor in full, or the value of the property to be distributed under the plan is less than the debtor's projected disposable income to be received during the 5-year period beginning on the date the first payment is due under the plan, or during the period for which the plan provides payments, whichever is longer. 11 U.S.C. § 1129(a)(15). Although both chapter 13 debtors and individual chapter 11 debtors are now subject to the projected disposable income test, significantly, chapter 13 does not impose the absolute priority rule on debtors. *See Roedemeier,* 374 B.R. at 276.

It is incongruous for Congress to make chapter 11 for individuals more like chapter 13 through the 2005 amendments, but leave the absolute priority rule and limitations on "new value" intact.[4] Without abrogation of the absolute priority rule, it is difficult to discern the purpose of the chapter 13-like amendments to chapter 11. *See Roedemeier,* 374 B.R. at 276. Pre-BAPCPA, the Bankruptcy Code made the absolute priority rule applicable to individual chapter 11 debtors while excluding from property of the estate their postpetition property and income. Under the narrow interpretation of sections 1129(b)(2)(B)(ii) and 1115 adopted by *Ghadebo* and its progeny, BAPCPA did little to change chapter 11 for individual debtors. As is evidenced by the dearth of case law under section 1129(a)(15) as compared to 1325(b), the projected disposable income test of section 1129(a)(15) is of little use to unsecured creditors so long as the absolute priority rule continues to apply to individual chapter 11 debtors. In essence,

[4]In congressional consideration of the bill that eventually became BAPCPA, the post-petition income and absolute priority rule changes were all part of a single amendment. Section 1115 (which includes both § 541 property and post-petition earnings in property of the estate in individual chapter 11 cases), the individual debtor exception to the absolute priority rule in § 1129(b)(2)(B)(ii), and the disposable income requirement (originally added to the bill as part of § 1129(a)(14) but which became § 1129(a)(15)) were all added as a single amendment to S.625, 106th Cong. *See* 145 Cong. Rec. S14097, S14100, § 321 (106th Cong., 1st Sess., Nov. 19, 1999). These three sections were ultimately adopted as a single section of BAPCPA, *see* Pub. L. 109-8, § 321, 119 Stat. 23, 94-95 (April 20, 1995), and work together as a unit. *See* Daly, *Post-Petition Earnings and Individual Chapter 11 Debtors: Avoiding a Head Start,* 68 Fordham L.Rev. 1745, 1777-79 (2000). In fact, the reference to subsection (a)(14) in § 1129(b)(2)(B)(ii) appears not to have changed when what was (a)(14) in the prior version was re-numbered (a)(15), and thus appears intended to be a reference to the disposable income requirement, not domestic support obligations. *See In re Shat*, 424 B.R. at 860 n.21.

the narrow view renders surplusage the 2005 amendments with respect to individual chapter 11 debtors. "'[C]ourts should disfavor interpretations of statutes that render language superfluous.'" *Conn. Nat'l Bank v. Germain,* 503 U.S. 249, 253, 112 S.Ct. 1146, 117 L.Ed.2d 391 (1992).

D. RETENTION OF THE ABSOLUTE PRIORITY RULE MAKES IT VIRTUALLY IMPOSSIBLE FOR SOLE PROPRIETORS WHO ARE INDIVIDUAL CHAPTER 11 DEBTORS TO CONFIRM A PLAN OF REORGANIZATION.

As noted by the court in *In re Shat,* the uniform application of the absolute priority rule to individuals and corporations alike effectively means that individual debtors with small businesses can never confirm a chapter 11 plan. *See Shat,* 424 B.R. at 859. By contrast, the *Gbadebo* court found that all that was needed for individual debtors to obtain plan confirmation was to "sweeten the pot" so that holders of unsecured claims would vote in favor of the plan. *Gbadebo,* 431 B.R. at 230-31. Based on the experience of NACBA members, we find reality to be closer to the description provided by the court in *Shat.* Unsecured creditors routinely do not vote in favor of a plan even where they would receive, as they must under section 1129(a)(7), more through the proposed chapter 11 plan than in a chapter 7 liquidation. This is true, even where debtors are paying all that they can afford to pay and have committed all their projected disposable income to plan payments for five years. The absolute priority rule as applied to individual chapter 11 debtors after the 2005 amendments runs counter to the basic principles of the Bankruptcy Code, which offer the honest

but unfortunate debtor a fresh start, and of chapter 11, which favors reorganization over liquidation.

CONCLUSION

For all of these reasons, Amicus, the National Association of Consumer Bankruptcy Attorneys, requests that this Court affirm the decision below and hold that the absolute priority rule does not apply to individual chapter 11 reorganizations.

Respectfully Submitted,

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CERTIFICATION OF COMPLIANCE
WITH TYPE-VOLUME LIMITATION

I hereby certify that the foregoing Brief contains 5,115 words, excluding the parts of the Brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii). In preparing this certification, I relied on the word-processing system used to prepare the foregoing Brief.

The foregoing Brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because it was prepared in a proportionally spaced typeface using Microsoft Word 9.0 in 14-point Garamond font.

Dated: May 21, 2012.

/s/ Tara Twomey
Tara Twomey

CERTIFICATE OF SERVICE

I hereby certify that on May 21, 2012, I electronically filed the foregoing document with the Clerk of the Court for the United States Court of Appeals for the Tenth Circuit by using the CM/ECF system.

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