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THE PARTIALLY SECURED CREDITOR UNDER CHAPTER XIII OF THE BANKRUPTCY ACT

Wayne C. Dabb, Jr.*

I. Introduction

Under current bankruptcy law, a partially secured creditor¹ can force a struggling debtor into straight bankruptcy² despite the debtor's voluntary attempt to rescue himself from insolvency under a Chapter XIII wage earner plan.³ Since the partially secured creditor has a security interest in the debtor's personal property, though it may be one of only negligible value, he is generally treated under Chapter XIII as a wholly secured creditor.⁴ If the partially secured creditor is affected by the wage earner

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¹A partially secured creditor is a secured creditor who has a security interest in collateral which is worth less than the debt secured thereby. See 10 W. COLLIER, *BANKRUPTCY* 47-48 (14th rev. ed. 1963); Copenhaver, *Bankruptcy--Rights and Powers in Chapter XIII*, 68 W. VA. L. REV. 375, 386-87 (1966). The partially secured creditor usually has his security interest in collateral such as an automobile, household furnishings, or tools which are subject to rapid depreciation and have a limited resale value. See Lee, *Who Is a Secured Creditor in Wage Earner Proceedings?*, 38 REF. J. 45 (1964); and Copenhaver, *supra*.

²Bankruptcy Act Chapters I-VII (1968)

³Bankruptcy Act §§601-86, 11 U.S.C. §§1001-86 (1968) [hereinafter all citations will be to the Bankruptcy Act only.] Chapter XIII provides a procedure which allows an insolvent wage earner to undertake voluntarily a plan to pay his debts through payments from future earnings under the supervision of a bankruptcy court without resorting to straight bankruptcy. In 1959, when amendments to the Bankruptcy Act were being considered, the House Judiciary Committee observed that:

...Chapter XIII provides a highly desirable method for dealing with the financial difficulties of individuals. It creates an equitable and feasible way for the honest and conscientious debtor to pay off his debts rather than have them discharged in bankruptcy. The power of the court to change the amount and maturity of installment payments makes chapter XIII particularly applicable to the present day financial problems generated by heavy installment buying.

H. R. REP No. 193, 86th Cong. 1st Sess.2(1959).

⁴See generally, Countryman, *Chapter XIII Wage Earner's Plans: Past, Present and Future*, 18 CATH. U.L. REV. 275,277 (1969).

plan, his assent to it is required before the court can confirm the plan. He may therefore, by his single dissent, thwart the debtor's attempt to resolve his financial problems under Chapter XIII even though the debtor's other secured or unsecured creditors agree to the wage earner plan.⁵ The partially secured creditor thereby obtains an inequitable advantage over the other creditors and is put in a position to undermine the usefulness of Chapter XIII as an alternative to straight bankruptcy. This article will examine the position of the partially secured creditor under Chapter XIII wage earner plans and will recommend ways to deal with him which can result in more equitable treatment of the debtor and other creditors and will at the same time effectuate the chapter's purpose.

II. The Role of the Partially Secured Creditor

A. Operation of Chapter XIII Wage Earner Plans

The operation of a Chapter XIII wage earner plan is quite simple. The wage earner-debtor⁶ submits a plan, either of composition⁷ or of extension,⁸ to the bankruptcy court. The court confirms the plan upon its acceptance by a majority in number and amount of the unsecured creditors and by all secured creditors who are "dealt with by the plan."⁹ The plan must provide

⁵Even though the plan is accepted by a majority in number and amount of the debtor's unsecured creditors, the court cannot confirm the plan if a secured creditor who is affected by it dissents. Bankruptcy Act § 652(1)(1968).

⁶"[W]age earner" shall mean an individual whose principal income is derived from wages, salary or commissions." Bankruptcy Act § 606(8) (1968).

⁷A composition plan is a plan which provides for payment of less than 100% of the debt owed by the wage earner-debtor to the unsecured creditors. #8 W. Collier, Bankruptcy ¶2.20 (14th rev. ed. 1963).

⁸An extension plan is a plan which provides for payment of 100% of the debt owed by the wage earner-debtor to unsecured creditors, but over an extended period of time—ordinarily not more than three years. Most wage earner plans are extension plans and the greater percentage of payments is made under such plans. In 1964, for example, 95% of the funds paid to creditors under Chapter XIII proceedings derived from extension plans. *Perry v. Commerce Loan Co.*, 383 U.S. 392, 395-396, n. 4 (1966).

⁹Bankruptcy Act § 652(1) (1968). "Dealt with by the plan" was defined in the rule announced in *Cheetham v. Universal SIT Credit Corp.*, 390 F.2d 234, 238 (1st Cir. 1968):

If Chapter XIII is to serve any real purpose where there are secured creditors, section 652 must be read as written, to require assent only of those "whose claims

for payment on all unsecured debts and may provide for debts secured by personal property. However, it cannot cover debts secured by real property, which debts must remain unaffected by the plan.¹⁰ Upon confirmation of the plan, the debtor submits the necessary amount of his earnings or wages to a trustee appointed by the court, and the trustee, in turn, makes the payments provided for under the plan.¹¹ Upon successful completion of the plan,¹² or, after three years, upon failure to perform in accordance with the plan where the court finds that such failure "was due to circumstances for which he could not justly be held accountable,"¹³ the debtor is discharged from liability for any amounts remaining unpaid on the debts under the plan.

Although a wage earner plan may be easily set up and administered, it is not always easy to obtain the acceptances required for confirmation. Most creditors, particularly unsecured creditors, recognize that such a plan is the best way to avoid the losses which would otherwise be thrust upon them by straight bankruptcy and therefore willingly accept a debtor's wage earner plan.¹⁴ Some secured creditors and some partially secured creditors, however, may refuse to accept the plan because they believe that with their security interest they can do better outside the plan.¹⁵ As a result, the plan may be frustrated *ab initio*.

are dealt with," meaning expressly adversely dealt with. Irrespective of what general inconveniences may occur to non-assenting secured creditors as a result of Chapter XIII proceedings, we hold that secured claims are dealt with only when the plan expressly limits the amount recoverable on the claim, or restricts the creditor's security interest.

But see In re O'Dell, 198 F. Supp. 389 (D. Kans. 1961), discussed in text *infra*, which holds that all of a debtor's secured creditors are "dealt with by the plan" because a Chapter XIII proceeding affects their security interest by its very nature.

¹⁰Bankruptcy Act §606(1) (1968).

¹¹Bankruptcy Act §633(4) (1968).

¹²Bankruptcy Act §660 (1968).

¹³Bankruptcy Act §661 (1968).

¹⁴See Comment, *The Bankruptcy Boom*, 77 HARV. L. REV. 1452, 1456 (1964).

¹⁵Comment, *Nonassenting Secured Creditors to Chapter XIII Wage Earner Plans*, 47 Tex. L. Rev. 302-303 (1969). When the debtor has become insolvent, the secured creditor may choose to reclaim the collateral, which may be worth as much as or more than the debt owed him, rather than take a chance on the debtor's ability to successfully complete his plan. Of course, with the partially secured creditor, the collateral is not worth as much as the debt owed him. However, even he may believe that there is less risk of loss if he forecloses and recovers what he can by selling the collateral.

B. Effect of Dissent by the Partially Secured Creditor

Since the partially secured creditor is considered as a wholly secured creditor and allowed thereby to prevent adoption of a proposed plan by his single dissent,¹⁶ he is placed in a strong bargaining position.¹⁷ By threatening to exercise his veto power, the partially secured creditor can demand that the plan provide for his payment *in full according to the terms of his contract* as a condition of his acceptance of the plan. Thus, the partially secured creditor would receive payment of both the secured and unsecured portions of his claim. A dilemma results. If the partially secured creditor is paid in full, according to the terms of his contract, there may well be insufficient funds remaining to make the wage earner plan workable.¹⁸ On the other hand, if his terms are not met and he is allowed to reclaim collateral that may be necessary to effectuate the plan, the plan will still be frustrated.¹⁹ Since the financial value of the partially secured creditor's security interest is, by definition, disproportionately small in relation to the debt owed him,²⁰ such a result is clearly undesirable. The partially secured creditor is given significantly greater control over the debtor's property than is warranted by his security interest. Moreover, the objectives of fairness and equity between creditor and creditor and between creditor and debtor which underlie the entire Bankruptcy Act²¹ are denied, and the specific

¹⁶Each secured creditor who is dealt with by the plan must assent to the plan in order for the court to confirm it. Bankruptcy Act §652(1) (1968). Since the partially secured creditor is treated as a secured creditor, his dissenting vote alone will prevent confirmation of the plan. Copenhaver, *supra* note 1, at 387.

¹⁷See Comment, *supra* note 15, at 306.

¹⁸The main problem here is that after the debtor has made his monthly payments to his secured creditors and then pays his partially secured creditors in full, the amount of money available for proportional distribution among his unsecured creditors may be so small that it would entail more in bookkeeping and collection costs than they would receive. This result is inequitable when one considers that the partially secured creditor whose security interest is worth very little is able to collect in full.

¹⁹*In re Pizzolato*, 268 F. Supp. 353 (W.D.Ark. 1967), was just such a case. The creditor attempted to foreclose and reclaim an automobile which was the debtor's only means of transportation to and from work. Without transportation, of course, the debtor would be unable to work to obtain the funds for the plan, the plan would fail, and the unsecured creditors would likely receive less than full payment on their claims. In light of these facts, the court held that the creditor's security interest would not be injured by the plan, and enjoined him from foreclosing.

²⁰Note 1, *supra*.

²¹*Vanston Bondholders Protective Comm. v. Green*, 329 U.S. 156, 165, 169 (1946). See also Copenhaver, *supra* note 1, at 388.

purpose of Chapter XIII of providing a means of relief and rehabilitation for wage earner-debtors²² is defeated.

Thus, the current operation of Chapter XIII with respect to the partially secured creditor²³ creates what one bankruptcy referee has called "perhaps the most perplexing of all problems in Chapter XIII."²⁴ In order to determine the proper solution to this problem, it is necessary to examine the body of law which has created it.

C. Current Treatment of Dissenting Secured and Partially Secured Creditors

It should be noted at the outset that the existing case law deals primarily with the wholly secured creditor and fails to consider the case of the partially secured creditor.²⁵ However, since the partially secured creditor is currently treated as a secured creditor under Chapter XIII, these cases have been allowed to govern the partially secured creditor as well.²⁶

Two different lines of thought have developed under Chapter XIII at both the district court and circuit court levels.²⁷ Although the cases representing both lines of reasoning ultimately result in allowing the secured creditor to enforce the terms of the contract creating his security interest, each line of cases has a different effect with respect to the utility of the wage earner plan involved. The first line of cases severely restricts the use of the wage earner plan by requiring that either *all* secured creditors assent to the plan as a condition of confirmation,²⁸ or that any dissenters be allowed to enforce their security interests and to reclaim their collateral. The second line of cases requires the assent of only those secured creditors who are *directly* dealt with by the plan,²⁹

²²Hallenbeck v. Penn Mutual Life Ins. Co., 323 F. 2d 566, 570 (4th Cir. 1963).

²³See generally Comment, *supra* note 15, at 306; Copenhaver, *supra* note 1, at 387-88.

²⁴Copenhaver, *supra* note 1, at 387.

²⁵Comment, *Bankruptcy: Enforcing a Chapter XIII Wage Earner's Plan over the Objection of a Secured Creditor*, 6 SAN DIEGO L. REV. 69, 77-78 (1969).

²⁶Copenhaver, *supra* note 1, at 386.

²⁷The District Courts of Kansas and Ohio and the 5th Circuit Court of Appeals follow the first line of cases, while the District Courts of Arkansas and Georgia and the 4th and 7th Circuit Courts of Appeals follow the second line of cases. See text accompanying notes 29-44 for a discussion of these cases.

²⁸See *In re O'Dell*, 198 F. Supp. 389 (D. Kans. 1961). See also note 9 *supra*.

²⁹See *Cheetham v. Universal CIT Credit Corp.*, 390 F.2d 234, discussed *supra* note 9.

and further seeks to make the wage earner plan practicable by preventing reclamation by dissenters, where necessary, on the condition that they receive full payment according to the terms of their contracts.

The restrictive line of cases with respect to Chapter XIII wage earner plans begins with *In re O'Dell*.³⁰ *O'Dell* involved a plan providing for payment of \$37 per week to secured creditors whose contracts had called for payments of \$38 per week. The court held that a wage earner plan must provide for full payment of all secured creditors according to the terms of their contracts in order to be confirmed.³¹ In discussing the problem, the court stated that:

...a plan proposed under Chapter XIII which does not provide for assumption of executory contracts by the trustee or otherwise make provision for the payment of the claims of secured creditors according to the terms of the instrument creating the debt, does *deal with* such claims. A plan without such provisions should not be confirmed unless accepted by the secured creditors.³² [Emphasis added.]

Thus the court was clearly of the opinion that even if the debtor had not purported to reduce the size of payments to secured creditors, indeed even if he had failed to mention secured creditors, the plan nonetheless "dealt with" their claims. In *In re Pappas*,³³ the court was concerned with a plan which provided for payment to the assenting secured creditors of one-half the funds received by the trustee, but which made no provision for dissenting secured creditors. The court followed the reasoning of *O'Dell*, holding that since no provision was made for the dissenting secured creditor, he was restricted, and therefore "dealt with," by the plan. As a consequence, the plan could not be confirmed without his assent.³⁴ This line of reasoning was more succinctly and more forcefully restated in *In re Copes*,³⁵ where

³⁰198 F. Supp. 389 (D.Kans. 1961).

³¹198 F. Supp. 389.

³²198 F. Supp. at 391.

³³216 F. Supp. 819 (S.D.Ohio 1962).

³⁴216 F. Supp. at 822.

³⁵206 F. Supp. 329 (D.Kans. 1962).

the plan provided for payments of \$27 per month instead of \$45.61 per month as required by the secured creditor's contract. Even though the referee had found that reclamation of the collateral—household furnishings—would interfere with consummation of the plan, the court held that “a secured creditor who rejects a plan is entitled either to his contract benefits or the return of his security.”³⁶ This line of cases reached its logical result when the court recently held in *Terry v. Colonial Stores*³⁷ that when a secured creditor who is “dealt with” by the plan refuses to assent to it, the debtor may not use that plan.³⁸

Thus, in any jurisdiction following this line of cases, a wage earner plan will have little chance for confirmation where there is a partially secured creditor who is trying to use the strength of his bargaining position to obtain full payment according to the terms of his contract because without his assent the plan cannot be confirmed. Even though the plan does not affect him *directly*, these cases indicate that he is nonetheless “dealt with” by the plan, and his assent is therefore required.

The more permissive and, in the author's opinion, the more reasonable line of cases seeks to make wage earner plans workable in fact. This line of cases begins with *In re Clevenger*,³⁹ which involved a plan providing for payment of debts held by assenting secured creditors, but which did not provide for dissenting secured creditors. The court here took a different tack from *O'Dell*⁴⁰ and *Pappas*⁴¹ in saying that the plan did not affect creditors who rejected it.⁴² The court held that:

...where the plan did not cover secured creditors who rejected the plan, the Court had jurisdiction of the debtor and all of the property in which he had an interest, and possessed the power and authority to enjoin the prosecution of the reclamation petition.⁴³

³⁶206 F. Supp. at 329.

³⁷411 F.2d 553 (5th Cir. 1969).

³⁸411 F.2d at 555.

³⁹282 F.2d 756 (7th Cir. 1960).

⁴⁰198 F. Supp. 389.

⁴¹216 F. Supp. 819.

⁴²282 F. 2d at 757.

⁴³282 F.2d at 757. The court reached this result by construing together sections 611 and 614 of the Bankruptcy Act.

By so holding, the court was able to prevent the dissenting creditor from reclaiming the debtor's automobile and television set, thereby making the plan more beneficial and feasible. Such a result is particularly important where the collateral sought to be reclaimed by the secured or partially secured creditor is deemed necessary to the plan. Obviously, without his tools or automobile, the debtor, being unable to work, would be unable to earn the funds necessary to implement his plan.

*Hallenbeck v. Penn Mutual Life Ins. Co.*⁴⁴ followed *Clevenger*,⁴⁵ but laid down specific requirements which must be met before an injunction can issue against reclamation:

(1) The injunction or stay must be necessary to preserve the debtor's estate or to carry out the Chapter XIII plan; (2) the granting of the injunction must not directly or indirectly impair the security of the lien; and (3) the owner of the secured indebtedness must not be required to accept less than the full periodic payments specified in his contract.⁴⁶

Of course, the third requirement gives rise to difficulty when the secured creditor is only partially secured. A wage earner plan can function in such a case only if the court is free to readjust the periodic payments of the partially secured creditor. Otherwise, there may be insufficient funds to satisfy the other creditors under the plan.⁴⁷ The third requirement allows the partially secured creditor to obtain an inequitable advantage with respect to other creditors.

The court in *In re Pizzolato*⁴⁸ further extended this line of cases by slightly modifying the secured creditor's rights in order to implement the proposed plan.⁴⁹ The plan provided for monthly payments in the full amount required by the contract creating the

⁴⁴323 F.2d 566.

⁴⁵323 F. 2d at 570.

⁴⁶323 F.2d at 572.

⁴⁷See note 20, *supra*.

⁴⁸268 F. Supp. 353.

⁴⁹In so doing the court distinguished *In re O'Dell* and *In re Copes*, *supra*. O'Dell was distinguished on the ground that the main issues in that case were whether a secured creditor was dealt with by the plan and whether he could be forced to collect payments pursuant to the plan, and on the further ground that the court did not discuss enjoining foreclosure. 268 F. Supp. at 355. The court said that Copes was also distinguishable because the plan in that case provided for a reduction by almost

security interest, except for the final “balloon payment” under the contract, which was more than six times the normal monthly payment. The court enjoined foreclosure and held that the final “balloon payment” was to be paid in installments of the same amount as the other payments under the contract, with interest for the additional period of time required.⁵⁰ In discussing its decision, the court said:

It is clear that to allow the foreclosure would be highly inequitable in view of the facts and circumstances surrounding this case. The bank is in the business of lending money and collecting interest thereon. In this case it appears that the bank will recover the total amount due it together with interest, and, as mentioned . . . , it is *highly* unlikely that any impairment of the security could occur. On the other hand, if the foreclosure were allowed, the plan would most likely be destroyed.⁵¹

In *re Wilder*⁵² also allowed a slight modification of the secured creditor's contract rights in order to preserve a proposed wage earner plan. That plan provided for full monthly payments as called for by the contract, but made no provision for the two payments which the debtor had missed. The court upheld the plan nonetheless, saying:

The confirmation of the plan did not give rise to the arrearage complained of. Nor had creditor exercised its option to declare the entire debt due. A two-month arrearage in a debt contracted on the basis of a two-year span cannot be said seriously to delay payments, especially where the creditor had not considered the arrearage of sufficient importance to exercise its right to accelerate the due dates of the payments. Moreover, there has been no suggestion that the plan seriously affects creditor's security.⁵³

⁵⁰1/2 of the payments called for by the contracts of the secured creditors, and because the opinion did not discuss the debtor's equity in the collateral or the impairment of the security. 268 F. Supp. at 356.

⁵⁰268 F. Supp. at 356-57.

⁵¹268 F. Supp. at 357.

⁵²225 F. Supp. 67.

⁵³225 F. Supp. at 69.

Thus there can be no doubt that this second line of cases, by enjoining reclamation of collateral and by slightly modifying the payments called for under the contract, makes the Chapter XIII wage earner plan a genuinely useful device and, at the same time, maintains a reasonable and fair position *vis-a-vis* the secured creditors. Yet, even this line of cases will not be sufficient to make wage earner plans feasible where a partially secured creditor is affected by a particular plan. Although these decisions are authority for enjoining reclamation, they still require full payment substantially in accordance with the terms of the contract creating the security interest. Since a modification of the terms of payment with respect to the partially secured creditor is needed to make a plan workable, this line of cases, without more, will not be enough. While the courts in *Pizzolato*⁵⁴ and *Wilder*⁵⁵ did modify the contract terms slightly, it must be remembered that those cases involved special circumstances: a "balloon payment," and unpaid installments about which the secured creditor had not complained. In the case of the partially secured creditor, however, it is not "special circumstances," but the very nature of his security interest which requires different treatment. If the wage earner plan is to be successful where a partially secured creditor is involved, some other solution to the problem will be required. The remainder of this article will consider possible judicial and legislative solutions.

III. Proposed Solutions to the Problem of the Partially Secured Creditor

A. The Judicial Approach

Existing case law currently provides a foundation upon which to build a judicial rule for the treatment of the partially secured creditor in wage earner plans which would make the plans workable and would result in fair treatment of all of the debtor's creditors. In fact, the judicial approach which should be followed in such cases *is* the black-letter law that underlies the treatment of secured creditors in every chapter and section of the Bankruptcy

⁵⁴268 F. Supp. 353.

⁵⁵225 F. Supp. 67.

Act, including Chapter XIII: “. . . if the debt exceeds the value of the security, then to the extent of the excess he is the holder of an unsecured debt and to that extent must be treated as all unsecured creditors.”⁵⁶ [Emphasis added.] Although the cases supporting this statement⁵⁷ are pre-Chandler Act cases,⁵⁸ there can be no doubt of its general applicability to any chapter of the Bankruptcy Act.⁵⁹ Furthermore, the application of such a rule in Chapter XIII cases is supported by analogy⁶⁰ to the treatment of partially secured creditors under other chapters of the Act. For example, the cases decided under Chapter XI arrangements⁶¹ treat the partially secured creditor as unsecured to the extent that the debt exceeds the value of his security interest.⁶² Likewise, in a corporate reorganization case under Chapter X, the Supreme Court held that where the security provisions of the corporate bond indenture provided for priority in distribution of an amount which was less than the bondholders' claim, the bondholders would be treated as secured creditors only to the amount provided and would be treated as unsecured creditors for the excess.⁶³

Moreover, there have been some encouraging developments in recent cases under Chapter XIII suggesting that the approach proposed here is proper. For example, one court has held that it was not the intention of Chapter XIII to give secured creditors any special advantage over other creditors, except to the extent of their valid security.⁶⁴ Again, in *In re Bernhardt*,⁶⁵ the court

⁵⁶10 W. COLLIER, BANKRUPTCY 47 (14th rev. ed. 1963). See Copenhaver, *supra* note 1, at 387-88.

⁵⁷See *In re Everick Art Corp.*, 39 F.2d 765 (2d Cir. 1930). See also *In re Dorb the Chemist Inc.*, 3 F. Supp. 457 (S.D.N.Y. 1933); *In re Hereford Oil Co.*, 43 F. 2d 997 (N.D. Tex. 1930). 10 W. COLLIER, BANKRUPTCY 48, n. 10 (14th rev. ed. 1963).

⁵⁸Pub. L. No. 696, 52 Stat. 840-940 (June 22, 1938). This was the first major revision of the Bankruptcy Act of 1898.

⁵⁹See Copenhaver, *supra* note 1, at 388. This is the basic premise underlying the Bankruptcy Act.

⁶⁰A Federal District Court has held it proper to draw analogies between Chapters X, XI, and XIII. *In re Bernhardt*, No. 67-B-1746, at 3-4 (E.D. Wis. July 9, 1968).

⁶¹It should be noted that Chapter XI plans do not deal with secured creditors. They provide for payment of unsecured debts only. Bankruptcy Act, §356 (1968).

⁶²*United States v. Nat'l Furniture Co.*, 348 F.2d 390 (8th Cir. 1965); *Wm H. Wise & Co. v. Rand McNally & Co.*, 195 F. Supp. 621 (S.D.N.Y. 1961).

⁶³*Group of Institutional Investors v. Chicago, Mil. St. P. & Pac. R.R.* 318 U.S. 523, at 573 (1943).

⁶⁴*In re Garrett*, 203 F. Supp. 459, 460-461 (N.D. Ala. 1962).

⁶⁵No. 67-B-1746 (E.D. Wis. July 9, 1968).

thought that it would be inequitable to the unsecured creditors under a Chapter XIII plan to allow the secured creditor to receive interest where his security was worth less than the value of his debt.⁶⁶ That court also expressed the correct rule when it held: "Because of the security, the claim of First Credit Corporation will be paid in full, but the portion in excess of the value of the security will not receive priority of payment."⁶⁷ Finally, the Supreme Court in *Perry v. Commerce Loan Co.*⁶⁸ recently held that the provisions of Chapter XIII should be construed to give effect to and prevent frustration of the purpose of wage earner plans.⁶⁹

The judicial approach proposed herein would operate quite simply. First, the court would evaluate each security interest in order to determine the extent to which it should be given effect.⁷⁰ The plan would be required to provide for payment in full according to the terms of the contract as to that part of the debt which was found to be secured. The excess amount of the debt over the value of the security interest would be treated as unsecured, and the creditor would share in the fund provided by the plan for the unsecured debts. The portion of the debt which is treated as secured is fully provided for by the plan, thereby allowing the court to enjoin a dissenting creditor from foreclosing on his security interest and reclaiming the collateral. Since the remainder of the debt will be treated as unsecured, the creditor would not be able to defeat the plan by his single dissent.⁷¹ As a result, wage earner plans in which a partially secured creditor is involved would become viable alternatives to straight bankruptcy.

⁶⁶No. 67-B-1746, at 4-5

⁶⁷No. 67-B-1746, at 2.

⁶⁸383 U.S. 392 (1966).

⁶⁹383 U.S. 392. According to the Senate report, the purpose of Chapter XIII is to provide "...a procedure by which a debtor who is financially involved and unable to meet his debts as they mature, over a period of time, works out of his involvement and pays his debts in full ..." S. REP. NO. 179, 86th Cong. 1st Sess. 2 (1959). See H.R. REP. No. 193, *supra* note 2.

⁷⁰Determination of the value of the security interest is already done by bankruptcy courts under other chapters of the Bankruptcy Act. See, for example, Bankruptcy Act §§ 57(h), 216 (7)(c), and 351, which provide a basis for evaluating the security interest of the partially secured creditor and for treating him according to the classification of each portion of the debt owed him.

⁷¹Bankruptcy Act § 56(b) (1968), which provides that a secured creditor shall be entitled to vote his claim at a creditors meeting only to the extent that his claim exceeds the value of his security.

Although there is sufficient foundation, both in law⁷² and in reason, for its application in Chapter XIII cases, the rule discussed herein has been applied in only one district court decision. Recently, in *In Re Worley*,⁷³ the court held that since the value of the property subject to the security interest—a refrigerator, a gas range, and a dinette set—was substantially less than the amount due and owing thereon, the creditor would be treated as a secured creditor only to the extent of the value of the security interest, and as an unsecured creditor for the excess amount.⁷⁴ As the wage earner plan provided for payment in full according to the terms of the contract creating the security interest *up to the full value of the security interest*, the court enjoined the partially secured creditor from reclaiming the collateral as long as those payments were made and required him to file an unsecured claim for the excess.⁷⁵ However, since this recent decision is, of course, subject to reversal on appeal, and because of the natural hesitancy of most courts to break new ground, a legislative solution to the problem may well be more desirable.

B. The Legislative Approach

While the adoption of the judicial approach which has been proposed in this article would be sufficient to make the plans workable and to effectuate the purpose of Chapter XIII, a legislative solution to the problem seems preferable. Aside from the fact that a legislative solution would overcome judicial inertia, it would result in a broader and more complete treatment of the problem and would promote uniformity among the courts administering the Bankruptcy Act. To this end, a bill has been introduced in Congress⁷⁶ which approaches the problem in a manner similar to the proposed judicial solution. The bill goes much farther, however, by providing the courts with other extremely useful tools.

⁷²The rule is entirely compatible with the spirit of such cases as *Pizzolato*, *Wilder*, *Bernhardt*, and *Perry*, discussed *supra*.

⁷³No. 69-2244-B (E.D.Mich. March 9, 1970).

⁷⁴No. 69-2244-B, at 6.

⁷⁵No. 69-2244-B, at 6-7.

⁷⁶H.R. 6792, 91st Cong., 1st Sess. (1969). The bill was sponsored by the National Bankruptcy Conference. For a good discussion of the bill and of wage earner plans generally, see Countryman, *supra* note 3.

Basically, the bill would deal with the problem in five important ways. First, the bill provides that the value of all security interests in a Chapter XIII proceeding would be determined in order to allow the court to consider the extent of each security interest.⁷⁷ This would be accomplished through a procedure similar to that employed in straight bankruptcy to determine the amount of secured interest where the creditor holds collateral: conversion into money, or by agreement, arbitration, compromise, or litigation between the trustee and the secured creditor.⁷⁸

Second, the bill provides that where the claim of a secured creditor exceeds the value of his security interest, it will be treated as unsecured to that extent.⁷⁹ This provision of the bill is a codification of the black-letter law discussed earlier in this article and would function in the same manner.

Third, the bill provides that a wage earner plan "may include provisions dealing with secured debts severally and may alter or modify the rights of the holders of such debts."⁸⁰ While this same result has been achieved under existing law,⁸¹ a clear statutory basis is more satisfactory and provides greater latitude to the courts.

Fourth, the bill authorizes the injunction of foreclosure or reclamation if the debtor cures any defaults, according to the conditions and terms prescribed by the court.⁸² While the result would be the same as that reached by the courts in *Pizzolato*⁸³ and *Wilder*,⁸⁴ a statutory basis for such a result would give the courts broader authority for such injunctions and would promote uniformity among the courts. In addition, this provision would allow the courts to deal with various conditions of default rather than the quite narrow and limited ones in the cases cited herein.⁸⁵

⁷⁷H.R. 6792, 91st Cong., 1st Sess. § 2 (1969).

⁷⁸Bankruptcy Act § 57(h) (1968).

⁷⁹H.R. 6792, 91st Cong., 1st Sess. § 2 (1969).

⁸⁰H.R. 6792, 91st Cong., 1st Sess. § 11 (1969).

⁸¹*In re Pizzolato*, 268 F. Supp. 353; *In re Wilder*, 225 F. Supp. 67.

⁸²H.R. 6792, 91st Cong. 1st Sess. § 3 (1969).

⁸³268 F. Supp. 353, discussed *supra*, at pp. 292-294 of text.

⁸⁴225 F. Supp. 67, discusses *supra*, at pp. 293-294 of text.

⁸⁵It will be recalled that *In re Pizzolato* involved a "balloon payment," and that *In re Wilder* involved a two-month arrearage which the creditors had done nothing to correct.

Fifth, the bill would apply the familiar "cram down" provisions of section 77(e) and section 216(7)⁸⁶ to Chapter XIII proceedings and would authorize the court to confirm a plan that "deals with" a dissenting secured creditor if the court finds that the plan provides adequately for the preservation of his claim against the property and future earnings of the debtor.⁸⁷ The effect of this provision of the bill is to reduce the veto power by which a single creditor can destroy a plan to reasonable proportions under justifiable circumstances. Such a provision would be particularly efficacious where a secured or partially secured creditor attempts to gain an inequitable advantage over the other creditors through the strong bargaining position bestowed upon him by his autonomous, omnipotent vote. The dissenting creditor is thereby removed as an obstacle to confirmation of the plan.

From the previous discussion of wage earner plans and the problem created thereunder by the partially secured creditor, it should be apparent that the bill would provide the tools that are badly needed to implement the purpose of Chapter XIII. The partially secured creditor will no longer be treated as a wholly secured creditor. Rather, he will be dealt with according to the twofold nature of his claim: one part secured and the other unsecured. Moreover, the courts will be authorized to use fair and equitable methods to make the wage earner plans readily practicable. Therefore, these provisions of H.R. 6792 should be enacted into law.⁸⁸

⁸⁶For example, § 216(7) provides that a plan of corporate reorganization under Chapter X:

...shall provide for any class of creditors which is affected by and does not accept the plan by the two-thirds majority in amount required under this chapter, adequate protection for the realization by them of the value of their claims against the property dealt with by the plan and affected by such claims, either as provided in the plan or in the order confirming the plan, (a) by the transfer or sale, or by the retention by the debtor, of such property subject to such claims; or (b) by the sale of such property free of such claims at not less than a fair upset price, and the transfer of such claims to the proceeds of such sale; or (c) by appraisal and payment in cash of the value of such claims; or (d) by such method as will, under and consistent with the circumstances of the particular case, equitably and fairly provide such protection; Bankruptcy Act, § 216(7) (1968).

⁸⁷H.R. 6792, 91st Cong., 1st Sess. § 13 (1969).

⁸⁸However, at the date of this writing, little action has been taken on the bill.

IV. Conclusion

Chapter XIII wage earner plans offer a desirable alternative to straight bankruptcy for consumer debtors. Unsecured creditors are given the full benefits of Chapter XIII wage earner plans. The legitimate interest of secured creditors which have been procured through their diligence are fully protected, and the debtor is given the ability to extricate himself honorably from the burdens of his financial strait jacket by providing for full or nearly full payment of his debts. Because of the special position of the partially secured creditor, however, the wage earner plan is not currently a viable alternative to straight bankruptcy. If the breakdown of the wage earner plan is to be forestalled and Chapter XIII is to reach its fruition, solution to the problem should be promptly provided.