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Under section 70a(5) of the Bankruptcy Act,[1] the bankruptcy trustee is entitled to take the debtor's interest in "property" that "prior to the filing of the petition [the debtor] could by any means have transferred or which might have been levied upon and sold under judicial process against him."[2] The Act does not, however, specifically define the term "property," and, as a result, the Supreme

1. 11 U.S.C. § 110(a)(5) (1970).

2. Bankruptcy Act § 70a, 11 U.S.C. § 110(a) (1970), provides:
The trustee of the estate of a bankrupt . . . shall in turn be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition . . . except insofar as it is to property which is held to be exempt, to all of the following kinds of property wherever located . . . (5) property, including rights of action, which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process

Court has developed its own definition. No problem has been presented by money or assets held by the bankrupt at the time of filing; such items are uniformly considered to be property.[3] Nor has a problem arisen with respect to property acquired after filing; with limited exceptions,[4] such property does not pass to the trustee as part of the bankrupt's estate.[5] However, where a right to money has arisen prior to filing but the sum is not available until some time after filing, the Court has exercised its power to determine whether the money is "property" for the purposes of section 70a(5). The most recent case in which this last situation was presented was *Lines v. Frederick*,[6] which held that vacation pay accrued but unpaid at the time of filing is not section 70a(5) property. Two circuit courts,[7] however, have split on the question of whether the analysis in *Lines* should be interpreted to prevent a trustee in bankruptcy from reaching a tax refund received by the bankrupt[8] after filing but attributable to withholding from wages earned prior to that time. In so far as a tax refund is held to be "property," the applicability of the provisions of the Consumer Credit Protection Act (CCPA)[9] that exempt a certain portion of earnings from garnishment[10] must also be considered,

against him, or otherwise seized, impounded, or sequestered: *Provided*, That rights of action ex delicto for libel, slander, injuries to the person of the bankrupt . . . shall not vest in the trustee unless by the law of the State such rights of action are subject to attachment, execution, garnishment, sequestration, or other judicial process . . . .

3. *See, e.g.*, Everett v. Judson, 228 U.S. 474, 479 (1913); Heffron v. Western Loan & Bldg. Co., 84 F.2d 301, 303 (9th Cir.), *cert. denied*, 299 U.S. 597 (1936).

4. *See, e.g.*, Bankruptcy Act § 70a, 11 U.S.C. § 110(a) (1970), which provides that nonexempt property "which vests in the bankrupt within six months after bankruptcy by bequest, devise or inheritance" can be reached by the trustee.

5. *See* Salisbury Motors, Inc. v. United States, 210 F.2d 171, 174 (9th Cir.), *cert. denied*, 347 U.S. 953 (1954); *In re* Leibowitt, 93 F.2d 333 (3d Cir. 1937), *cert denied sub nom.* Stein v. Leibowitt, 303 U.S. 652 (1938).

6. 400 U.S. 18 (1970).

7. *In re* Kokoszka, 479 F.2d 990 (2d Cir. 1973), *cert. granted sub nom.* Kokoszka v. Belford, 42 U.S.L.W. 3352 (U.S., Dec. 11, 1973); *In re* James, 470 F.2d 996 (9th Cir. 1972), *cert. denied sub nom.* Walsh v. Cedor, 411 U.S. 973 (1973).

8. Pursuant to INT. REV. CODE OF 1954, § 3402.

9. 15 U.S.C. §§ 1671-77 (1970).

10. Consumer Credit Protection Act § 303, 15 U.S.C. § 1673 (1970), provides:

(a) Maximum allowable garnishment. Except as provided in subsection (b) of this section and in section 1675 of this title, the maximum part of the aggregate disposable earnings of an individual for any work week which is subjected to garnishment may not exceed

(1) 25 per centum of his disposable earnings for that week, or

(2) the amount by which his disposable earnings for that week exceed thirty times the Federal minimum hourly wage prescribed by section 206(a)(1) of Title 29 in effect at the time the earnings are payable, whichever is less. In the case of earnings for any period other than a week, the Secretary of Labor shall by regulation prescribe a multiple of the Federal minimum hourly wage equivalent set forth in paragraph (2).

(b) Exceptions.

The restrictions of subsection (a) of this section do not apply in the case of

(1) any order of any court for the support of any person.

since, if they are applicable, the trustee will be unable to reach the entire amount of the refund attributable to prefiling wages. The same two circuits have also split on this issue.

This Note will focus on the issue of whether, under *Lines*, tax refunds are to be considered section 70a(5) property; however, the applicability of the CCPA and the solutions to both issues suggested by the Proposed Bankruptcy Act of 1973[11] will also be discussed.

In reaching its decision that vacation pay was not section 70a(5) "property" the Court in *Lines* relied on an interpretation of the policies of the Bankruptcy Act. Specifically, the Court referred to the policy of marshalling the assets of the bankrupt for the benefit of his creditors, as limited by the competing policy of relieving the bankrupt from the burden of his debt.[12]

This conception of the purposes of the law of bankruptcy is the result of a long process of evolution over the past two centuries. Until 1800, bankruptcy law in America was much the same as the English law and had as its main purpose the protection of creditors.[13] Debtors could be granted discharges only if they were able to pay a specified percentage of their debts,[14] and voluntary bankruptcy was not a part of the system.[15] The Bankruptcy Act that was passed in 1800[16] essentially adopted the English law of the time. Voluntary bankruptcy was still not permitted, and only a small class of people—mainly

(2) any order of any court of bankruptcy under Chapter XIII of the Bankruptcy Act.

(3) any debt due for any State or Federal tax.

(c) Execution or enforcement of garnishment order or process prohibited.

No court of the United States or any State may make, execute, or enforce any order or process in violation of this section.

11. H.R. 10792, 93d Cong., 1st Sess. (1973).

The problem of the treatment of tax refunds was the subject of research and discussion in the Commission on the Bankruptcy Laws of the United States. It was found that the treatment of the refund was far from uniform in the country. *See* D. STANLEY & M. GIRTH, BANKRUPTCY: PROBLEM, PROCESS, REFORM 85-86 (1971). A survey revealed, however, that of all denials of discharges under section 14c of the present Bankruptcy Act, 11 U.S.C. § 32(c) (1970), 67 per cent involved section 14c(6), under which the failure to obey an order in bankruptcy can be punished by a denial of discharge. Of these denials, 64 per cent were related to an order concerning tax refunds. Minutes of the Commission on the Bankruptcy Laws of the United States, April 10, 1972. These conclusions were made by the Commission on the basis of responses made to a survey of *all* referees, 69 per cent of whom responded. *Id.*, Jan. 30-31, 1972.

12. 400 U.S. at 19.

13. 1 H. REMINGTON, A TREATISE ON THE BANKRUPTCY LAW OF THE UNITED STATES 12 (4th ed. 1934).

14. *See* 1 *id.* § 6 (5th ed. J. Henderson 1950). The treatise notes: "As [bankruptcy] was then constituted, it might have been defined as a law devised for seizing the person and property of fraudulent and dishonest debtors, for punishing them for their frauds and for distributing their effects ratably amongst the creditors, and if their assets reached a certain percentage of their debts, of granting them a discharge from the remainder of their debts." *Id.*

15. *See id.*

16. Act of April 4, 1800, ch. 19, 2 Stat. 19.

tradesmen—were subject to compulsory bankruptcy. By 1867, voluntary bankruptcy had been accepted, and relief was no longer limited to those groups specified in the 1800 Act. Therefore, some progress had been made toward providing more relief to the debtor, but the 1867 Act[17] still contained a substantial list of grounds for denying a discharge,[18] and thus bankruptcy, even under the 1867 Act, was primarily for the benefit of creditors.

The Bankruptcy Act that was passed in 1898[19] has remained in effect, with amendments, until the present.[20] At the time it was passed, relief of the debtor, though not usually characterized as the primary purpose of the bankruptcy law, was recognized to be a necessary and important part of the law. Judge Ray, who had been a member of the House of Representatives Judiciary Committee[21] that passed the 1898 Act, stated: "The main purpose of the bankruptcy law is to prevent preferences, and secure a fair and equitable division of the bankrupt estate among the creditors, not to grant discharges. This end accomplished, the bankrupt is granted a discharge from all his debts."[22] Another commentator, however, emphasized that the release of debts was the feature of the Act that was primarily responsible for passage:

> When Congress passed the law of 1898 the people in general little comprehended the magnitude of the work done. Its passage was secured chiefly because of its one feature, the release of debts. A great multitude of victims of years of industrial depression were lying stranded on the rocks of hopeless debts. These debtors were skulking along the streets hardly daring to lift their eyes to passers by lest they might remind some creditor of an almost forgotten if not forgiven debt.[23]

More recently, the relief of the debtor has become an objective coequal with the protection of creditors.[24] One commentator, writing during the 1930's, described the objectives of the Act as follows:

> The purpose of the Bankruptcy Act is to distribute the assets of the

17. Act of March 2, 1867, ch. 176, 14 Stat. 517.

18. Act of March 2, 1867, ch. 176, § 29, 14 Stat. 517. The majority of these grounds refer to fraud of one kind or another.

19. Act of July 1, 1898, ch. 541, 30 Stat. 544.

20. Codified at 11 U.S.C. §§ 1-1103 (1970).

21. 1 H. REMINGTON, *supra* note 13, at 18.

22. *In re* Leslie, 119 F. 406, 410 (N.D.N.Y. 1903).

23. 1 H. REMINGTON, *supra* note 13, at 18-19.

24. *See* J. WEINSTEIN, THE BANKRUPTCY LAW OF 1938: CHANDLER ACT (1938); Lashly, *The Chandler Bill*, 11 REF. J. 27 (1936); McLaughlin, *Aspects of the Chandler Bill to Amend the Bankruptcy Act*, 4 U. CHI. L. REV. 369 (1937); Weinstein, *The Debtor Relief Chapters of the Chandler Act*, 5 U. PITT. L. REV. 1 (1938); Note, *The Chandler Bankruptcy Amendatory Bill Is Enacted*, 12 REF. J. 124 (1938); Note, *Editorial*, 23 VA. L. REV. 54 (1936).

> bankrupt equitably among his creditors and then to relieve the honest debtor from the burden of his debt and permit him to start anew, free from the obligations consequent on business misfortunes. It is not necessary that both objects be attainable. *In many cases the relief of the debtor is the only object,* since there are no assets for distribution.[25]

One aspect of the new emphasis on the policy of relieving the debtor is found in Chapter XIII,[26] added in 1938 by the Chandler Act.[27] It gives the wage earner an opportunity to repay his debts out of future earnings, under a plan supervised by the bankruptcy court, rather than forcing him to take an immediate and total discharge. This procedure thus allows the debtor to retain his property while relieving him from the harassment of his creditors.

Another aspect has been characterized as the fresh-start doctrine.[28] It was this aspect that the Court emphasized in *Lines v. Frederick.* It is not new, however, for it has been stressed in many cases since the enactment of the 1898 law.[29] One of the earliest formula-

25. F. GILBERT, COLLIER ON BANKRUPTCY 4 (4th ed. J. Moore & E. Levi 1937) (emphasis added).

26. Bankruptcy Act §§ 601-86, 11 U.S.C. §§ 1001-86 (1970).

27. Ch. 575, 52 Stat. 840.

28. Although it can be argued that the policy of relieving the debtor and the fresh-start doctrine are interchangeable terms for the same idea, this approach has not been taken. Rather, the fresh-start doctrine is taken to refer to that aspect of the policy of relief of debtors that is concerned with the effectiveness of the bankrupt's discharge. Thus, for example, a Chapter XIII proceeding, although it relieves the debtor, is not an implementation of the fresh-start doctrine since a complete discharge is not involved unless the plan fails.

Although the discussion of fresh start is limited in this Note to the way in which that doctrine will operate as a limitation on the definition of property under section 70a(5) of the Bankruptcy Act, the problem of ensuring the bankrupt a fresh start has other facets. For example, a bankrupt may be forced by a creditor to promise to pay a debt discharged in bankruptcy as a condition to the extension of further credit. In a jurisdiction that recognizes the contract doctrine of moral consideration, *see, e.g.,* Zavelo v. Reeves, 227 U.S. 625 (1913); First Natl. Bank v. Henderson, 243 Ala. 636, 11 S.2d 366 (1942), the new promise would be enforceable, and the debtor will be deprived of a fresh start by being forced to satisfy a discharged debt out of income earned after bankruptcy. *See generally* 1A A. CORBIN, CONTRACTS § 222 (1963); Boshkoff, *The Bankrupt's Moral Obligation To Pay His Discharged Debts: A Conflict Between Contract Theory and Bankruptcy Policy,* 47 IND. L.J. 36 (1971). Some state licensing statutes, *e.g.,* CAL. BUS. & PROF. CODE §§ 6876.2-78 (West 1964), also deprive a debtor of his ability to make a fresh start by requiring applicants for licenses to disclose whether they have been adjudged bankrupt. Similarly, state legislatures may indirectly force a bankrupt to pay a discharged debt, thus depriving him of his fresh start, by making the enjoyment of some other activity contingent upon payment of the discharged debt. Such a statute was at issue in Perez v. Campbell, 402 U.S. 637 (1971), in which an Arizona statute that provided for suspension of a driver's license for failure to pay a judgment, even where the judgment debt had been discharged in bankruptcy, was held unconstitutional as in conflict with the Bankruptcy Act. This case overruled the contrary decision in Reitz v. Mealey, 314 U.S. 33 (1941).

29. *See* Stellwagen v. Clum, 245 U.S. 605, 617 (1918); Williams v. United States Fidelity & Guar. Co., 236 U.S. 549, 557 (1915); Burlingham v. Crouse, 228 U.S. 459,

tions of the doctrine can be found in dicta in *Wetmore v. Markoe*,[30] which, although it did not find the policy of relieving the debtor persuasive enough to allow the discharge of an obligation to pay alimony, would have applied the fresh-start doctrine had the indebtedness arisen out of a less personal transaction: "Systems of bankruptcy are designed to relieve the honest debtor from the weight of indebtedness which has become oppressive and to permit him to have a fresh start in business or commercial life, freed from the obligation and responsibilities which may have resulted from business misfortunes."[31]

The doctrine was applied to support the holding that a debt was discharged in *Williams v. United States Fidelity & Guaranty Co.*[32] The Court was faced with the problem of whether bankrupt partners were freed by discharge from their obligation to indemnify their surety on a performance bond guaranteeing the partnership's performance of a building contract. Prior to filing in bankruptcy the bankrupts had breached the contract and failed to pay damages on demand, and the surety did not make payment until after the filing. Claiming that no debt had arisen until it made payment, the surety brought suit against the bankrupts for repayment. The Court concluded that the effectiveness of the discharge would be jeopardized if the surety were allowed to prevail, for this would allow a surety, simply by failing to pay on the bond until after the bankruptcy of the principal, to preserve a right of recovery against the bankrupt and thus deprive him of his fresh start.[33]

Implicit in the fresh-start doctrine is the idea that a debtor should not be forced to satisfy a preexisting debt out of income obtained after his discharge in bankruptcy. This situation was presented explicitly in *Local Loan Co. v. Hunt*.[34] The bankrupt had borrowed

473 (1913); Wetmore v. Markoe, 196 U.S. 68, 77 (1904); Imperial Assur. Co. v. Livingston, 49 F.2d 745, 748 (8th Cir. 1931); Equitable Life Assur. Soc. v. Stewart, 12 F. Supp. 186, 192 (W.D.S.C. 1935). Indeed, although interpreting earlier Bankruptcy Acts, cases even before 1898 spoke of the fresh-start doctrine. *See, e.g.*, Strang v. Bradner, 114 U.S. 555, 559 (1885); Traer v. Clews, 115 U.S. 528, 541 (1883); Neal v. Clark, 95 U.S. 704, 709 (1877).

30. 196 U.S. 68 (1904).

31. 196 U.S. at 77.

32. 236 U.S. 549 (1915).

33. *See* 236 U.S. at 557.

34. 292 U.S. 234 (1934). *Local Loan* is more often cited as authority for the proposition that the bankruptcy court has jurisdiction to declare the effect of, as well as to grant, discharge. *See, e.g.*, Strasburger, *The Wage Assignment Problem*, 19 MINN. L. REV. 536, 555 (1935); Casenote, 83 U. PA. L. REV. 92 (1934). Prior to this it was felt that the bankruptcy court had no such power, that the discharged bankrupt would be required to plead his discharge as an affirmative defense in any state court action brought against him by a creditor, and that the state court would be free to decide the merits of the claimed defense. *See* Countryman, *The New Dischargeability Law*, AM. BANKR. L.J. 1, 2-3 (1971). While the Court in *Local Loan* recognized that the

a sum of money and had assigned a portion of his future wages to his creditor as security. Thereafter he was discharged in bankruptcy, and the creditor sued the bankrupt's employer in state court to enforce the assignment.[35] The bankrupt obtained from the bankruptcy court a decree that enjoined the prosecution of the state court suit.[36] The Supreme Court upheld the decree and stressed that "[o]ne of the primary purposes of the bankruptcy act is to 'relieve the honest debtor from the weight of oppressive indebtedness and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortunes.' "[37]

Although the above cases dealt with the question of whether a certain obligation persisted after discharge, their insistence that post-discharge income not be used to satisfy predischarge debts is also found in cases in which the issue is whether certain income should be applied to satisfy debts in existence at the time of filing. In deciding this latter question the courts have tried to define property as it is used in section 70a(5) in a way that is consistent with the competing goals of benefiting the creditor and providing the debtor with a fresh start. Their attempts have often resulted in precise, easily applicable formulas, which have not always been satisfactory. For example, at one time the Supreme Court seemed to emphasize the time at which the right to the property accrued to the debtor. In *Local Loan Co. v. Hunt*, the Court stressed that the bankrupt will not be granted a discharge until he surrenders the property "which he owns *at the time of bankruptcy*."[38] Since those wages that were to be earned by the bankrupt in the future were not owned by him at the time of bankruptcy, they could not be used to satisfy an obligation that had been incurred before filing.[39]

Although the *Local Loan* approach fulfills the basic goal of giving the debtor a fresh start under the facts of that case, a case decided three years later indicates the inadequacy, from a policy point of view, of applying the accrual approach in all situations. In *Legg*

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federal court had the power to declare the effect of the discharge in bankruptcy, it also stated that it should probably not do so except where a failure to do so would, in effect, deny the bankrupt any relief. *See* 292 U.S. at 241. A recent amendment to the Bankruptcy Act goes even further and declares the effect of a discharge in every case. Act to Amend the Bankruptcy Act, Pub. L. No. 91-467, § 3, 84 Stat. 992 (1970), *amending* Bankruptcy Act § 14 (codified at 11 U.S.C. § 32 (1970)).

35. 292 U.S. at 238.

36. 292 U.S. at 238.

37. 292 U.S. at 244, *quoting* Williams v. United States Fidelity & Guar. Co., 236 U.S. 549, 554-55 (1915).

38. 292 U.S. at 244 (emphasis original). It should be noted that discharge is not granted to every bankrupt. *See* Bankruptcy Act § 14c, 11 U.S.C. § 32(c) (1970).

39. In some situations, property acquired after filing must be turned over to the trustee. *See* Bankruptcy Act § 70a, 11 U.S.C. § 110(a) (1971).

v. St. John,[40] petitioner had purchased a life insurance policy and, at the same time and for an additional premium, a disability policy that entitled him to a monthly payment if he became totally and permanently disabled before he reached the age of sixty. Before he went bankrupt, petitioner became disabled and began receiving benefits under the disability policy. The Court held that, since petitioner's right to the monthly payments had been acquired before the bankruptcy proceedings, the right to receive subsequent payments should go to the trustee. By applying the accrual concept in the *Legg* case, the Court reached a result that deprived the petitioner of all future income and thus deprived him of any opportunity to make a fresh start.

Another mechanical approach that can lead to inequitable results looks merely to the time of payment. Such an approach would have avoided the result in *Legg* by allowing petitioner to retain money received after bankruptcy, but it could prejudicially affect the rights of creditors. Assume a situation in which a potential bankrupt converts all of his nonexempt assets to cash and purchases an annuity contract before filing for bankruptcy. If the criterion for determining which assets are to go to the trustee is time of payment, the bankrupt would be able to protect all his assets—assuming, for the sake of argument, that a discharge is not denied under other provisions of the Act.[41] A similar situation was presented in *In re Power*,[42] and the Seventh Circuit, recognizing the possibility of abuse,[43] decided that the proceeds of an annuity contract, even though it was purchased thirteen years before bankruptcy, must be turned over to the trustee. The provisions of the Internal Revenue Code that allow withholding[44] could be similarly abused. By withholding more than the amount required to cover his tax liability and collecting the surplus in the form of a refund after filing, a potential bankrupt could keep part of his income out of the reach of the trustee. One court that found tax refunds not to be property under section 70a(5) explicitly recognized this possibility and ruled that only the portion of the refund attributable to *mandatory* withholding was to remain with the bankrupt.[45] Either mechanical approach—accrual or time of payment—would, by definition, always answer the problems raised in this Note in the same way. The accrual approach would always require that the asset be turned over to the trustee, while the time-of-payment approach would always exempt the asset.

40. 296 U.S. 489 (1936).

41. *See generally* Bankruptcy Act § 14, 11 U.S.C. § 32 (1965) (states when discharges may be granted).

42. 115 F.2d 69 (7th Cir. 1940).

43. 115 F.2d at 73.

44. INT. REV. CODE OF 1954, § 3402.

45. *In re* Cedor, 337 F. Supp. 1103, 1106 (N.D. Cal. 1972).

In later cases the Supreme Court has refused to use a mechanical formula to define "property" and has concentrated instead on the policies underlying the Bankruptcy Act. For instance, in *Segal v. Rochelle*,[46] where the Court was asked to determine whether a loss-carryback tax refund[47] was "property" that would pass to the trustee in bankruptcy, the Court recognized that the definition of property is limited by the fresh-start doctrine:

> The main thrust of § 70a(5) is to secure for creditors everything of value the bankrupt may possess . . . when he files his petition. . . . However, limitations on the term ["property"] do grow out of other purposes of the Act; one purpose which is highly prominent and is relevant in this case is to leave the bankrupt free after the date of his petition to accumulate new wealth in the future.[48]

However, the Court found that requiring the refund to be turned over to the trustee was not inconsistent with the fresh-start doctrine in this case because the refund was "sufficiently rooted in the pre-bankruptcy past and so little entangled with the bankrupt's ability to make an unencumbered fresh start that it should be regarded as 'property.' "[49] The Court could easily have found that, since the right to the refund had accrued at the time of filing, the refund should be considered property, but the Court relied instead on the ground that allowing the refund to go to the trustee would not contravene the policies of the Act.[50]

In *Lines* the Court reiterated the statement made in *Segal*: " 'It is impossible to give any categorical definition to the word "property," nor can we attach to it in certain relations the limitations which would be attached to it in others.' "[51] The problem in *Lines* concerned vacation pay that had been earned but not yet paid at the time that the petitions in bankruptcy were filed by the wage earners. The sum could be collected, in the case of one respondent, either during the annual plant shutdown or upon final termination of employment. In the case of the other respondent, it could be drawn either on termination or under a conventional voluntary vacation plan.

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46. 382 U.S. 375 (1966).

47. Under INT. REV. CODE OF 1954, § 172, a taxpayer, under conditions defined in that section, is permitted to apply losses of the current year against income in prior year(s) and receive a refund for any overpayment of tax in the earlier year(s).

48. 382 U.S. at 379.

49. 382 U.S. at 380.

50. 382 U.S. at 380. This discussion is not meant to imply that courts have ceased to use the accrual approach, *see, e.g., In re* Stanley, [1970-1973 Transfer Binder] BANKR. L. REP. ¶ 64,160 (E.D. Va. 1971); *In re* Byrd, [1970-1973 Transfer Binder] BANKR. L. REP. ¶ 64,209 (D. Conn. 1971), but to show that even before *Lines* the Supreme Court did not consider the approach entirely adequate.

51. 400 U.S. at 19, *quoting* 382 U.S. at 379, *quoting* Fisher v. Cushman, 103 F. 860, 864 (1st Cir. 1900).

The Court said specifically that the question could not be resolved on the basis of when the right to the property "vested";[52] nor did the decision turn on the time of payment. Instead, the Court in *Lines*, as in *Segal*, emphasized that, although section 70a(5) was intended to collect all the property of the debtor for the benefit of his creditors, the definition of "property" should be limited where allowing the trustee to take the property would deprive the bankrupt of a fresh start.[53] The Court concluded that, since the assets were part of the bankrupts' wages, their function was to support the bankrupts and their families during a particular postfiling period and they would not be considered "property."

Lines could be read to hold that every payment due the bankrupt at the time of filing is not a part of the bankrupt's estate if it is used for necessities. However, such a reading would put an intolerable burden on referees in bankruptcy, since the use of every payment would have to be investigated to determine whether it were being spent on a "necessity." This reading would also extend the goal of giving the bankrupt an opportunity to make a new life to the point where it seriously infringes on the rights of creditors, which the Act is also designed to protect.

Lines must be read narrowly, in accordance with its language, to hold that, of those payments accruing to the bankrupt before filing but paid after, only those that stand in the position of wages in that they are to provide basic support for a specific postfiling period of time are not to be considered "property."

Those courts that have refused to apply *Lines* to limit the definition of property under section 70a(5) have done so because of this narrow decisional basis. In *In re Kanter*,[54] a federal district court interpreted *Lines* narrowly and held that a personal injury cause of action, where suit had been filed but no damages awarded prior to bankruptcy, was "property" under section 70a(5) of the Act. Consequently, the court held that a statute[55] that, in its effect, would prohibit a bankruptcy trustee from acquiring rights in a bankrupt's cause of action was unconstitutional because it conflicted with the Bankruptcy Act.[56] In distinguishing *Lines* the court stressed that *Kanter* did not deal with "wages or vacation pay."[57] The court expressed the fear that, if a cause of action were held not to be section 70a(5) property, the bankrupt could receive and retain the damages

52. 400 U.S. at 19.

53. 400 U.S. at 19.

54. 345 F. Supp. 1151 (C.D. Cal. 1972). *But see In re* Schmelzer, 350 F. Supp. 429 (S.D. Ohio 1972).

55. CAL. CIV. PRO. CODE § 688.1(b) (West 1970).

56. 345 F. Supp. at 1156.

57. 345 F. Supp. at 1157.

arising from the cause of action while escaping, through the discharge in bankruptcy, the expenses on which the damage award would be based.[58]

In *In re Aveni*,[59] a case decided by the Sixth Circuit two months before *Kanter*, the court held that, under the test set forth in *Segal*, wages earned prior to bankruptcy but payable afterwards were not exempt from a turnover order. *Lines* was mentioned only briefly, and the court apparently felt that the decision in *Lines* did not apply to the facts presented in *Aveni*. The Sixth Circuit did point out, however, that the bankrupt would still receive his fresh start, since a state statute[60] exempted all but $71.50 of the $925.90 in question and "the statutorily authorized exemptions provide[d] the bankrupt with a purse from [the wages in question] to meet his basic needs."[61] One could argue that the *Lines* case required a different result in *Aveni*. Since the wages were paid after discharge (although for work done before discharge), they arguably were to provide for the basic support of the bankrupt during the period *after* payment and after discharge. In *Aveni*, however, the Ohio statute blunted this argument by reaching, in effect, the same result.

The largest number of cases in which the problem of the application of *Lines* has been presented have involved tax refunds,[62] and two circuits have split on the resolution of this problem. In *In re Kokoszka*,[63] the three bankrupt petitioners had been ordered to turn their income tax refunds over to the trustees. The district court upheld the referee's ruling that the tax refunds were subject to the turnover order.[64] The Second Circuit affirmed and refused to find that *Lines* dictated a contrary result. The court found the holding of *Lines* to be a very narrow one, restricted to the situation in which

58. 345 F. Supp. at 1157.

59. 458 F.2d 972 (6th Cir. 1972), *cert. denied sub nom.* Aveni v. Richman, 409 U.S. 877 (1972).

60. OHIO REV. CODE ANN. § 2329.66 (Page 1954), *as amended*, OHIO REV. CODE ANN. § 2329.66 (Page Supp. 1972).

61. 458 F.2d at 973.

62. *See In re* Kokoszka, 479 F.2d 990 (2d Cir. 1973), *cert. granted sub nom.* Kokoszka v. Belford, 42 U.S.L.W. 3352 (U.S., Dec. 11, 1973); *In re* Marsh, [1970-1973 Transfer Binder] BANKR. L. REP. ¶ 64,748 (D.R.I. 1973); *In re* Schmelzer, 350 F. Supp. 429 (S.D. Ohio 1972); *In re* Kanter, 345 F. Supp. 1151 (C.D. Cal. 1972); *In re* Kingswood, 343 F. Supp. 498 (C.D. Cal.), *revd.*, 470 F.2d 996 (9th Cir. 1972), *petition for cert. filed sub nom.* Michelman v. Kingswood, 42 U.S.L.W. 3101 (U.S., Aug. 13, 1973) (No. 289); *In re* Cedor, 337 F. Supp. 1103 (N.D. Cal.), *affd. sub nom. In re* James, 470 F.2d 996 (9th Cir. 1972); *In re* Stanley, [1970-1973 Transfer Binder] BANKR. L. REP. ¶ 64,160 (E.D. Va. 1971); *In re* Jones, 337 F. Supp. 620 (D. Minn. 1971).

63. 479 F.2d 990 (2d Cir. 1973), *cert. granted sub nom.* Kokoszka v. Belford, 42 U.S.L.W. 3352 (U.S., Dec. 11, 1973). *See also In re* Marsh, [1970-1973 Transfer Binder] BANKR. L. REP. ¶ 64,748 (D.R.I. 1973); *In re* Stanley, [1970-1973 Transfer Binder] BANKR. L. REP. ¶ 64,160 (E.D. Va. 1971); *and In re* Jones, 337 F. Supp. 620 (D. Minn. 1971), which have similar holdings.

64. *See* 479 F.2d at 993.

the property contested is "weekly or other periodic income required by a wage earner for his basic support."[65] The petitioners argued that the refund fell within the special category of wages protected by *Lines*. However, the court felt that, although a tax refund has its source in wages, it does not fall within the narrow exception carved out by *Lines* because "to deprive him of it will not hinder his ability to make a *fresh* start unhampered by the pressure of preexisting debt."[66] In addition, the court rejected the argument that a tax refund should not be characterized as section 70a(5) property because the taxpayer relies on it as an expected annual payment and thus the deprivation of it would prevent him from making a fresh start. This argument sounds very similar to the time-of-payment approach, and the court was quick to point out its possible adverse consequences.[67] The court said that many payments, including Christmas Club accounts and year-end stock dividends, could be characterized as expected annually recurring events and that that fact alone did not render them immune to a turnover order.[68]

Faced with the same question, a California federal district court in *In re Cedor*[69] reached exactly the opposite result. The Ninth Circuit, in *In re James*,[70] affirmed *Cedor* "upon the authority of *Lines v. Frederick* . . . and the carefully reasoned opinion" by the district court.[71] The district court had found that the tax refund was similar "in a practical sense" to the vacation pay with which the Court was concerned in *Lines*: "While the amount of refund is not so easy to calculate as the amount of vacation pay, it may generally be said to be an amount that, by reason of past experience, is anticipated by the wage-earner as an annual event. To deprive the wage-earner of that planned-on annually recurring payment, cannot be said to be less severe than the deprivation of two weeks of paid vacation, in terms of a fresh start."[72] Although the court disclaimed any mechanical approach, this argument, as pointed out above, sounds very much like the time-of-payment approach. The court recognized the possibility of abuse by deliberate excessive withholding[73] and restricted its decision by finding that the refund was not property only

65. 479 F.2d at 995.

66. 479 F.2d at 995 (emphasis original).

67. 479 F.2d at 995. The adverse consequences are mentioned in the text accompanying notes 44-45 *supra*.

68. 479 F.2d at 995.

69. 337 F. Supp. 1103 (N.D. Cal. 1972).

70. 470 F.2d 996 (9th Cir. 1972).

71. 470 F.2d at 996.

72. 337 F. Supp. at 1105.

73. 337 F. Supp. at 1105.

to the extent that it resulted from the minimum withholding required by law.[74]

In drawing a parallel between tax refunds and vacation pay the *Cedor* decision completely ignores the language in *Lines*[75] that restricts that decision to amounts paid as basic support for the bankrupt and his family after bankruptcy. In fact, the court in *Cedor* seems to have drawn its arguments, not from the Supreme Court opinion, but from the opinion of its own circuit court[76] that was affirmed in *Lines*. Although the Supreme Court affirmed the Ninth Circuit decision, it did not adopt all of the arguments made by the lower court. In particular, the Ninth Circuit opinion in *Lines* stressed that, from the employee's point of view, the time when the right to payment accrues is irrelevant and that the employee is concerned only with the time of payment.[77] The *Cedor* opinion shows this emphasis when it states: "If *Lines* stands for anything, it is that the practical realities are controlling in this determination. [T]he amount of refund . . . is anticipated by the wage-earner as an annual event."[78] Unlike these lower court opinions, the Supreme Court in *Lines* simply does not mention that the employee's expectations are relevant. Whether the employee anticipates receiving the money does not affect the question of whether the money is in fact necessary to provide him with a fresh start.

Lines must be read more narrowly than it was by the court in *Cedor*, for it represents a careful balancing of the two policies underlying the Bankruptcy Act. *Cedor* ignores this fact by overemphasizing the expectations of the debtor to the detriment of his creditors. The decisions in both *Lines* and *Kokoszka*, however, represent an awareness of the need to protect the creditors, even where the debtor has not deliberately attempted to defraud them.

Even if the position presented above—that a tax refund is section 70a(5) property—is accepted, the debtor may further argue that the garnishment provisions of the CCPA,[79] which provide that no more than a specified portion of an individual's disposable earnings may be subject to garnishment, prevent the bankruptcy trustee from taking more than a specified fraction of the refund. This argument was raised in both *Cedor* and *Kokoszka*; the Court did not have to consider it in *Lines* because the bankrupt was allowed to keep all of the vacation pay on the basis of the Court's interpretation of the

74. 337 F. Supp. at 1107.

75. 400 U.S. at 20.

76. Frederick v. Lines, 425 F.2d 215 (9th Cir. 1970).

77. 425 F.2d at 217.

78. 337 F. Supp. at 1105.

79. Consumer Credit Protection Act § 303, 15 U.S.C. § 1673 (1970). For text of section 303, see note 10 *supra*.

term "property" in section 70a(5). Although *Cedor* held that the bankrupt could retain that part of the refund attributable to the minimum mandatory withholding, it still had to deal with the question of the applicability of the CCPA to the rest of the refund. Its decision in that regard squarely conflicts with the decision in *Kokoszka.*

The court in *Cedor* argued that the source of the funds that constituted the refund falls within the definition of "earnings" under section 302(a)[80] of the Act; that, since nothing was required by law to be withheld from the refund, the entire amount was "disposable earnings" under section 302(b);[81] and that the taking of title to the refund by the bankruptcy trustee was a "garnishment" under section 302(c).[82] As a result, the court reasoned that, under section 303(a)(2),[83] the trustee could only take a fraction of the amount of the refund not attributable to minimum withholding.[84] The court also argued that by excepting only orders made in a Chapter XIII proceeding[85] from the limitations on the amount that could be garnished,[86] Congress had indicated its intent to subject orders in all other types of bankruptcy proceedings to the restrictions of the CCPA.[87]

The Second Circuit, in *Kokoszka,* reached the opposite conclusion with very little discussion.[88] In essence, the court argued, on the basis of a House report[89] and a Labor Department regulation[90] that

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80. Consumer Credit Protection Act § 302(a), 15 U.S.C. § 1672(a) (1970). The section provides:

> The term "earnings" means compensation paid or payable for personal services, whether denominated as wages, salary, commission, bonus, or otherwise, and includes periodic payments pursuant to a pension or retirement program.

81. 15 U.S.C. § 1672(b) (1970). The section provides:

> The term "disposable earnings" means that part of the earnings of any individual remaining after the deduction from those earnings of any amounts required by law to be withheld.

82. 15 U.S.C. § 1672(c) (1970). The section provides:

> The term "garnishment" means any legal or equitable procedure through which the earnings of any individual are required to be withheld for payment of any debt.

83. 15 U.S.C. § 1673(a)(2) (1970).

84. 337 F. Supp. at 1106.

85. Bankruptcy Act §§ 601-86, 11 U.S.C. §§ 1001-86 (1970).

86. *See* Consumer Credit Protection Act § 303, 15 U.S.C. § 1673 (1970). The section is quoted in note 10 *supra.*

87. 337 F. Supp. at 1107. Finally, the *Cedor* court referred to a letter written by the Administrator of the Wage and Hour Division of the Department of Labor (U.S. Labor Dept. Op. WH-103, Dec. 18, 1970), which expressed the opinion that orders in bankruptcy other than those made in a Chapter XIII proceeding "would appear subject to the garnishment restrictions." 337 F. Supp. at 1107-08.

88. *See also In re* Marsh, [1970-1973 Transfer Binder] BANKR. L. REP. ¶ 64,748 (D.R.I. 1973).

89. H.R. REP. No. 1040, 90th Cong., 1st Sess. 20-21 (1967).

90. 29 C.F.R. § 870.10(b) (1972). The regulation states, with regard to the statutory

interprets section 303 of the CCPA, that the Act was clearly intended to protect only compensation made in the form of periodic payments—in order to guarantee that a wage earner has enough cash to meet his basic needs in any given pay period—and was not designed to protect every asset traceable to such compensation.[91]

There are a number of arguments in support of the *Kokoszka* holding in addition to those made in the case. In implying that no policy reason dictates a result contrary to its conclusion the *Cedor* court failed to look beyond the CCPA. It ignored the Bankruptcy Act, one of the basic aims of which is assembling all of the debtor's assets for the benefit of his creditors.[92] Any statute that deprives the trustee in bankruptcy of assets that would otherwise be available undercuts this purpose of the Bankruptcy Act. In addition, although it was suggested by the court in *Kokoszka* that the CCPA was only incidentally aimed at preventing harsh garnishment from forcing debtors into bankruptcy,[93] the legislative history indicates that such prevention is one of the central purposes of the garnishment provisions of the CCPA. For example, a House report on the subject concluded that "[t]he limitations on the garnishment of wages adopted by your committee, while permitting the continued orderly payment of consumer debts, will relieve countless honest debtors driven by economic desperation from plunging into bankruptcy in order to preserve their employment and insure a continued means of support for themselves and their families."[94] It seems anomalous to argue, especially in light of the protection afforded a bankrupt under the Bankruptcy Act itself, that, although the CCPA has failed to prevent a bankruptcy, it will nevertheless continue to protect the bankrupt by allowing creditors only limited access to his assets. There is no reason why, for example, a bankrupt should be allowed the exemptions of the CCPA when the Bankruptcy Act already entitles him to the exemptions afforded by state laws. Thus, it seems that the CCPA is aimed at preventing consumers from entering bankruptcy and that the adequate protection provided by the Bankruptcy Act makes the protections of the CCPA unnecessary, if not superfluous, once the debtor has submitted to bankruptcy.

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exemption formula: "Its intent is to protect from garnishment and save to an individual earner, the specified amount of compensation for his personal services rendered in the work week, or lesser period."

91. 479 F.2d at 997.

92. *See, e.g.*, Segal v. Rochelle, 382 U.S. 375, 379 (1966).

93. "The intent of the Consumer Act was to make sure that wage earners were able to receive at least 75% of their take home pay in any one pay period so that they would have enough cash to meet basic needs. As a side effect, it was hoped that honest debtors, with this protection on their wages, would not be forced into bankruptcy." 479 F.2d at 996-97.

94. H.R. REP. No. 1040, *supra* note 89, at 21.

Cedor further argues[95] that, since the only part of the Bankruptcy Act specifically excluded from the operation of the CCPA was Chapter XIII,[96] Congress must not have intended to exclude the other portions of the Bankruptcy Act. However, there is an alternative, and more convincing, explanation of why Chapter XIII was singled out for a specific exclusion. Chapter XIII allows a wage earner to satisfy his creditors out of future income under a supervised plan.[97] This procedure seems more similar than does a straight bankruptcy proceeding to the normal credit situation in which garnishment may be used and toward which the provisions of the CCPA are directed. Thus, the legislature may have felt it necessary to exclude Chapter XIII specifically. However, it may never have occurred to the legislature that the question of the applicability of the CCPA to other provisions of the Bankruptcy Act would ever be raised. Therefore, the position taken in *Kokoszka*, although perhaps not as persuasively argued as it could have been, is more appropriate than that taken in *Cedor*, since it does not enforce one federal act at the expense of the other.

A discussion of the question of property in bankruptcy and of the applicability of the CCPA to orders in bankruptcy would not be complete without mention of the proposed Bankruptcy Act of 1973.[98] This bill is the product of two years of study by the Commission on the Bankruptcy Laws of the United States, which was established by a joint resolution of Congress in 1970.[99] The proposed law would prevent the application of the CCPA in all bankruptcy proceedings, including those situations presented in *Cedor* and *Kokoszka*, since it specifically allows exemptions only in accordance with the proposed Act.[100] The drafters made their intent even more clear, however, in a note to the Act: "The section controls what property of the debtor is to be set aside to the debtor; conflicting laws are superseded. Federal laws thereby superseded include . . . garnishment restrictions of the Federal Consumer Credit Protection Act . . . to the extent they constitute exemptions."[101]

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95. 337 F. Supp. at 1107.

96. For a complete list of the exclusions, see text of 15 U.S.C. § 1673(b) (1970) in note 10 *supra*.

97. Bankruptcy Act § 646, 11 U.S.C. § 1046 (1970) (sets out provisions that wage earner plan *must* include, as well as those it *may* include).

98. H.R. 10792, 93d Cong., 1st Sess. (1973).

99. Jt. Res. of July 24, 1970, Pub. L. No. 91-354, 84 Stat. 468.

100. H.R. 10792, 93d Cong., 1st Sess. § 4-503(a) (1973):

> CONTROLLING LAW. An individual debtor, who has filed a petition for relief or against whom relief has been directed under this Act, shall be allowed exemptions of property as provided in this section. Property allowed as exempt under this section is exempt from creditors holding claims allowable against the debtor's estate, other than claims excepted from discharge under section 4-506(a)(6).

101. COMMISSION ON BANKRUPTCY LAWS OF THE UNITED STATES, REPORT pt. II, § 4-503(a), note 2 (1973) [hereinafter COMMISSION REPORT].

Although the proposed Act makes substantial changes in all aspects of bankruptcy proceedings, the most significant change for the purposes of this discussion is the creation of federal uniform exemptions in section 4–503. The proposed law rejects the approach of section six of the present Act,[102] which allows the bankrupt to claim exemptions provided by the controlling state law. Instead, it delimits quite specifically what is to be considered "property" of the bankrupt estate[103] and just as specifically defines the available exemptions. Section 4–503(c)(3) answers the problem of *Cedor* and *Kokoszka* by exempting "cash, securities, and receivables, including unpaid personal earnings, accrued vacation pay, and *income tax refund*, to the aggregate value of not more than $500."[104] Other exemptions also draw monetary lines. Thus, under the homestead exemption, only the value of a homestead up to 5,000 dollars is exempted;[105] under section 4–503(c)(1) certain other classes of property are exempted, but only to the value of 1,000 dollars. This approach may appear to be as arbitrary as the accrual and time-of-payment approaches discussed above, but, unlike those approaches—the first of which always gives the asset to the creditor, and the second of which always leaves it to the debtor—the proposed Act tries to ensure that the rights of each are protected. The debtor is provided with an amount necessary for his basic support, and the remainder is used to satisfy the creditors. The commission has adopted an approach that balances the competing policies of gathering the debtor's assets for the benefit of his creditors and providing the debtor with a fresh start.

That the relief of the debtor was in the minds of the Commission members is also clear from other provisions of the proposed Act. Section 4–505 provides that a bankrupt shall be granted a discharge unless he has committed any of several specified acts, and the number of grounds upon which discharge can be denied are fewer than in the present Act.[106] Section 4–506 declares that a discharge "extinguishes" a debt rather than just releasing the debtor, and, under section 4–507(a), debts so extinguished cannot be revived by a re-

102. Bankruptcy Act § 6, 11 U.S.C. § 24 (1970).

103. *See* H.R. 10792, 93d Cong., 1st Sess. §§ 4–601, –603 to –608, –610, 5–202 (1973).

104. H.R. 10792, 93d Cong., 1st Sess. § 4–503(c)(3) (1973) (emphasis added).

105. H.R. 10792, 93d Cong., 1st Sess. § 4–503(b)(1) (1973). This section also provides an additional 500-dollar exemption for each dependent.

106. For example, the previous six-year ban on refiling for bankruptcy contained in the present Bankruptcy Act § 14c(5), 11 U.S.C. § 32(c)(5) (1970), has been reduced to five years and made flexible. Under the proposed Act a second discharge may be granted within five years if "the inability of the debtor to pay his debts is the result of causes not reasonably within his control and if payment of them from future income or other wealth will impose an undue hardship on the debtor and his dependents." H.R. 10792, 93d Cong., 1st Sess. § 4–505(a)(7) (1973). *See also* COMMISSION REPORT, *supra* note 101, § 4–505, notes 4, 12.

affirmation or by a "bargain creating a new debt." This is so even though the state in which the debt was incurred recognizes the concept of moral consideration and would thus allow a debtor to reaffirm a debt discharged in bankruptcy by subsequently promising to pay without receiving further consideration.[107] The comment to this section is particularly revealing: "*Subdivision (a)* is new. [I]t carries out a policy of protecting individual debtors from erosion of the 'fresh start' which discharge and other relief under the proposed Act are intended to afford."[108] Section 4–508 similarly ensures that the debtor has an opportunity for a fresh start. Under this provision, he cannot be subjected to discriminatory treatment because he has been discharged in bankruptcy.[109]

The vitality and importance of the fresh-start policy, which, in general, is directed toward providing a bankrupt with an effective discharge, has been dramatically reaffirmed in the proposed Act. The significance of the policy has been consistently emphasized in the case law as well, most obviously in *Lines v. Frederick*. However, problems have arisen since *Lines* in determining how the policy is to be applied in specific situations. The proposed Act should eliminate the problem, since it expressly defines what must be given to the bankrupt in order to provide him with a fresh start. Until the new Act is passed, however, the courts must continue to struggle with that problem.

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107. For further discussion of this concept, see 1A A. CORBIN, *supra* note 28.

108. COMMISSION REPORT, *supra* note 101, § 4–507, note 1 (emphasis original).

109. A note to this section indicates that it is meant to codify the principle of Perez v. Campbell, 402 U.S. 637 (1971), which invalidated a state law on the ground that it conflicted with the fresh-start policy of the Bankruptcy Act by forcing a motorist either to pay a judgment from which he had been discharged or to lose his license. COMMISSION REPORT, *supra* note 101, § 4–508, note 2.