THE ABSOLUTE PRIORITY RULE FOR INDIVIDUALS AFTER *MAHARAJ*, *LIVELY*, AND *STEPHENS*: NEGOTIATIONS OR GAME OVER?

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A husband and wife owned and operated an auto body repair shop in Virginia and, after falling victim to fraud, were left with considerable debt. The couple filed for Chapter 11 Bankruptcy—the chapter of the Bankruptcy Code typically used for corporate reorganizations—because their debt exceeded the limits for types of bankruptcies usually used by individuals. The couple filed a reorganization plan, which provided for the continued ownership and operation of their auto body business, and for the payment of the claims of unsecured creditors with future income from the business. All but one of the creditors approved the plan. Despite the creditor's objection, the couple began a process called a "cram down" to confirm the plan.

Whether this couple would be allowed to retain their business without the consent of the dissenting creditor came down to a very specific section of the Bankruptcy Code, commonly referred to as "the absolute priority rule." The absolute priority rule traditionally prevented businesses from retaining assets, such as stock equity, when forcing through a bankruptcy plan over the objections of creditors. However, recent amendments to the Code made it unclear whether this rule continued to apply to individuals in addition to businesses.

In Maharaj*, the U.S. Court of Appeals for the Fourth Circuit denied the couple's cram down and held that the absolute priority rule applied to individual debtors. Other courts have since addressed this issue, with the majority following* Maharaj*. As a result, many individual Chapter 11 debtors may be forced to liquidate their businesses and other property if not all classes of senior creditors approve their reorganization plans.*

However, a large number of early decisions, and a minority of recent opinions, continue to hold that the absolute priority rule does not apply to individual debtors. This disparity has profound consequences for bankruptcy debtors and has

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created uncertainty within jurisdictions that have not yet had appellate decisions on the issue. This Note argues that the minority view is better reasoned from both a statutory perspective and policy standpoint, and that the absolute priority rule should not apply to individual debtors.

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INTRODUCTION

Since the 2008 economic recession began, the total number of individual Chapter 11 bankruptcy filings has increased dramatically.[1] Although Chapter 11 filers were historically businesses,[2] in 1991 the Supreme Court held that individuals could also file under Chapter 11.[3] Individuals filing under Chapter 11

1. AM. BANKR. INST., BANKRUPTCY FILING STATISTICS—ANNUAL NON-BUSINESS FILINGS BY CHAPTER (2007–11). The percentage increase in the number of individual Chapter 11 filings each year after 2007 has been 44%, 69%, 29% and –10% from 2008 to 2011 respectively. *Id.*

2. *See Chapter 11: Reorganization Under the Bankruptcy Code*, *The Chapter 11 Debtor in Possession*, U.S. COURTS, http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/Chapter11.aspx (last visited Sept. 23, 2013). Chapter 11 is typically used to reorganize a business, which may be a corporation, sole proprietorship, or partnership. *Id.*

3. Toibb v. Radloff, 501 U.S. 157, 166 (1991) (recognizing that individual debtors may file Chapter 11).

are generally one of three types: small businesses operated as sole proprietorships,[4] individuals who have made personal guarantees,[5] or individuals with significant mortgage debt.[6]

In 2008, approximately 71.5% of U.S. businesses filed with the Internal Revenue Service as sole proprietorships[7]—comprising the majority of businesses in the United States. These owners are personally liable for all of their businesses' debts, liabilities, and losses.[8] Business form can result in major financial consequences for owners filing for bankruptcy because, although some business structures offer limited liability to their owners or members,[9] sole proprietorships do not. For example, the shareholders of a corporation only risk the loss of their investment in the business, whereas a sole proprietor may lose personal assets as well as the entire business in bankruptcy, which is often his sole source of income.

There are various reasons why an individual debtor may choose to file under Chapter 11, despite some of its unfavorable provisions, as compared to other chapters. Such unfavorable provisions include: increased filing fees,[10] higher attorney fees,[11] and the absolute priority rule.[12] The absolute priority rule is an

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4. Within the realm of business bankruptcies, sole proprietorships are the only recognized "individual filer" because corporations, partnerships, and other business forms are separate legal entities.

5. Douglas G. Baird, *The Hidden Virtues of Chapter 11: An Overview of the Law and Economics of Financially Distressed Firms* 5 & n.14 (Chi. Working Papers in Law and Econ. 2d Series, Working Paper No. 43, 1997).

6. *Id.* at 4.

7. INTERNAL REVENUE SERV., TABLE 1. NUMBER OF RETURNS, TOTAL RECEIPTS, BUSINESS RECEIPTS, NET INCOME (LESS DEFICIT), NET INCOME AND DEFICIT BY FORM OF BUSINESS: TAX YEARS 1980–2008, *available at* http://www.irs.gov/uac/SOI-Tax-Stats-Integrated-Business-Data (last updated Jan. 22, 2013). This table does not include farm sole proprietorships, which would increase the percentage of sole proprietorships filed.

8. *Sole Proprietorship*, SMALL BUS. ADMIN., http://www.sba.gov/content/sole-proprietorship-0 (last visited Sept. 23, 2013); *see also Chapter 11: Reorganization Under the Bankruptcy Code*, *The Chapter 11 Debtor in Possession*, U.S. COURTS, http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/Chapter11.aspx (last visited Sept. 23, 2013) ("A sole proprietorship (owner as debtor), on the other hand, does not have an identity separate and distinct from its owner(s). Accordingly, a bankruptcy case involving a sole proprietorship includes both the business and personal assets of the owners-debtors.").

9. *Corporation*, U.S. SMALL BUS. ADMIN., http://www.sba.gov/content/corporation (last visited Aug. 14, 2013); *Limited Liability Company*, U.S. SMALL BUS. ADMIN., http://www.sba.gov/content/limited-liability-company-llc (last visited Sept. 23, 2013).

10. *Bankruptcy Filing Fees—Effective November 21, 2012*, U.S. COURTS, http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyResources/BankruptcyFilingFees.aspx (last visited Sept. 23, 2013). Total fees collected at filing as of November 2012 for Chapter 7, 11, and 13 respectively were $306, $1,213, and $281, respectively. *Id.*

11. Average attorneys' fees post-Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA") for Chapter 7 and 13 were $1,072 and $2,564, respectively. LOIS R. LUPICA, AM. BANKR. INST., THE CONSUMER BANKRUPTCY FEE STUDY 6–7 (Dec. 2011). Chapter 11 fees are significantly higher with fees ranging from $10,000 to costs in the millions. *See* David Prelle Eron, *The Basics of Filing Chapter 11*, AVVO,

equitable standard that prevents retention of any property under a plan of reorganization when a plan cannot be confirmed by a vote of all creditors.[13] This means that a business may have to liquidate and that owners could be required to give up their assets.

So why do some individuals file under Chapter 11 rather than Chapter 7 or Chapter 13?[14] Chapter 7 facilitates liquidations, not reorganizations, making it unattractive for the debtor that wants to keep a business open.[15] Alternatively, some debtors are ineligible for Chapter 7 because they exceed the median income test.[16] Furthermore, an individual may be ineligible for Chapter 13 if he owes debts exceeding the threshold amount under the chapter.[17]

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http://www.avvo.com/legal-guides/ugc/the-basics-of-filing-chapter-11 (last visited Oct. 12, 2013); Jacqueline Palank, *$1,000/Hour Bankruptcies: Attorneys Justify Their Fees*, THE WALL STREET JOURNAL (June 3, 2012, 6:29 PM), http://online.wsj.com/news/articles/SB10001424052702303506404577444374260079502.

12. *See* 11 U.S.C. § 1129(b)(2)(B)(ii) (2012); *see also In re* Maharaj, 681 F.3d 558, 561 (4th Cir. 2012) (stating that, by enacting the Bankruptcy Code, "Congress specifically incorporated the absolute priority rule into § 1129(b)(2)(B)(ii)"); *In re* Arnold, 471 B.R. 578, 594 (Bankr. C.D. Cal. 2012) ("Specifically, § 1129(b) in its current form allows debtors to confirm a plan over the objection of unsecured creditors so long as the unsecured class is given 'fair and equitable' treatment under the plan through one of the two options under § 1129(b)(2)(B)(i) or (ii).").

13. *In re Arnold*, 471 B.R. at 590–97 (discussing the absolute priority rule as an equitable standard).

14. Individuals can generally file for three chapters of bankruptcy—7, 11, and 13—unless they are family farmers or fishermen. Chapter 7 is the chapter of the Bankruptcy Code providing for liquidation—the sale of the debtor's nonexempt property and distribution to creditors. *Chapter 7*, U.S. COURTS, http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/Chapter7.aspx (last visited Sept. 23, 2013). Chapter 11 is the chapter of the Bankruptcy Code providing for reorganization—keeping a business alive and paying creditors over time. *Chapter 11*, U.S. COURTS, http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/Chapter11.aspx (last visited Sept. 23, 2013). Chapter 13 is the chapter of the Bankruptcy Code which provides for the adjustment of individual's debts—allows for debtor to keep property and pay off the creditors over time. *Chapter 13*, U.S. COURTS, http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/Chapter13.aspx (last visited Sept. 23, 2013).

15. Chapter 11 is an alternative to Chapter 7, and is intended to avoid liquidations—leading to the preservation of jobs, a better return for owners, and more ultimately paid to creditors. United States v. Whiting Pools, 462 U.S. 198, 203–07 (1983).

16. 11 U.S.C. § 707(b) (2012). The median income test states that a court may dismiss or convert a Chapter 7 filing if the debtor's current monthly income (reduced by amounts as listed under clauses (ii), (iii), and (iv) and multiplied by 60) is not less than the lesser of (1) 25 percent of the debtor's nonpriority unsecured claims in the case, or $7,475, whichever is greater; or (2) $12,475. *Id.* § 707(b)(2)(A)(i).

17. *Id.* § 109(e) (2012). An individual may be a debtor under Chapter 13 of this title if he or she owes unsecured debts of less than $383,175 and secured debts of less than $1,149,525. *Id.*

Consequently, there exists a distinct subset of bankruptcy filers that only have the option of filing under Chapter 11.[18] This situation arises when an individual exceeds the debt limit of Chapter 13 and possesses an above-average income,[19] making the options for bankruptcy rather narrow and reducing leverage in bargaining with creditors.[20]

Part I of this Note begins by discussing the process of filing a Chapter 11 petition, which is fundamental to understanding the context of how the absolute priority rule functions in Chapter 11 bankruptcies. Next, this Note discusses the history of the absolute priority rule and recent congressional amendments to the Bankruptcy Code,[21] which created confusion as to whether the absolute priority rule applies to individuals filing for Chapter 11. Many bankruptcy courts have addressed this issue and have come to varying conclusions regarding the rule; Part II explores and analyzes some of the most illustrative examples.

Finally, Part III of this Note argues that the absolute priority rule should not apply to individuals. A plain reading of §§ 1129(b)(2)(B)(ii) and 1115 of the Bankruptcy Code, other amendments modifying Chapter 11 for individuals to imitate Chapter 13, the statutory framework of both Chapter 11 and recent congressional amendments, and the history of the absolute priority rule all support this argument. In addition to statutory analysis, this Note recognizes the important practical implications and problems surrounding the application of the rule to individuals, including: the virtual impossibility of confirming a plan of reorganization for certain debtors and the issue of whether an individual debtor may retain exempt property. Recognition of these issues is important, as they undermine the opposing argument that the amendments are consistent with congressional intent.

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18. Individual debtors whose current monthly income is greater than that of the median family income of their state and who owe $360,475 or more in unsecured debts or $1,149,525 or more in secured debts can only file for Chapter 11. *Id.* §§ 109(e), 707(b);

> An individual who wants to retain property, reorganize finances and obtain a discharge of debts may file a petition under Chapter 11, 12 or 13 of the Bankruptcy Code. However, if the individual is not a "family farmer" or "family fisherman," or if the amount of the individual's unsecured or secured debts exceeds the respective ceiling, the individual can only reorganize under Chapter 11.

Alan M. Ahart, *The Absolute Abolition of the Absolute Priority Rule in Individual Chapter 11 Cases*, 31 CAL. BANKR. J. 731, 731 (2011).

19. 11 U.S.C. §§ 109(e), 707(b); *see also* Ahart, *supra* note 18, at 731.

20. *See* Andrew G. Balbus, *Does the Absolute Priority Rule Apply to Individuals in Chapter 11?* 20 NORTON J. BANKR. L. & PRAC. 79, 82 (2011); s*ee also* HON. RONALD A. BARLIANT, AM. BNKR. INST., CHAPTER 11 PLANS OF REOGANIZATION (2001).

21. Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109–8, 119 Stat. 23–217 (2005) (codified as amended at scattered sections of 11 U.S.C.).

I. CHAPTER 11 AND THE ABSOLUTE PRIORITY RULE

A. The Process of Filing a Chapter 11 Petition

A voluntary Chapter 11 case begins when a debtor files a Chapter 11 petition in bankruptcy court.[22] After the case commences, the bankruptcy estate of the debtor is formed pursuant to § 541 and includes, "all legal or equitable interests of the debtor in property as of the commencement of the case."[23] Individual debtors are then permitted to exempt certain property from the estate.[24] The debtor typically files a plan of reorganization, which specifies the different classes of claims.[25] Chapter 11 also requires the debtor to specify which classes of claims are impaired and which classes are unimpaired under the plan.[26]

Once a plan is proposed, there are two routes to confirmation[27] under § 1129. First, the bankruptcy court may approve a debtor's plan if all classes of creditors approve.[28] Alternatively, if all classes of creditors do not accept the plan, but at least one class does,[29] the court may still confirm the reorganization plan through a process known as a "cram down."[30] Regardless of which method is used to confirm a plan, the best interest test applies, mandating that creditors be paid at least what they would get in liquidation.[31] The court may proceed with a cram down if: (1) the plan does not discriminate unfairly, and (2) the plan is fair and equitable, with respect to each class of impaired creditors that have not accepted the plan.[32]

One of the requirements for a plan to satisfy the fair and equitable standard is known as the absolute priority rule.[33] The absolute priority rule prohibits a debtor from retaining *any* property unless senior creditors are paid in full or all classes of creditors approve a reorganization plan.[34] Unfortunately, courts have long struggled with how best to apply the absolute priority rule to

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22. 11 U.S.C. § 301 (2012).
23. *Id.* § 541(a)(1) (2012).
24. *Id.* § 522(b)–(c) (2012).
25. *Id.* § 1123(a) (2012).
26. *Id.* § 1123(a)(2)–(3). The claims of creditors are impaired if their contractual rights are to be modified or if they will be paid less than the full value of their claims under the plan. *Id.* § 1124 (2012).
27. Confirmation is the process by which a bankruptcy judge approves a plan of reorganization or liquidation before the plan can be finalized. *See In re* 20 Bayard Views, LLC, 445 B.R. 83, 93–97 (Bankr. E.D.N.Y. 2011).
28. 11 U.S.C. § 1129(a) (2012). Unimpaired classes are deemed to have accepted the plan. *Id.* § 1129(a)(7)(A)(i).
29. *Id.* § 1129(a)(10).
30. *Id.* § 1129(b)(1). A cram down is the involuntary imposition of a bankruptcy plan by a court over the objection of some creditors.
31. *Id.* § 1129(a)(7).
32. *Id.* § 1129(b)(1).
33. *Id.* § 1129(b)(2)(B)(ii).
34. *Id.*

individuals, because "Chapter 11, as it was originally conceived, was never intended to be used by individual debtors."[35]

B. The Absolute Priority Rule

Section 1129(b)(2)(B)(ii) of the Bankruptcy Code, known as the absolute priority rule, does not allow any unsecured junior creditor or interest holder to retain *any* property unless all senior creditors are paid in full or all classes of creditors approve a reorganization plan.[36] Courts have looked to the history of the absolute priority rule as an aid to their decisions on its applicability to individual debtors.[37] This Part begins with a brief overview of that history.

1. The History of the Absolute Priority Rule

The absolute priority rule was originally a judicially created concept arising from a series of early twentieth-century railroad cases.[38] The U.S. Supreme Court adopted the absolute priority rule primarily to prevent deals that imposed unfair terms on unsecured creditors and allowed equity shareholders to retain property during corporate reorganizations.[39] The rule ensured that creditors would be fully repaid before equity holders could receive or retain any property under a plan of reorganization.[40] Although never codified by name, in 1952, Congress expressly repealed the concept of the absolute priority rule in what was the predecessor to Chapter 11, "which was designed for small privately held businesses."[41] In 1978, Congress passed the Bankruptcy Reform Act—merging many aspects of Chapters X, XI, and XII into the current Chapter 11—and incorporated the absolute priority rule into the Bankruptcy Code.[42] This rule remained unchanged in § 1129(b)(2)(B)(ii) until the 2005 Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA") amendments.[43]

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35. Anthony Mendenhall, *Does the Absolute Priority Rule Still Apply to Individual Chapter 11 Debtors Post-BAPCPA?* 2 (June 29, 2012) (Univ. of Tenn., Working Paper).

36. "[T]he holder of any claim or interest that is junior to the claims of such class will not receive or retain under the plan on account of such junior claim or interest any property . . . ." 11 U.S.C. § 1129(b)(2)(B)(ii).

37. *See In re* Maharaj, 681 F.3d 558, 560 (4th Cir. 2012); *In re* Friedman, 466 B.R. 471, 478 (B.A.P. 9th Cir. 2012).

38. *In re Friedman*, 466 B.R. at 478; *see, e.g.*, Case v. L.A. Lumber Prods. Co., 308 U.S. 106, 115–17 (1939); N. Pac. Ry. Co. v. Boyd, 228 U.S. 482, 508 (1913); Chi., Rock Island & Pac. R.R. v. Howard, 74 U.S. 392, 409–10 (1868).

39. *In re Friedman*, 466 B.R. at 478.

40. Mendenhall, *supra* note 35, at 1–2.

41. *In re Maharaj*, 681 F.3d at 561 & n.3 ("The absolute priority rule remained a fixture of Chapter X of the Act, which was designed for public companies.") (citing Ralph A. Peeples, *Staying in: Chapter 11, Close Corporations and the Absolute Priority Rule*, 63 AM. BANKR. L.J. 65, 66 (1989)).

42. *Id.* at 561.

43. *Id.*

The absolute priority rule functions as a creditor protection. For example, in a corporate reorganization, if there is not enough value to reach a junior class, such as equity holders, that class is eliminated and gets nothing.[44] "Elimination of the 'equity' class in an individual case[—where the owner is the entire equity class—]is something most courts would avoid."[45] Historically the absolute priority rule was not designed to apply to individuals.[46] Because individuals are now permitted to file under Chapter 11, courts have struggled with how to apply the absolute priority rule to individual debtors and have come to differing results.[47] Amidst conflicting rulings, it is clear that Chapter 11 and the issue of the absolute priority rule have "now crossed over to the general consumer bankruptcy practice"[48] as indicated by the increased number of individual cases filed under Chapter 11.[49]

Despite its name, the absolute priority rule has never been absolute,[50] and courts have recognized exceptions throughout its existence. Under the "new value exception," equity holders may retain an interest in new capital, often represented by stock, if the new value ensures successful reorganization.[51] Consequently, the new capital contributed to a company is exempt from the bankruptcy estate.[52] Corporations are often able to obtain funding from other sources of capital, which gives some weight to the new value exception.[53] For individuals, however, the assets that they have are usually already invested in the business and outside capital is typically unavailable.[54] The Supreme Court has held that individual debtors cannot use the promise of future services as new value,[55] and additionally, postpetition profits are not included as new value if they were derived from estate

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44. Bruce A. Markell, *The Sub Rosa Subchapter; Individual Debtors in Chapter 11 After BAPCPA*, 2007 U. ILL. L. REV. 67, 89 (2007).

45. *Id.*

46. Mendenhall, *supra* note 35, at 9.

47. *Id.* at 9 & n.53.

48. *In re* Friedman, 466 B.R. 471, 478, n.13 (B.A.P. 9th Cir. 2012); *see also* AM. BANKRUPTCY INST., *supra* note 1. In fact, "[t]here is no doubt that the absolute priority rule was a necessary feature to be considered in individual debtors' [sic] [C]hapter 11 plans of reorganization prior to the enactment of the BAPCPA." *In re Friedman*, 466 B.R. at 478 n.13. Nevertheless, "Congress has not significantly increased the outer limits of eligibility for [C]hapter 13 debtors." *Id.* As a result, "a combination of the present day national economic climate, the amendment to § 1129(b)(2)(B)(ii) and the addition of the new § 1115 has presented consumer bankruptcy lawyers with growth opportunities in the individual debtor [C]hapter 11 practice." *Id.*

49. *See supra* note 1 and accompanying text.

50. *In re Friedman*, 466 B.R. at 478.

51. *In re* Gen. Teamsters, Warehousemen & Helpers Union, Local 890, 265 F.3d 869, 873 (9th Cir. 2001).

52. *See* Case v. L.A. Lumber Prods. Co., 308 U.S. 106, 121 (1939); *see also* Brief for the Nat'l Ass'n. of Consumer Bankr. Attorneys as Amici Curiae Supporting Appellants at 12, *In re* Maharaj, 681 F.3d 558 (2012) (No. 11-1747) [hereinafter Brief for Appellants].

53. *See* Brief for Appellants, *supra* note 52, at 12.

54. *See id.*

55. *See* Norwest Bank Worthington v. Ahlers, 485 U.S. 197, 204–06 (1988).

assets.[56] Unless an individual receives a generous gift from a family member or friend, there is usually no source for new value and therefore, no new value exception.[57]

Another exception to the absolute priority rule is the equity interest exception.[58] This exception stems from the previously mentioned new value exception, where equity holders in for-profit corporations must choose between contributing new value and liquidating their interest. Courts have interpreted the term "interest" to mean an equity interest in a for-profit corporation.[59] For example, members of a nonprofit do not hold an equity interest[60] and therefore can maintain the organization's assets without satisfying the new value exception to the absolute priority rule.[61]

2. Recent Amendments to the Absolute Priority Rule

In 2005, Congress amended the Bankruptcy Code with the BAPCPA.[62] The legislation added an exception to the absolute priority rule that has become the source of disagreement among courts: Whether the absolute priority rule was abrogated for individuals filing under Chapter 11. The absolute priority rule and the added exception read as follows:

> [T]he holder of any claim or interest that is junior to the claims of such class will not receive or retain under the plan on account of such junior claim or interest any property, *except that in a case in which the debtor is an individual, the debtor may retain property included in the estate under § 1115* . . . .[63]

The legislation simultaneously created § 1115, which states:

> 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

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56. *See In re* Stegall, 865 F.2d 140, 142–44 (7th Cir. 1989).

57. Brief for Appellants, *supra* note 52, at 12.

58. *In re* Friedman, 466 B.R. 471, 48–79 (B.A.P. 9th Cir. 2012) (citing *In re* Gen. Teamsters, Warehousemen & Helpers Union, Local 890, 265 F.3d 869, 874 (9th Cir. 2001)).

59. *In re Gen. Teamsters*, 265 F.3d at 873–74 (9th Cir. 2001) (discussing *In re* Wabash Valley Power Ass'n, Inc., 72 F.3d 1305 (7th Cir. 1995)).

60. The Seventh Circuit identified three components of equity interest: (1) control; (2) profit share; and (3) ownership of corporate assets. *In re Wabash Valley*, 72 F.3d at 1318.

61. *In re Gen. Teamsters*, 265 F.3d at 873–74 (discussing *In re Wabash Valley*, 72 F.3d at 1318–19).

62. Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109–8, 119 Stat. 23–217 (2005) (codified as amended at scattered sections of 11 U.S.C.).

63. 11 U.S.C. § 1129(b)(2)(B)(ii) (2012) (emphasis added).

> 1. all property of the kind specified in section 541 that the debtor acquires after the commencement of the case . . .
> 2. earnings from services performed by the debtor after the commencement of the case . . .[64]

Section 541, in turn, defines the property of the estate to include "all legal or equitable interests of the debtor in property as of the commencement of the case."[65]

Thus, the main controversy as to what the exception in § 1129(B)(2)(b)(ii) means depends on its "included in the estate under § 1115" language. There are two competing constructions of the phrase. In one view, property specified in § 541 is incorporated by reference into the property of the estate as defined in § 1115.[66] This would exempt an individual debtor's entire estate from the absolute priority rule, by including: prepetition property, postpetition property, and postpetition income earned from services.[67] This view is known as the "broad view," and would effectively eliminate the absolute priority rule for individuals.[68]

Under the competing view, "included in" means something closer to "added to" § 1115,[69] in which case only postpetition property and earnings could be retained, rather than all property included under § 541.[70] According to this interpretation, as will be further explained below, Congress intended that Chapter 11 debtors could only retain property and earnings acquired after the commencement of the case that—absent the 2005 BAPCPA amendment—would otherwise be included in the estate.[71] This interpretation is known as the "narrow view."[72]

In addition to the changes made to the absolute priority rule, the legislation added various sections that affect only individuals and, in effect, transformed Chapter 11 for individuals to be more similar to Chapter 13.[73] These changes include the addition of the disposable income test, permitting modification of a plan after substantial consummation, delaying the discharge until the completion of all plan payments, and permitting a discharge for cause before all payments are completed.[74]

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64. *Id.* § 1115(a)(1)–(2) (2012).
65. *Id.* § 541(a)(1) (2012).
66. *In re* Maharaj, 681 F.3d 558, 569 (4th Cir. 2012).
67. Mendenhall, *supra* note 35, at 13.
68. *Id.*
69. *In re Maharaj*, 681 F.3d at 569.
70. Mendenhall, *supra* note 35, at 13–14.
71. *Id.*
72. *Id.*
73. Brief for Appellants, *supra* note 52, at 13.
74. *See infra* Part III.A.2.

In particular, the disposable income test is an interesting addition to Chapter 11. This test adds a supplementary level of creditor protection, and requires that if the holder of an unsecured claim is not paid in full, then property of a value at least equal to five years of the debtor's projected disposable income must be paid to unsecured creditors.[75] Thus, whatever postpetition property the individual debtor is permitted to keep must be reduced by five years' worth of his or her disposable income.[76] This amendment to Chapter 11 has very different meanings under narrow and broad interpretations of the BAPCPA amendments.[77] Under a narrow view analysis, the debtor cannot retain prepetition property at all, allowing a debtor to retain only postpetition property.[78] Thus, when read in context with the disposable income test, the addition of § 1115 would only allow a debtor to retain disposable income after five years.[79] As interpreted by courts following the broad view, a debtor would be permitted to keep both prepetition property as defined in § 541 and post-fifth-year income.[80]

These amendments to the Bankruptcy Code caused confusion in the bankruptcy community regarding whether the absolute priority rule continued to apply to individual debtors filing for Chapter 11 bankruptcy. Numerous bankruptcy courts have addressed the issue and have reached different interpretations, resulting in a split of authority.[81]

II. DISCUSSION OF THE MAIN CASES

More than a dozen courts have come to the conclusion that the absolute priority rule applies to individuals[82]—making the narrow view the majority rule among courts.[83] Nevertheless, several bankruptcy courts, including the Ninth

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75. 11 U.S.C. § 1129(a)(15)(B) (2012).

76. *See* Markell, *supra* note 44, at 89–90.

77. *Id.* at 90 ("Given the paucity of legislative history on this point, the section's intended scope is unclear." Either a debtor would be able to retain "miserly post-fifth year income" or "all estate property.").

78. *Id.* at 89–90.

79. *Id.*

80. *See id.*

81. *See, e.g.*, *In re* Lively, 717 F.3d 406, 407 (5th Cir. 2013); *In re* Stephens, 704 F.3d 1279, 1287 (10th Cir. 2013); *In re* Maharaj, 681 F.3d 558, 560 (4th Cir. 2012); *In re* Arnold, 471 B.R. 578, 581 (Bankr. C.D. Cal. 2012); *In re* Gbadebo, 431 B.R. 222, 229 (Bankr. N.D. Cal. 2010). *But cf. In re* Friedman, 466 B.R. 471, 473 (B.A.P. 9th Cir. 2012); *In re* O'Neal, 490 B.R. 837, 851 (Bankr. W.D. Ark. 2013); SPCP Group, L.L.C. v. Biggins, 465 B.R. 316, 322–23 (M.D. Fla. 2011); *In re* Shat, 424 B.R. 854, 856 (Bankr. D. Nev. 2010); *In re* Johnson, 402 B.R. 851, 852–53 (Bankr. N.D. Ind. 2009); *In re* Roedemeier, 374 B.R. 264, 276 (Bankr. D. Kan. 2007); *In re* Tegeder, 369 B.R. 477, 480 (Bankr. D. Neb. 2007); *In re* Bullard, 358 B.R. 541, 543–44 (Bankr. D. Conn. 2007).

82. Richard L. Costella & Juliana Bell, Maharaj*: Absolute Priority Rule Lives On (at Least in Fourth Circuit)*, AM. BANKR. INST. J., Aug., 2012, at 30; *see also, e.g.*, *In re Lively*, 717 F.3d at 407; *In re Stephens*, 704 F.3d at 1287; *In re Maharaj*, 681 F.3d at 56; *In re Arnold*, 471 B.R. at 581; *In re Gbadebo*, 431 B.R. at 229.

83. Courts adopting the narrow view outnumber those adopting the broad view 16 to 6 as of June 30, 2012. Mendenhall, *supra* note 35, at 15, 22.

Circuit Bankruptcy Appellate Panel, have adopted the broad view, holding that the absolute priority rule is inapplicable to individual debtors filing for Chapter 11 Bankruptcy.[84]

A. Analysis of Narrow View Cases

In June 2012, the Fourth Circuit Court of Appeals in *Maharaj* held that Congress intended for the absolute priority rule to apply to individuals,[85] making *Maharaj* the first appellate decision regarding the absolute priority rule. This opinion was followed by the Fifth Circuit in *Lively*, and, most recently, by the Tenth Circuit in *Stephens*. In these cases, the courts also held that the absolute priority rule applies to individual debtors. The analysis is most complete in *Maharaj*, and I will use that analysis to frame this Part.

In *Maharaj*, the court started its analysis by discussing the history of the absolute priority rule.[86] The court traced the rule's establishment in railroad cases from the late 1800s, and recognized that the rule developed from the old Bankruptcy Act requirement that a reorganization plan be fair and equitable.[87]

The court then analyzed the statutory language at issue. Central to the court's analysis was the determination that the language of §§ 1129(b)(2)(B)(ii) and 1115 is ambiguous.[88] The court concluded that more than one reasonable interpretation regarding the language of these statutes exists, and noted that "courts that have considered this issue have arrived at plausible, competing arguments as to why their respective approaches are consistent with Congressional purpose in enacting BAPCPA."[89]

Generally, narrow view courts disagree as to whether the language of §§ 1129(b)(2)(B)(ii) and 1115 is ambiguous. Several narrow view courts have determined, like *Maharaj*, that the language of these statutes is ambiguous.[90] Two courts found ambiguity in that there was a split among courts.[91] In *Arnold*, the court engaged in a lengthy grammatical analysis of the language, finding ambiguity and determining that the absolute priority rule should still apply to

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84. Costella & Bell, *supra* note 82, at 30; *see also, e.g.*, *In re O'Neal*, 490 B.R. at 851; *In re Friedman*, 466 B.R. at 473; *SPCP Grp., L.L.C.* , 465 B.R. at 322; *In re Shat*, 424 B.R. at 856; *In re Johnson*, 402 B.R. at 852–53; *In re Rodemeier*, 374 B.R. at 276; *Tegeder*, 369 B.R. at 479; *In re Bullard*, 358 B.R. at 543–44.

85. *In re Maharaj*, 681 F.3d at 568.

86. *Id.* at 560.

87. *Id.* at 560–61.

88. *Id.* at 568.

89. *Id.* at 569.

90. *See*, *e.g.*, *In re* Arnold, 471 B.R. 578, 598–99 (Bankr. C.D. Cal. 2012); *In re* Lindsey, 453 B.R. 886, 903 (Bankr. E.D. Tenn. 2011); *In re* Kamell, 451 B.R. 505, 509 (Bankr. C.D. Cal. 2011); *In re* Gelin, 437 B.R. 435, 441 (Bankr. M.D. Fla. 2010).

91. Mendenhall, *supra* note 35, at 22–23; *see also In re Arnold*, 471 B.R. at 598–99 (recognizing that the language of §§ 1115 and 1129(b)(2)(B)(ii) is ambiguous because a split in authority exists); *In re Lindsey*, 453 B.R. at 903 ("[I]t is axiomatic that the language of § 1129(b)(2)(B)(ii) and § 1115 is ambiguous, otherwise there would be no split of authority and the arguments in favor of each position so diverse.").

individuals.[92] Other courts emphasized that, in addition to ambiguous language, the statute also has an ambiguous legislative history.[93]

Beginning with *Gbadebo*, some narrow view courts have come to the conclusion that the language is clear and unambiguous.[94] In *Gbadebo*, the court found the phrase "included in the estate under section 1115" reasonably susceptible to only one meaning: added to the bankruptcy estate by § 1115.[95] *Lively* agreed with *Gbadebo*, and ruled that the language was unambiguous,[96] agreeing that "included in" was equivalent to "added to."[97]

The *Maharaj* court was also persuaded that Congress could have abrogated the rule in a far less convoluted manner.[98] The opinion stressed that implied repeal is strongly disfavored, especially in the bankruptcy context.[99] Thus, the court reasoned that it would be inappropriate to abrogate the absolute priority rule absent plain language or evidence of congressional intent.[100] In support of this position, the court referenced prior congressional abrogation of the absolute priority rule in 1952, where there was a clear explanation in the legislative history.[101] In contrast, the court noted the complete absence of any prerogative to eliminate the absolute priority rule with respect to individuals in BAPCPA's legislative history, and found the congressional silence "telling."[102]

Unlike the issue of ambiguity where narrow view courts disagree, there is a consensus that Congress could have abrogated the rule in a far less convoluted manner. Narrow view courts use this as support for a lack of congressional intent.[103] It follows in their opinions that, in light of the well-established place of the absolute priority rule,[104] Congress could have been more clear, and could even

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92. *In re Arnold*, 471 B.R. at 599–604.

93. *In re Kamell*, 451 B.R. at 509; *In re Gelin*, 437 B.R. at 441.

94. *In re* Gbadebo, 431 B.R. 222, 229 (Bankr. N.D. Cal. 2010); *see also In re* Lively, 717 F.3d 406, 409 (5th Cir. 2013); *In re* Karlovich, 456 B.R. 677, 681 (Bankr. S.D. Cal. 2010); *In re* Mullins, 435 B.R. 352, 360 (Bankr. W.D. Va. 2010).

95. *In re Gbadebo*, 431 B.R. at 229 ("If the Court were writing on a clean slate, it would view the language of § 1129(b)(2)(B)(ii) as unambiguous.").

96. *In re Lively*, 717 F.3d at 409.

97. *Id*. at 410.

98. *In re* Maharaj, 681 F.3d 558, 571 (4th Cir. 2012).

99. *Id.* at 570–71. Courts "will not read the Bankruptcy Code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure." *Id.* at 570 (quoting Hamilton v. Lanning, 560 U.S. 505, 515 (2010)).

100. *Id.* at 570–72.

101. *Id.* at 572–73 ("History shows that Congress knows how to abrogate the absolute priority rule, and it has not done so here.").

102. *Id.* at 572.

103. *See*, *e.g.*, *id.* at 565–66; *In re* Kamell, 451 B.R. 505, 508 (Bankr. C.D. Cal. 2011) ("[The broad] reading seems rather convoluted and strained considering the language . . . ."); *In re* Karlovich, 456 B.R. 677, 682 (Bankr. S.D. Cal. 2010); *In re* Gelin, 437 B.R. 435, 442 (Bankr. M.D. Fla. 2010) ("[Congress] could have simply stated that § 1129(b)(2)(B)(ii) is inapplicable in a case in which the debtor is an individual.").

104. *See In re Maharaj*, 681 F.3d at 565–66; *see also In re Kamell*, 451 B.R. at 509.

have simply inserted the words "'except with respect to individuals' at the beginning of § 1129(b)(2)(B)(ii)."[105]

Another common discussion in narrow view opinions is the legislative history—or lack thereof. Because the legislative history regarding the changes to the absolute priority rule is generally sparse and unhelpful,[106] the *Maharaj* court discussed the lack of legislative history and the general themes of the BAPCPA as part of its statutory analysis.[107] In line with other narrow view courts, an important point of analysis for the *Maharaj* court was the creditor-friendly approach of the BAPCPA.[108] The court stated, "[n]o one who reads BAPCPA as a whole can reasonably conclude that it was designed to enhance the individual debtor's 'fresh start.'"[109]

The *Maharaj* court briefly addressed and rejected the arguments made by some of the broad view courts[110]—including the argument that Congress intended the amendments to harmonize Chapter 11 and Chapter 13 in the case of individual debtors.[111] Nor were public policy concerns persuasive, as the court had reached the conclusion that Congress did not intend to abrogate the absolute priority rule.[112] For instance, the court rejected the argument that confirmation is virtually impossible for individuals with the absolute priority rule in place.[113] In the view of the *Maharaj* court, negotiating a consensual plan is still very much a possibility.[114] The court suggested that debtors could "pay higher dividends, pay dissenting

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105. *In re Maharaj*, 681 F.3d at 566 (quoting *In re Karlovich*, 456 B.R. at 682).

106. *Id.* at 572 ("BAPCPA's legislative history is sparse."); *In re* Arnold, 471 B.R. 578, 607–09 (Bankr. C.D. Cal. 2012) ("Thus, the legislative history specifically referencing the addition of § 1115 and the amendment of § 1129(b)(2)(B)(ii) in BAPCPA as reflected in the House committee report is unhelpful because it simply restates the statutory language."); *In re Gelin*, 437 B.R. at 441 (finding the legislative history unhelpful and noting that it is entirely silent as to whether the drafters intended to abrogate the absolute priority rule for individuals).

107. *In re Maharaj*, 681 F.3d at 566, 572–73 (considering congressional intent in enacting the BAPCPA); *see also In re* Gbadebo, 431 B.R. 222, 229 (Bankr. N.D. Cal. 2010).

108. *In re Maharaj*, 681 F.3d at 573 ("This was a frequently expressed overall purpose of BAPCPA: i.e., to ensure that debtors who can pay back a portion of their debts do so.") (quoting *In re Gbadebo*, 431 B.R. at 229–30); *see also In re Kamell*, 451 B.R. at 508 ("[I]n general, BAPCPA has been read to tighten, not loosen, the ability of debtors to avoid paying what can reasonably be paid on account of debt.").

109. *In re Maharaj*, 681 F.3d at 573 (quoting *In re Gbadebo*, 431 B.R. at 229).

110. *Id.* at 565–66.

111. *Id.* at 566.

112. *Id.* at 574.

113. *Id.* at 575 ("Moreover, we remain unconvinced that the doom and gloom scenario presented by Debtors is an accurate picture of the state of bankruptcy law. . . . To the contrary, plan acceptance is still very much a possibility, even within the confines of the absolute priority rule.").

114. *Id*.

classes in full, or comply with the [absolute priority rule] by contributing prepetition property."[115]

B. Analysis of Broad View Cases

In contrast to the narrow view courts, several courts have come to the conclusion, and continue to hold, that the absolute priority rule does not apply to individual debtors filing under Chapter 11. Most notably, the Ninth Circuit Bankruptcy Appellate Panel's decision in *Friedman* provided thoughtful analysis and held that the absolute priority rule was inapplicable to individual debtors filing under Chapter 11 Bankruptcy.[116]

Like the *Maharaj* court, the *Friedman* court began its analysis by looking to the history of the absolute priority rule.[117] Unlike the narrow view courts, which focused on the legislative history of the absolute priority rule, the *Friedman* court concentrated on courts' treatment of the rule over time.[118] Noting that the rule has never been absolute, the court discussed judicial exceptions, including the "new value" exception and the equity interest rule for nonprofits.[119] Based on these exceptions, the court noted that the important historical implication is that "courts have always reviewed § 1129(b)(2)(B)(ii) through the lens of common sense and have approached legislative interpretation in a way to facilitate the goals of the statute."[120]

With this goal in mind, the court stressed that rather than focusing on specific words in statutes, which may carry duplicate meanings, more importance should be placed on reading words "in context with the sentence, the paragraph, and the entire text of the statute (in this case, the Bankruptcy Code)."[121] The court pointed out that the word "interest" in § 1129(b)(2)(B)(ii) has been given various meanings throughout its history,[122] and rejected the argument that because words may have various usages there necessarily exists ambiguity.[123]

After discussing the history of the absolute priority rule, the court examined the language added by the 2005 BAPCPA amendments to the Bankruptcy Code. The court determined that this language was clear and

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115. *Id.* (quoting *In re* Friedman, 466 B.R. 471, 491 (B.A.P. 9th Cir. 2012) (Jury, J., dissenting)).

116. *See In re Friedman*, 466 B.R. at 473.

117. *See id.* at 478; *In re Maharaj*, 681 F.3d at 571–73.

118. *In re Friedman*, 466 B.R. at 479.

119. *See supra* Part I.B.1.

120. *In re Friedman*, 466 B.R. at 479

121. *Id.*

122. *Id.* Courts have agreed that although the term "equity interest" does not appear anywhere in § 1129(b)(2)(B)(ii), the term "interest" means an "equity interest" in a for-profit corporation—fulfilling the goal of protecting unsecured creditors from unscrupulous corporate shareholders. *Id.*; *see also In re* Gen. Teamsters, Warehousemen & Helpers Union, Local 890, 265 F.3d 869, 873–74 (9th Cir. 2001); *In re* Wabash Valley Power Ass'n, Inc., 72 F.3d 1305, 1314–15 (7th Cir. 1995).

123. *In re Friedman*, 466 B.R. at 479.

unambiguous.[124] In the court's view, the language in § 1115 incorporated all precommencement property of the estate under § 541.[125] The court concluded that because "included" is not a word of limitation, the plain language of §§ 1115 and 1129(b)(2(B)(ii) demonstrates that the absolute priority rule no longer applies to individual debtors.[126] The *Friedman* court determined that due to the unambiguous meaning in the words of the amendments, "[r]ecourse to legislative history and spirited analytics [was] unnecessary."[127] Other courts taking the broad view have also held that §§ 1115 and 1129(b)(2)(B)(ii) are comprised of clear and unambiguous language.[128]

However, other broad view courts found the language to be ambiguous.[129] One court reached the same result as the *Friedman* court on the basis of the context in which the ambiguous word or phrase is used in English, and the context in the overall statutory scheme of the Bankruptcy Code.[130] The *Shat* court determined that "[g]iven the relatively straightforward reading of the statute supporting the broader reading, and the general rehabilitative aim of chapter 11 . . . Section 1129(b)(2)(B)(ii)'s exception extends to *all* property of the estate."[131]

In support of its conclusion, the *Friedman* court also noted "significant contextual concordance" in reading §§ 1115 and 1129(b)(2)(B)(ii) to mean that the absolute priority rule no longer applied to individuals.[132] For instance, numerous changes, triggered by BAPCPA, making Chapter 11 similar to Chapter 13 are consistent with eliminating the absolute priority rule for individuals.[133] Because of the numerous changes made to Chapter 11 of the Bankruptcy Code that mirrored Chapter 13, the court found that "clearly, the drafters of § 1129(a)(15) tried to create symmetry between [C]hapters 11 and 13 for individual debtors."[134] The

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124. *Id.* at 482–84.

125. *Id.* at 482.

126. *Id.*

127. *Id.* at 484.

128. *E.g.*, *In re* Tegeder, 369 B.R. 477, 480 (Bankr. D. Neb. 2007) ("Since § 1115 broadly defines property of the estate to include property specified in § 541, as well as property acquired post-petition and earning from service performed post-petition, the absolute priority rule no longer applies to individual debtors who retain property of the estate under § 1115."); SPCP Group, L.L.C. v. Biggins, 465 B.R. 316, 322–23 (M.D. Fla. 2011) ("Reading these statutes together, 'property of the estate' for purposes of Section 1115 includes property and earnings acquired both before and after the commencement of the bankruptcy case. The meaning of these statutes is clear, and therefore, the Court's inquiry stops here.") (citing Reeves v. Astrue, 526 F.3d 732, 734 (11th Cir. 2008)).

129. *See In re* Shat, 424 B.R. 854, 863 (Bankr. D. Nev. 2010); *In re* Roedemeier, 374 B.R. 264, 274–76 (Bankr. D. Kan. 2007).

130. *See In re Shat*, 424 B.R. at 863–65.

131. *Id.* at 865.

132. *In re Friedman*, 466 B.R. at 481.

133. *See id.* (These similarities include "(1) the new requirement for dedication of all debtor's disposable income for five years, (2) the straight-forward best interest of creditors test, and (3) the delay of issuance of discharge until the plan has been fully consummated"). *See also infra* notes 168–172 and accompanying text.

134. *In re Friedman*, 466 B.R. at 484.

court focused special attention on the new requirement that a debtor contribute five years of disposable income.[135] If the absolute priority rule was maintained in individual Chapter 11 cases, it would illogically "remove the debtor's means of production of debtor's disposable income" in most cases, and thus the new disposable income rule would be superfluous.[136]

Other broad view courts follow the same analysis with regard to congressional intent as evidenced by similarities between Chapters 11 and 13.[137] For example, a recent U.S. Bankruptcy Court opinion discusses that Congress adopted and applied many of Chapter 13's principles to the Chapter 11 amendments in an attempt to ensure no easy escape from means testing for individuals.[138] The 2005 revisions brought individual Chapter 11's more in line with Chapter 13,[139] and a broad reading of them helps to explain why "a number of changes . . . were made to Chapter 11, namely, so that it could function for individual debtors much like Chapter 13 does."[140]

The *Friedman* court concluded its analysis by rejecting the narrow view contention that a broad reading of the amendments created an anomaly in that a debtor may ignore votes that the debtor must solicit from an impaired creditor.[141] In the eyes of the *Friedman* court, a no vote is not ignored, but is trumped by the disposable income test[142] if its requirements are satisfied.[143] The court found the interpretation by the narrow view courts to be speculative analysis that merely suggested a theoretical possibility unlikely in reality.[144]

III. COURTS SHOULD ADOPT THE BROAD VIEW

The current state of the law regarding whether the absolute priority rule applies to individuals is unresolved and has created uncertainty in consumer bankruptcy practice. In order to fix this problem, additional circuit courts, and eventually the U.S. Supreme Court, should take up the issue and follow the broad view courts in abrogating the absolute priority rule for individual debtors filing

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135. *Id.* at 481–82; *see also* 11 U.S.C. § 1129(a)(15)(B) (2012).

136. *In re Friedman*, 466 B.R. at 482.

137. *Id.*; *In re* O'Neal, 490 B.R. 837, 850–51 & n.10 (Bankr. W.D. Ark. 2013).

138. *See In re O'Neal*, 490 B.R. at 851.

139. *See In re Friedman*, 466 B.R. at 484.

140. *In re* Roedemeier, 374 B.R. 264, 275 (Bankr. D. Kan. 2007).

141. *In re Friedman*. 466 B.R. at 483 ("[I]f §§ 1129(b)(2)(B)(ii) and 1115 are read to eliminate the 'absolute priority rule' for individual chapter 11 debtors, the Court is faced with a procedural anomaly. If the plan proposes to pay them anything, the debtor is required to send them a ballot. Yet, their vote can be ignored.") (quoting *In re* Gbadebo 431 B.R. 222, 230 (Bankr. N.D. Cal. 2010)).

142. "The court shall confirm a plan . . . if . . . the value of the property to be distributed under the plan is not less than the projected disposable income of the debtor (as defined in section 1325(b)(2)) to be received during the 5-year period beginning on the date that the first payment is due under the plan, or during the period for which the plan provides payments, whichever is longer." 11 U.S.C. § 1129(a)(15)(B) (2012).

143. *In re Friedman*, 466 B.R. at 483–84.

144. *Id.*

under Chapter 11. Although the narrow view has recently become the majority rule—especially as shown by *Maharaj*, *Lively*, and *Stephens*—this is due in large part to a line of reasoning stemming from flawed analysis in *Gbadebo*, and an unnecessary convolution of plain legislative language.

In addition to highlighting the flawed analysis applied by narrow view courts, this Note argues that the broad view is superior based on various methods of statutory interpretation, which strongly support the abrogation of the absolute priority rule with respect to individual Chapter 11 debtors. This statutory analysis includes consideration of the statutory language at issue, the framework and wording of other sections of the Bankruptcy Code, and the history of the absolute priority rule. Furthermore, this Note argues that the broad view is appropriate based on the important practical implications and problems surrounding application of the rule to individuals, including the difficulty of confirming a plan of reorganization and the issue of whether individuals may retain exempt property.

A. Statutory Interpretation

There are three schools of thought with respect to statutory interpretation: intentionalism, purposivism, and textualism.[145] Intentionalism is the view that a court should attempt to discover and apply the legislature's original intent.[146] Purposivism is the view that a court should look to the purpose of legislation and interpret the law to solve ambiguities.[147] Textualism is the view that a court should solely refer to the plain meaning of the statutory language.[148] These theories of interpretation are inconsistently used, and judges often use practical reason rather than a specific theory of interpretation.[149] It is important to keep this in mind when anticipating a court's theory of interpretation and arguing for a certain construction. However, a detailed analysis of a statute's language, structure, legislative history, and policy consequences is important because the U.S. Supreme Court consistently interprets statutes using all of these methods.

1. The Plain Language of §§ 1115 and 1129(b)(2)(b)(ii)

This Note argues that a close look at the language of §§ 1115 and 1129(b)(2)(B)(ii) mandates a finding that the rule is abrogated with respect to individuals. The Supreme Court "has never insisted that a legislative body articulate its reasons for enacting a statute."[150] When the language of the statute is clear, it must be assumed that Congress intended what it enacted.[151] And, "when the statute's language is plain, the sole function of the courts—at least where the disposition required by the text is not absurd—is to enforce it according to its

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145. William N. Eskridge & Philip P. Frickey, *Statutory Interpretation as Practical Reasoning*, 42 STAN. L. REV. 321, 324 (1990).

146. *Id.* at 325.

147. *Id.* at 333–34.

148. *Id.* at 340–41.

149. *Id.* at 321–22.

150. U.S. R.R. Ret. Bd. v. Fritz, 449 U.S. 166, 179 (1980).

151. *See id.*

terms."[152] Ordinary meaning should be given to undefined terms,[153] and a statute should be construed so that effect is given to all its provisions.[154] It is irrelevant whether Congress wrote a law in the clearest way possible, and once a court finds that there is a plain meaning to a statute, a result will be deemed absurd only if it is unthinkable, bizarre, or demonstrably at odds with the intentions of its drafters.[155]

The plain language of § 1129(b)(2)(b)(ii), read in conjunction with § 1115 and § 541, shows that the absolute priority rule no longer applies to individual Chapter 11 debtors. The 2005 BAPCPA legislation added a new clause in § 1129(b)(2)(b)(ii), created § 1115, and cross-referenced the preexisting § 541 as displayed in the table below.

Addition to § 1129(b)(2)(B)(ii)	**§ 1115**	**§ 541**
In a case in which the debtor is an individual, the debtor may retain property included in the estate under section 1115	In a case in which the debtor is an individual, property of the estate includes, in addition to the property specified in section 541— • all property of the kind specified in section 541 that the debtor acquires after the commencement of the case . . . • earnings from services performed by the debtor after the commencement of the case . . .	The estate includes all legal or equitable interests of the debtor in property as of the commencement of the case

Thus, when these portions of the statutes are combined into one sentence, the statute naturally reads:

152. Hartford Underwriters Ins. Co. v. Union Planters Bank, 530 U.S. 1, 6 (2000) (quoting United States v. Ron Pair Enters., Inc., 489 U.S. 235, 241 (1989) (internal quotations omitted)).

153. Hamilton v. Lanning, 130 S. Ct. 2464, 2471 (2010) (citing Asgrow Seed Co. v. Winterboer, 513 U.S. 179, 187 (1995)).

154. Corley v. United States, 556 U.S. 303, 314 (2009) (citing Hibbs v. Winn, 542 U.S. 88, 101 (2004)).

155. *See* Demarest v. Maspeaker, 498 U.S. 184, 190–91 (1991) (citing Griffin v. Oceanic Contractors, Inc., 458 U.S. 564, 571 (1982)).

> In a case in which the debtor is an individual, the debtor may retain property included in the estate under § 1115 . . . under § 1115, property of the estate includes, in addition to all legal or equitable interests of the debtor in property as of the commencement of the case, all post-commencement earnings and property.

Interpreted together, the statutes show that Congress intended to allow individual debtors to retain not only postcommencement property and earnings, but also precommencement property included under § 541.[156] This is the view adopted by broad view courts, and it is in accord with an ordinary reading of the statutory language.[157]

Narrow view courts find the word "included" to mean something closer to "added."[158] This interpretation is unnecessarily confusing. Congress clearly understood the difference between the words "include" and "add," as both words are used in the BAPCPA amendments.[159] Ordinary meaning should be given to all words in a statute.[160] Add is defined as "to join or unite so as to bring about an increase or improvement."[161] Include is defined as "to take in or comprise as part of a whole or group."[162] The definition of include clearly describes the word as part of a larger whole, not as a word of limitation, or as only referring to the additional part of a whole.[163] To limit the scope of estate property, as narrow view courts do, would require § 1129(b)(2)(B)(ii) to read: "included, except for the property set out in Section 541," and would require § 1115 to read: "in addition to, but not inclusive of the property described in Section 541."[164] In fact, all of the initial cases held that the absolute priority rule did not apply to individuals—many deciding this based on plain language analysis.[165]

It was not until *Gbadebo*, which misstated the actual language of § 1115, that a bankruptcy court found the absolute priority rule intact for individual Chapter 11 filers.[166] Subsequently, many courts relied on, and cited, *Gbadebo*

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156. *In re* Friedman, 466 B.R. 471, 482–84 (B.A.P 9th Cir. 2012).

157. *Id.*; *In re* Tegeder, 369 B.R. 477, 480 (Bankr. D. Neb. 2007); SPCP Group, L.L.C. v. Biggins, 465 B.R. 316, 322–23 (M.D. Fla. 2011).

158. *In re Friedman*, 466 B.R. at 482 & n.20 (citing Am. Surety Co. v. Marotta, 287 U.S. 513, 517 (1933)); *See also* Mendenhall, *supra* note 35, at 13.

159. *See* 11 U.S.C. §§ 541, 1115, 1129(b)(2)(b)(ii) (2006).

160. Hamilton v. Lanning, 130 S. Ct. 2464, 2471 (2010) (citing Asgrow Seed Co. v. Winterboer, 513 U.S. 179, 187 (1995)).

161. *Add,* MERRIAM-WEBSTER DICTIONARY ONLINE, http://www.merriam-webster.com/dictionary/add (last visited Feb. 15, 2013).

162. *Include,* MERRIAM-WEBSTER DICTIONARY ONLINE, http://www.merriam-webster.com/dictionary/include (last visited Feb. 15, 2013).

163. *In re Friedman*, 466 B.R. at 482.

164. *Id.*

165. *In re* Shat, 424 B.R. 854, 856 (Bankr. D. Nev. 2010); *In re* Johnson, 402 B.R. 851, 852–53 (Bankr. N.D. Ind. 2009); *In re* Roedemeier, 374 B.R. 264, 276 (Bankr. D. Kan. 2007); *In re* Tegeder, 369 B.R. 477, 479 (Bankr. D. Neb. 2007); *In re* Bullard, 358 B.R. 541, 543–44 (Bankr. D. Conn. 2007).

166. *See* 431 B.R. 222, 229 (N.D. Cal. 2010).

when holding that "included in" either meant the equivalent of "added to,"[167] or that the language was ambiguous due to the fact that other courts had interpreted it differently.[168] Compare the language used by the *Gbadebo* court with the actual language of the statute:

> *Gbadebo*: "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."[169]
>
> § 1115: "in a case in which the debtor is an individual, property of the estate *includes, in addition to the property specified in section 541*," the debtor's post petition property and earnings.[170]

By inverting the order of the clauses, the court's analysis—that "includes in" only refers to the two categories of postpetition property—could be plausible. This is because *Gbadebo's* phrasing stresses the "in addition" language, thus making a clear distinction between the property of the estate in § 541 and the newly added postpetition property and earnings. Consequently, whether § 541 property is included in the estate "under § 1115" by the words "in addition" would be a necessary determination. However, the word "includes" in § 1115 actually precedes "in addition to the property specified in § 541," which reads in an entirely different manner. When read as written in the statute, the words are not ambiguous.

Not only did the *Gbadebo* court invert the order of the clauses, but it also read the words "included in the estate *under* section 1115"[171] to mean "added to the bankruptcy estate *by* § 1115."[172] The language could be ambiguous if the statute read that § 541 property was "added" to the estate "by" § 1115, and it has in fact been confused in the sequence of cases citing this misstatement of the statute. However, a plain and accurate reading shows that § 541 property is "included" in the estate "under" § 1115, not "added by."

Narrow view courts also question whether the "awkward" language of § 1115(a) would have been the clearest way to effect the change Congress made, and they use that as proof that Congress intended no such effect.[173] However, speculation regarding ways that Congress may have drafted the statute with greater

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167. *See In re* Lively, 467 B.R. 884, 891 (S.D. Texas 2012); *In re* Karlovich, 456 B.R. 677, 681–82 (Bankr. S.D. Cal. 2010); *In re* Mullins, 435 B.R. 352, 360–61 (Bankr. W.D. Va. 2010).

168. *In re* Arnold, 471 B.R. 578, 598–99 (Bankr. C.D. Cal. 2012); *In re* Lindsey, 453 B.R. 886, 903–04 (Bankr. E.D. Tenn. 2011).

169. *In re Gbadebo*, 431 B.R. at 228–30.

170. 11 U.S.C. § 1115 (2012) (emphasis added).

171. 11 U.S.C. § 1129(b)(2)(B)(ii) (2012) (emphasis added).

172. *In re Gbadebo*, 431 B.R. at 229 (emphasis added) ("The Court would read the phrase 'included in the estate under section 1115' to be reasonably susceptible to only one meaning: i.e., added to the bankruptcy estate by § 1115.").

173. *In re* Maharaj, 681 F.3d 558, 565–66 (4th Cir. 2012); *In re* Kamell, 451 B.R. 505, 508–10 (Bankr. C.D. Cal. 2011); *In re* Karlovich, 456 B.R. 677, 682 (Bankr. S.D. Cal. 2010); *In re* Gelin, 437 B.R. 435, 441–42 (Bankr. M.D. Fla. 2010).

clarity is not a valid justification for rejecting a plain reading of the language actually used.[174] This is especially true here, where the language in § 1115 was copied from language in § 1306, showing that Congress was attempting to create symmetry between the chapters. A desire for consistency is the most plausible explanation for the unclear language. Ignoring the plain meaning and instead declaring that Congress could have effected the change in a clearer manner is incorrect and unnecessarily complicates the inquiry.

2. The Changes Made to Chapter 11 Mirror Language in Chapter 13

An analysis of other portions of the Bankruptcy Code shows that Congress intended that the absolute priority rule no longer apply to individuals filing under Chapter 11. Namely, several BAPCPA amendments to Chapter 11 of the Code evidence congressional attempts to harmonize Chapter 11 for individuals with existing Chapter 13 provisions.[175] For instance: the disposable income test,[176] permitting modification of a plan after substantial consummation,[177] delaying the

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174. *See* U.S. R.R. Ret. Bd. v. Fritz, 449 U.S. 166, 179 (1980).

175. *See In re* Shat, 424 B.R. 854, 862–64 (Bankr. D. Nev. 2010); Brief for Appellants, *supra* note 52, at 13; *See also Chapter 11: Reorganization Under the Bankruptcy Code*, *How Chapter 11 Works*, UNITED STATES COURTS, http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/Chapter11.aspx (last visited Sept. 28, 2013). For many individuals:

> [C]hapter 11 bears some similarities to chapter 13. For example, property of the estate for an individual debtor includes the debtor's earnings and property acquired by the debtor after filing until the case is closed, dismissed or converted; funding of the plan may be from the debtor's future earnings; and the plan cannot be confirmed over a creditor's objection without committing all of the debtor's disposable income over five years unless the plan pays the claim in full, with interest, over a shorter period of time.

Id. (citing 11 U.S.C. §§ 1115, 1123(a)(8), 1129 (a)(15) (2012)).

176. *Compare* 11 U.S.C. § 1129(a)(15) ("In a case in which the debtor is an individual and in which the holder of an allowed unsecured claim objects to the confirmation of the plan—the value . . . of the property to be distributed under the plan is not less than the projected disposable income of the debtor . . . to be received during the 5-year period beginning on the date that the first payment is due under the plan, or during the period for which the plan provides payments, whichever is longer."), *with id.* § 1325(b)(1)(B) (2012) ("[A]ll of the debtor's projected disposable income to be received in the applicable commitment period beginning on the date that the first payment is due under the plan will be applied to make payments to unsecured creditors under the plan.").

177. *Compare id.* § 1127(e) (2012) ("If the debtor is an individual, the plan may be modified at any time after confirmation of the plan . . . whether or not the plan has been substantially consummated . . . to— (1) increase or reduce the amount of payments on claims of a particular class provided for by the plan; (2) extend or reduce the time period for such payments; or (3) alter the amount of the distribution to a creditor whose claim is provided for by the plan . . ."), *with id*. § 1329(a) (2012) ("At any time after confirmation of the plan . . . the plan may be modified . . . to—(1) increase or reduce the amount of payments on claims of a particular class provided for by the plan; (2) extend or reduce the time for such payments; (3) alter the amount of the distribution to a creditor whose claim is provided for by the plan . . .").

discharge until the completion of all plan payments,[178] and permitting a discharge for cause before all payments are completed,[179] are all terms that appear in both chapters after the BAPCPA amendments.

Of these amendments to Chapter 11, the disposable income requirement of § 1129(a)(15) is particularly important because it negates the need for the absolute priority rule for individual debtors.[180] The disposable income requirement applies only to individuals and mandates that a debtor commit all disposable income over the next five years to the plan unless the plan pays the claim in full.[181]

A narrow reading of § 1129(b)(2)(B)(ii), therefore, only exempts the debtor's disposable income starting five years after confirmation.[182] This narrow reading would only exempt "miserly post-fifth-year income." This interpretation is very different from the alternative broad interpretation, which would exclude the "generous designation of all estate property,"[183] or, in other words, precommencement property, postcommencement property, and postcommencement earnings after the contribution of five years worth of disposable income.

Another extremely important BAPCPA amendment to Chapter 11 is the new exception to the absolute priority rule that, "[i]n a case in which the debtor is

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178. *Compare id.* § 1141(d)(5)(A) (2012) ("[U]nless after notice and a hearing the court orders otherwise for cause, confirmation of the plan does not discharge any debt provided for in the plan until the court grants a discharge on completion of all payments under the plan . . . ."), *with id.* § 1328(a) (2012) ("[A]s soon as practicable after completion by the debtor of all payments under the plan . . . unless the court approves a written waiver of discharge executed by the debtor after the order for relief under this chapter, the court shall grant the debtor a discharge of all debts provided for by the plan . . . .").

179. *Compare id.* § 1141(d)(5)(B) ("[A]t any time after the confirmation of the plan, and after notice and a hearing, the court may grant a discharge to the debtor who has not completed payments under the plan if— (i) the value, as of the effective date of the plan, of property actually distributed under the plan on account of each allowed unsecured claim is not less than the amount that would have been paid on such a claim if the estate had been liquidated under chapter 7 on such date; (ii) modification of the plan under section 1127 is not practicable; and (iii) subparagraph (C) permits the court to grant a discharge."), *with id.* § 1328(b) ("[A]t any time after confirmation of the plan and after notice and a hearing, the court may grant a discharge to the debtor that has not completed payments under the plan only if— (i) the debtor's failure to complete such payments is due to circumstances for which the debtor should not justly be held accountable; (ii) the value, as of the effective date of the plan, of property actually distributed under the plan on account of each allowed unsecured claim is not less than the amount that would have been paid on such a claim if the estate of the debtor had been liquidated under chapter 7 of this title on such date; and (ii) modification of the plan under section 1329 of this title is not practicable.").

180. *See In re* Shat, 424 B.R. 854, 863–64 (Bankr. D. Nev. 2010).

181. 11 U.S.C. § 1129(a)(15).

182. *In re Shat*, 424 B.R. at 864.

183. *Id.*

an individual, the debtor may retain property included in the estate under section 1115 . . . ."[184]

The legislation simultaneously created § 1115, which states:

> 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 . . .
>
> 2. Earnings from services performed by the debtor after the commencement of the case . . .[185]

This section closely mirrors § 1306:

> a. Property of the estate includes, in addition to property specified in section 541 of this title—
>
> 1. All property of the kind specified in such section that the debtor acquires after the commencement of the case . . .
>
> 2. Earnings from services performed by the debtor after the commencement of the case . . .[186]

Congress most likely chose to use the awkward phrasing in § 1115 in order to maintain consistency in the Code and to mirror its Chapter 13 equivalent. The similarities identified in this section are strong evidence of a congressional attempt to harmonize Chapter 11 for individuals with Chapter 13, and support the abrogation of the absolute priority rule.

3. The Statutory Framework of Chapter 11, the Statutory Framework of the BAPCPA, and the History of the Absolute Priority Rule

Chapter 11 as a whole is designed to facilitate reorganization, rather than liquidation, and allows a debtor to enter into an agreement with creditors so that—with certain modifications—a business may continue to operate.[187] Chapter 11 is an alternative to Chapter 7 and is intended to avoid liquidations—ultimately leading to the preservation of jobs, a better return for owners, and more paid to creditors.[188] The working presumption is that a debtor's assets will be more valuable if "used in a rehabilitated business than if sold for scrap."[189] This policy is best served by the broad view, particularly in light of its ability to facilitate

184. 11 U.S.C. § 1129(b)(2)(B)(ii) (emphasis added).
185. *Id.* § 1115(a)(1)–(2) (2012).
186. *Id.* § 1306 (2012).
187. *See* Nat'l Labor Relations Bd. v. Bildisco, 465 U.S. 513, 527 (1984); *In re* Thirtieth Place, Inc., 30 B.R. 503, 504 (B.A.P. 9th Cir. 1983); *see also* Brief for Appellants, supra note 52, at 2 (citation omitted).
188. United States v. Whiting Pools, 462 U.S. 198, 203–07 (1983).
189. *Id.* at 203.

reorganization. This is as opposed to narrow view courts, which fail to give importance to the comprehensive goal of Chapter 11 of the Bankruptcy Code—to grant a fresh start to the honest but unfortunate debtor.[190]

Narrow view courts rely on the fact that the BAPCPA was generally creditor-friendly legislation. However, in addition to creating creditor protections, the stated purpose of BAPCPA "is to improve bankruptcy law and practice by restoring personal responsibility and integrity in the bankruptcy system and ensure that the system is fair for *both* debtors and creditors."[191] Other creditor protection provisions, such as the good faith requirement of § 1129(a)(3), the best interests liquidation test under § 1129(a)(7), and recent amendments in the BAPCPA adopted from Chapter 13, remain. Specifically, the five-year disposable income requirement and means testing were added to protect creditors who would otherwise receive only what they would receive in liquidation.[192] That certain provisions of BAPCPA were intended to protect creditors from abuses, however, does not mean that every provision of BAPCPA should be analyzed from only a pro-creditor point of view, especially as the law also had a stated consumer protection purpose in its title.[193] In other words, a provision protecting creditors and a different provision ensuring the accessibility of Chapter 11 to individuals are not necessarily mutually exclusive. For instance, adding the disposable income requirement for individuals, while also allowing individuals to retain both pre and postcommencement property, as they can in Chapter 13—and as they could under a broad view—is consistent with congressional intent to protect creditors. The provisions of BAPCPA that were added to Chapter 11, and that mirror those in Chapter 13, all dealt with individual bankruptcies only. The parallel language simply shows congressional intent to align the chapters for individuals and still adequately protects creditors with the disposable income test.

Furthermore, a look at the history of the rule and how it works shows that congressional elimination is not as far fetched as some narrow view courts believe. Although the absolute priority rule was never intended for individuals in the first place and has undergone a history of both elimination and exceptions, narrow view courts now deem the rule as sacrosanct.[194] The absolute priority rule—originating as a judicially created doctrine—has never adapted well to individual cases.[195] Moreover, the rule was eliminated completely in 1952 and did not reemerge for 26 years.[196] The rule is also still subject to the judicially recognized new value

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190. Brief for Appellants, *supra* note 52, at 3 (citing Marrama v. Citizens Bank of Mass., 549 U.S. 365, 367 (2007)).

191. H.R. Rep. No. 109–31(I), at 2 (2005), *reprinted in* 2005 U.S.C.C.A.N. 88, 89 (emphasis added).

192. *See id.*

193. *Id.* at 2–3.

194. See *In re* Maharaj, 681 F.3d 558, 571–72 (4th Cir. 2012) (referring to the absolute priority rule for individuals as "well-established," and a change in the absolute priority rule as a "dramatic departure").

195. *See* Markell, *supra* note 44, at 88.

196. *See In re Maharaj*, 681 F.3d at 561.

exception and equity interest exception.[197] Due to the inadequacy of the new value exception for individuals, forbidding these equity holders from retaining any interest is contrary to permitting reorganization. In simple terms, unless the debtor can get all classes to accept the plan, the narrow view allows reorganization, but only if all creditors are paid in full. Otherwise, even a single small claimholder can halt reorganization and force the debtor to liquidate.

B. Policy Concerns Regarding the Narrow View

Several policy concerns also highlight the problems with the narrow view, including the difficulty of confirming a plan for sole proprietors that wish to reorganize and continue their business, and the treatment of exempt property. Without a realistic opportunity for individuals who own businesses to negotiate a plan with unsecured creditors while continuing to operate their businesses, Chapter 11 of the Bankruptcy Code loses its purpose—to facilitate reorganizations. A broad reading of the statutory language provides the opportunity for individuals to negotiate with unsecured creditors while reorganizing rather than liquidating. A broad reading also avoids the problem of whether property exemptions apply to individuals filing under Chapter 11.

1. Difficulty of Confirming a Plan of Reorganization

Broad view courts think that retaining the absolute priority rule for individuals does not only affect negotiations, but actually stalls bankruptcies and ruins reorganization plans.[198] Narrow view courts repeatedly state that all an individual debtor needs to do in order to confirm a plan is "sweeten the pot" or propose a reasonable dividend that a creditor would not receive in a Chapter 7 case.[199]

A major issue with the narrow view courts' reasoning is that not all debtors have the option of filing under a different chapter, thus restricting their negotiating power.[200] Additionally, if debtors had the option of paying creditors in full, it is unlikely that they would be filing for bankruptcy at all. The reality is that as a practical matter, few individuals could use Chapter 11 under the narrow view.[201] Oftentimes, unsecured creditors vote to reject a plan regardless of whether they would get more than in Chapter 7, or if five years of the debtor's disposable income is already part of the plan.[202]

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197. *In re* Friedman, 466 B.R. 471, 478–79 (B.A.P. 9th Cir. 2012).

198. *In re* Shat, 424 B.R. 854, 858 (Bankr. D. Nev. 2010).

199. *In re* Maharaj, 681 F.3d 558, 574 (4th Cir. 2012) (citing *In re* Gbadebo, 431 B.R. 222, 229–30 (Bankr. N.D. Cal. 2010)).

200. *See supra* notes 14–20 and accompanying text.

201. *In re Shat*, 424 B.R. at 858 (citing *In re* Gosman, 282 B.R. 45, 52 (Bankr. S.D. Fla. 2002) ("this uniform application effectively mean[s] that no individual debtor could ever confirm a chapter 11 plan."). This quote may be somewhat of an overstatement, but expresses the concern that a narrow reading may make Chapter 11 unavailable to individuals.

202. Brief for Appellants, *supra* note 52, at 16.

2. If a Narrow View is Adopted, it is Unclear Whether Individual Debtors Could Retain Exempt Property

Individual debtors are permitted to exempt certain property from the estate under 11 U.S.C. § 522(b)–(c). Unless the case is dismissed, exempt property "is not liable during or after the case for any debt of the debtor that arose," or is deemed to have arisen, prepetition.[203] Bankruptcy is an area of litigation governed by both federal and state law, and Congress allows states to opt out of federal exemption law. As a result, wide disparities exist between states' exemption statutes.[204] Exempt property statutes typically include: a residence, motor vehicle, jewelry, and household items, up to a certain statutory amount.[205]

However, the absolute priority rule does not allow an unsecured junior creditor or interest holder to retain *any* property *under the plan* on account of such *junior* interest unless creditors are paid in full or all classes of creditors approve a reorganization plan—except, an individual debtor may retain property included in the estate under § 1115.[206] If a narrow view is adopted, and the debtor attempts a cram down, can the debtor retain any exempt property? Maybe.[207]

"Most courts have found that the interest of an individual debtor in property is junior to the claims of unsecured creditors." [208] So, what property did Congress intend for individuals to be able to keep? One interpretation is that "property" could mean nonexempt property.[209] However, this reading is contrary to the structure of the Code, which initially sweeps exempt property into property of the estate under § 541—so that it is under the control of the bankruptcy court until an individual debtor claims it as exempt under § 522. Furthermore, § 1129(b) does not allow junior interests to retain "any property," and under a plain reading exempt property clearly qualifies as such. Alternatively, if the interpretation of "property" does include exempt property, it would make little sense if the exception for an individual debtor pertained solely to property acquired postpetition—as narrow view courts read § 1129(b)—because exempt property is

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203. 11 U.S.C. § 522(c) (2012).

204. Ronel Elul & Narayanan Subramanian, *Forum-Shopping and Personal Bankruptcy*, 21 J. FIN. SERVICES RES. 233, 233–34 (2002).

205. *Id.* In addition to federal laws, all states have exemption laws, which specify certain property as beyond the reach of an individual's creditors. JOAN N. FEENEY, BANKRUPTCY LAW MANUAL § 5:34 (5th ed. 2012).

206. 11 U.S.C. § 1129(b)(2)(B)(ii) (2012).

207. *In re* Bullard, 358 B.R. 541, 544–45 (Bankr. D. Conn. 2007) (yes); *In re* Henderson, 321 B.R. 550, 559–61 (Bankr. M.D. Fla. 2005) (same); *In re* Shin, 306 B.R. 397, 404 n.17 (Bankr. D.D.C. 2004) (same); *In re* Egan, 142 B.R. 730, 733 (Bankr. E.D. Pa 1992) (same). *But see In re* Gosman, 282 B.R. 45, 51–52 (Bankr. S.D. Fla. 2002) (no); *In re* Kovalchick, 1995 WL 118171 (Bankr. E.D. Pa. 1995) (same); *In re* Ashton, 107 B.R. 670, 674 (Bankr. N.D. 1989) (same); *In re* Johnson, 101 B.R. 307, 308–09 (Bankr. M.D. Fla. 1989) (same); *In re* Yasparro, 100 B.R. 91, 95 (Bankr. M.D. Fla. 1989) (same).

208. Ahart, *supra* note 18, at 738 & n.34.

209. *Id.* at 738.

determined as of the date the petition is filed and is invariably limited to the debtor's interest in prepetition assets.[210]

Many narrow view courts have failed to address the issue of whether an individual debtor may retain exempt property in their analysis of whether the absolute priority rule still applies to individual Chapter 11 debtors.[211] It seems inherently wrong that a debtor would be required to surrender exempt property, which is no longer property of the estate after it is exempted[212] and is no longer "liable during the case (or after) for prepetition debts."[213] The problem with the narrow view is that it does not recognize this issue, and thus creates a big problem for making sense of the Code as applied to individuals. The effect of the narrow view is that in addition to individuals being forced into liquidating their business and possibly their sole source of income, they also can no longer keep their homestead or other exempted property. This effect is too harsh on debtors and would frustrate the purpose of the Bankruptcy Code as a means to give the honest but unfortunate debtor a fresh start.[214] If some states, in holding that the absolute priority rule continues to apply to individuals, also rule that individuals are no longer allowed to keep any exempt property, Chapter 11 bankruptcy would no longer be a viable option.

As most narrow view courts believe that § 1115 is ambiguous as to whether the absolute priority rule applies to individual Chapter 11 plans, "analysis of how other provisions of the Bankruptcy Code function is appropriate."[215] Here, analysis of this provision creates serious concerns as to how the narrow view affects individual Chapter 11 debtors and clashes with their statutory right to exempt property.

The broad view, however, is more consistent with the statutory language and policy concerns. A "statute should be construed [to give effect] to all its provisions, so that no part will be inoperative or superfluous, void or insignificant."[216] By interpreting § 1115 to include the debtor's postpetition property *and* prepetition property, there exists no conflict between § 1129(b)(2)(B)(ii) and § 522(c).[217] Individual debtors would be permitted to keep exempt property as a part of all prepetition property. Thus, exclusion of individuals from the absolute priority rule is the best way to avoid the potentially nonsensical result.

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210. *Id.*

211. *See id.* at 740.

212. Exempt property is initially property of the estate under § 541 until debtor exempts the property under § 522(c). *See* 11 U.S.C. §§ 522(c), 541 (2012); *see also* Ahart, *supra* note 18, at 738.

213. Ahart, *supra* note 18, at 740.

214. *See* Marrama v. Citizens Bank of Mass., 549 U.S. 365, 367 (2007).

215. Ahart, *supra* note 18, at 752. Ahart's analysis demonstrates that invocation of the absolute priority rule may conflict with §§ 522(c) and 1123(c) and would restrict or undermine the operation of §§ 1123(a)(8), 1129(a)(7), 1129(a)(15), 1127, and 1141. *Id*.

216. Corley v. United States, 556 U.S. 303, 314 (2009) (brackets in original, citations and internal quotation marks omitted).

217. *See* Ahart, *supra* note 18, at 740–41.

The issue of exempt property is significant, and further analysis in this rarely discussed area will be necessary regardless of how courts rule on the applicability of the absolute priority rule to individuals in the future.

CONCLUSION

Due to the recent economic recession, the total number of individual Chapter 11 filings has increased dramatically, and discrepancies in court decisions regarding the application of the absolute priority rule have left the consumer bankruptcy practice in uncertainty. These conflicting interpretations cause a dramatically disparate impact among similarly situated individuals. In some jurisdictions, an individual is permitted to retain all pre and postcommencement property. In others, the debtor can retain only property and earnings acquired after five years of disposable income is contributed to the plan. This discrepancy is due to unnecessary convolution and flawed statutory analysis stemming from the opinion in *Gbadebo* and continuing through *Maharaj*, *Lively*, and *Stephens*. Additionally, the treatment of exempt property may increase this variance even further, resulting in required forfeiture of basic personal property.

A renewed analysis of the Bankruptcy Code's statutory framework; a careful look at the plain language of §§ 1129(b)(2)(b)(ii), 1115, and 541; and several practical concerns all show that the absolute priority rule was abrogated with respect to individual Chapter 11 debtors by the 2005 BAPCPA amendments. Consequently, if Congress does not resolve the question, and additional circuit courts address the issue, or if the Supreme Court grants *certiorari* and decides to resolve the split in authority, the absolute priority rule should not apply to individual debtors. This result would provide individuals filing under Chapter 11 a chance to meaningfully negotiate with creditors consistent with the goals of the Bankruptcy Code and the BAPCPA legislation.