NATIONAL BANKRUPTCY CONFERENCE

Study of Individual Bankruptcy Cases and the Consumer Bankruptcy Reform Act

Consolidated Report of Key Consensus Points and Issues for Further Study
June 2022
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Overview of Project

In April 2021, the National Bankruptcy Conference (Conference) formed a working group to analyze issues in individual bankruptcy cases.[1] The primary charge of the working group involved reviewing and analyzing the Consumer Bankruptcy Reform Act of 2020 (CBRA) introduced by Senator Warren and Representative Nadler during the 116th Congress.[2] The CBRA proposes a new structure for individual bankruptcy cases that would consolidate all potential bankruptcy relief for eligible individuals into one chapter of the Bankruptcy Code (Code).[3]

Although the working group used the CBRA to frame the issues and develop related questions for study, it did not limit its research or discussions to the proposals set forth in the bill. Rather, the working group engaged in wide-ranging and in-depth deliberations concerning statutory, procedural, and policy issues relating to individual bankruptcy cases.

The Conference has not adopted a formal position on the CBRA, and this report should not be construed as acceptance or rejection of the proposed legislation. The Conference believes, however, that its study of certain issues raised by the CBRA and the Code provides a valuable resource for policymakers and other professionals to evaluate and consider potential reforms to the individual bankruptcy system.

Process Used to Facilitate Study

To tackle this project, the working group focused on five general topic areas: Structural Issues; Secured Credit; Accessibility and Eligibility Issues; Discharge Issues; and the Automatic Stay. It hosted virtual workshops on the first four topics, which included contributions from both Conferees and non-Conferees with expertise on, or particular experiences or research relating to, the study topics.[4] Conferees of the working group

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[1] The Conferees who participated on the working group are: Prof. Douglas Baird, Babette A. Ceccotti, Hon. Rebecca Connelly, Hon. Michelle M. Harner, Richardo Kilpatrick, Prof. Robert Lawless, Richard Levin, Marc A. Levinson, Prof. Bruce A. Markell, Richard G. Mason, Prof. Edward R. Morrison, John Rao, Hon. A. Thomas Small (ret.), Edwin E. Smith, Catherine Steege, Henry Sommer, J. Ronald Trost, Jane L. Vris, and Prof. Jay L. Westbrook. In addition, the working group received substantial support and input from Conferees on the Conference's Individual Debtor Committee. The views and analysis set forth in this paper represent those of the Conference and not any individual Conferee.
[2] Consumer Bankruptcy Reform Act of 2020, S.4991, 116th Cong. (2020).
[3] The CBRA also addresses several other aspects of individual bankruptcy cases under the Code, including the eligibility and filing requirements for individual debtors, the treatment of secured debt, the exemptions available to individual debtors, the kinds of debt that should be excepted from discharge, and the scope and timing of the bankruptcy discharge. The Conference reviewed these and other related issues, and most are discussed in this paper. It should be noted that this paper summarizes the extensive white papers produced by the Conference working group and does not try to capture all potentially relevant background, statutory law, case law, or policy considerations.
[4] The participants in the virtual workshops included Melyssa Barrett, Thomas L. Canary, Jr., Hon. Daniel Collins, Hon. Dennis Dow (Conferee), Edward M. Flynn, Henry Hildebrand, Prof. Ben Iverson,

volunteered to work on the various topics and produced preliminary reports and recommendations that thoroughly analyzed the various issues.

The Conference considered the working group's reports and recommendations at its annual meeting in November 2021 and its mid-year meeting in June 2022. By consensus, the Conference adopted several of these recommendations.

Executive Summary of Study

This paper reports the results of the Conference's study of individual bankruptcy cases.[5] It is organized by broad topic areas in individual bankruptcy cases, which generally correspond to the working group's study topics. Within each section, the paper summarizes recommendations on which the Conference reached consensus, identifies additional issues considered by the Conference, and encourages ongoing efforts to study and understand these important issues.

The following consensus recommendations highlight certain aspects of the Conference's study and deliberations. The primary factors underlying these recommendations and the corresponding analysis are set forth in the *Detailed Explanation of Study* section, as identified in the bullet points below. Notably, this *Executive Summary* section does not identify all consensus recommendations and readers are encouraged to review the *Detailed Explanation of Study* section in its entirety.

Key Consensus Recommendations:

- A single chapter of bankruptcy relief for individuals would be beneficial. Such an approach generally would consolidate the relief available to individuals and eliminate the need to determine which chapter best suited a particular individual debtor's needs. The Conference consensus supported the use of a single chapter for individuals to treat all of the individual's prepetition debt in the same case, at the same time. *See* Section II.A.

- The Conference supports a continued role for bankruptcy trustees in individual bankruptcy cases. *See* Section II.B.

Prof. Edward Janger, Prof. Dalié Jiménez, Soneet Kapila, Prof. Angela Littwin, Matthew Mason, Dr. William Rule, Ike Shulman, Hon. Erithe Smith, Robert Thomas, Hon. Deborah Thorne, Tara Twomey (Conferee), Prof. Jialan Wang, Dr. Elizabeth Wiggins. Conferees Hon. Rebecca Connelly, Richard Levin, Prof. Edward R. Morrison, and Catherine Steege moderated the virtual workshops. The views and analysis set forth in this paper represent those of the Conference and not any individual who participated in the virtual workshops.

[5] The focus of the Conference study and this report was individual debtors whose debts were incurred primarily for personal, family, or household purposes, such as a home mortgage, motor vehicle loan, student loan, tax liabilities, and similar obligations. These debtors generally do not have complex or elaborate financial arrangements with creditors that typically are associated with business enterprises. Issues related to eligibility for individual bankruptcy are discussed in Section IV below.

- With respect to individual debtors with few or no meaningful assets or income (i.e., NINA and LINA debtors), the Conference supports an almost immediate discharge, subject to adequate time for any objections to discharge but no other meaningful delay to the debtors' fresh start relief. Also, the Conference supports allowing individual debtors to discharge unsecured debt without performance on secured debt obligations. *See* Section II.C.

- The Conference proposes the following two alternative means to address the student loan dischargeability issue. First, modify section 523(a)(8) to eliminate "undue" from the statute (requiring only "hardship") and clarify that hardship pertains to the debtor <u>or</u> her dependents. Second, modify section 523(a)(8) to provide that student loan debt would be discharged without hardship if the debt was subject to repayment for at least five years prior to the bankruptcy. *See* Section III.A.

- The Conference consensus supports eliminating the ability of a state to opt out of the federal exemption scheme and require debtors in their state to use the state exemption scheme. A state still may adopt its own exemption scheme, but the individual debtor should be allowed to choose either the federal exemption scheme or the state exemption scheme in her bankruptcy case. *See* Section III.B.

- The Conference opposed the introduction of the means test to the Code in 2005 and continues to believe that such a test imposes unnecessary barriers to, and costs in, individual bankruptcy cases. The Conference's discussion of these issues under the Code and the CBRA uncovered a consensus that all individuals should be able to file a bankruptcy case. *See* Section IV.A.

- In order to improve effective and affordable access to the consumer bankruptcy system and establish a uniform system for the approval of attorney fees in consumer bankruptcy cases, the Conference supports amendments to the Code that would permit, subject to court approval, more flexible fee arrangements, including optional installment payments, for all attorney fees in connection with a consumer bankruptcy case. *See* Section IV.C.

- In the context of home mortgages, the Conference concluded that the secured creditor should receive the same treatment as other secured creditors, which focuses on providing the creditor the value of the collateral at the time of the bankruptcy case. The Conference also explored multiple valuation options for homes and motor vehicles and generally agreed that any such valuation standard should value the home or motor vehicle based on what the creditor would receive if required to sell the collateral outside of the bankruptcy case following modification of the automatic stay. *See* Section V.A and B.

- With respect to the repossession of a debtor's collateral prior to the bankruptcy case, the Conference determined that the creditor should bear the burden to turn over such property under section 542 of the Code. In the view of the Conference, the most sensible approach is to place this burden on the creditor who is obliged to turn over property under section 542. In addition, to ensure that a creditor either files a motion seeking adequate protection or turns over the property, the Conference supports statutory changes that would (i) protect creditors whose lien rights or priority rest on retention of the property itself and (ii) provide a private right of action against an offending creditor for damages or other appropriate sanctions. *See* Section VI.C.

Detailed Explanation of Study

I. General Approach to Individual Bankruptcy Cases

The Conference supports efforts to streamline and simplify the individual bankruptcy system. Bankruptcy should be available to all individuals who need financial relief. Although some individuals may have complex financial affairs that warrant the use of chapter 11 of the Code, most individuals will not need such complicated relief. Indeed, the overwhelming majority of individuals in financial distress qualify as either "no income and no assets" (NINA) or "low income and no assets" (LINA) debtors.[6] These individuals need a uniform system that is easy to access and understand.

Through its study of the CBRA and the individual bankruptcy system, the Conference identified several areas of existing law or practice that introduce uncertainty, delay, and cost into the system with no corresponding benefit. Those deficiencies prejudice not only individual debtors but also their creditors. A straightforward bankruptcy process that allows most individual debtors to eliminate or manage their debt and obtain a fresh financial start quickly benefits all stakeholders. Such a system should include appropriate safeguards to

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[6] The terms NINA and LINA are both commonly used in discussing individual bankruptcy relief, even though NINA debtors are necessarily consumed within the concept of LINA debtors. The Conference did not develop a precise standard for LINA debtors but acknowledged that the term should cover the overwhelming majority of individuals who seek bankruptcy relief. The Conference also did not reach consensus on any particular debt cap, means test, or minimum repayment obligation. *See infra* Section IV.A. Rather, the Conference consensus supported a debt cap only for those individuals with primarily business or commercial debt relating to an *ongoing* business operation, recognizing that a chapter designed for reorganizing operating businesses might be better suited for such cases. *See infra* Section IV.B.

protect against abuse but it should not create artificial barriers or impose unnecessary requirements that impede an individual's financial rehabilitation.

The Conference further encourages a thoughtful review of any limitations on an individual debtor's discharge in bankruptcy. The Conference believes that the honest but unfortunate individual debtor should receive as broad of a discharge as appropriate in a bankruptcy case.

II. Structural and General Discharge Issues

The Code currently provides an individual debtor relief under four chapters: chapters 7 (Liquidation), 11 (Reorganization), 12 (Adjustment of Debts of a Family Farmer or Fisherman), and 13 (Adjustment of Debts of an Individual With Regular Income). Although chapter 11 accommodates a repayment plan for an individual with non-business debts that exceed the limits for chapter 13, chapters 11 and 12 are primarily business-oriented chapters. All four chapters offer most individuals a discharge at the end of the bankruptcy case, which may be relatively quick in a chapter 7 case or may be delayed three to five years in a chapter 11, 12, or 13 case.

The Conference considered whether a different structure or an alternative oversight regime might benefit individuals needing relief under the Code. The following addresses the key issues explored during this analysis.

A. Bankruptcy Law Should Provide One Chapter to Address Individual Bankruptcy Cases

In contrast to the current structure of the Code, the CBRA provides one principal chapter, chapter 10, for individual debtors with aggregate noncontingent liquidated debts of not more than $7.5 million. An individual with debt in excess of such amount would continue to be eligible for relief under chapter 11 or 12. Chapter 13 would be repealed, and an individual would not be eligible for chapter 7. Chapter 10 would provide a menu of different forms of relief, giving the debtor a choice of one or a combination of up to three forms of repayment plans: a residence plan, a property plan, and a repayment plan.

An important component of any individual bankruptcy system is simplicity. Simplicity does not mean an easy out from one's debts or a lack of oversight. Rather, it means ensuring that the system is designed to meet the needs of individual debtors and their creditors, who generally do not have complex financial relationships and just need to understand the requirements imposed by the system to receive the necessary relief or, in the case of creditors, applicable protections.

Although the current structure of the Code and the optionality proposed by the CBRA are well-intentioned, both introduce potential costs and complexity into the system.[7] ***The consensus of the Conference was that a single chapter of bankruptcy relief for individuals would be beneficial. Such an approach generally would consolidate the relief available to individuals and eliminate the need to determine which chapter best suited a particular individual debtor's needs.***

In discussing the single chapter approach, the Conference also generally agreed that addressing all of an individual's debts in a single bankruptcy case was appropriate and aligned with core principles concerning the treatment of creditors in a bankruptcy case. This approach would, for example, allow an individual to discharge her unsecured debt while restructuring any secured debt (or perhaps surrendering the underlying collateral). As discussed below, the Conference concluded that the treatment and discharge of unsecured debt should not be dependent upon a debtor satisfying her secured debt obligations.[8]

Some Conferees supported even greater flexibility (or optionality) for individual debtors. They embraced the menu approach to bankruptcy articulated in the CBRA that would permit individuals to file a bankruptcy case to address only certain kinds of debt. For example, an individual could file a bankruptcy case to restructure her mortgage (called a residence plan under the CBRA) while leaving her unsecured debt unaltered (and not discharged) by the bankruptcy case. These Conferees believed that such an approach would offer more effective relief by giving individuals greater control over the scope of the bankruptcy case.

The Conference had robust and constructive discussions concerning optionality in individual bankruptcy cases. These discussions, like many during this study, reflected different perspectives on the policies and objectives best served by an individual bankruptcy system. The Conference understands the various policies at play in any bankruptcy legislation and explored their potential impact in the context of this study.

On balance, the majority of Conferees expressed concerns about whether an individual bankruptcy chapter that allowed debtors to pick and choose the debts to include in the case by filing separate, and perhaps multiple plans unduly increased complexity and potential "traps for the unwary."

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[7] The Conference discussed the delicate balance between simplicity and individual debtor choice in any individual bankruptcy system. Some Conferees felt strongly that the benefits to optionality outweigh any burdens associated with an increase in complexity. In general, Conferees agreed that the system should strive to manage complexity to avoid unnecessary barriers to effective relief.

[8] *See infra* Section II.C. For example, several Conferees explained the challenge to individual debtors posed by the current chapter 13 process, in which some courts will not grant the debtor a discharge of her unsecured debt, even after completing all plan payments, if she defaults on her mortgage obligations postpetition.

Indeed, some Conferees worried that individual debtors may not appreciate, for example, that a mortgage lender's deficiency claim would survive the bankruptcy if unsecured debt was not included in the case.

On balance, the Conference consensus supported the use of a single chapter for individuals to treat all of the individual's prepetition debt in the same case, at the same time.

B. Bankruptcy Trustees Should Continue to Assist Individuals in Their Bankruptcy Cases

A bankruptcy trustee currently plays an active role in an individual's chapter 7, 12, or 13 case. The trustee performs several functions in these cases, including by reviewing the debtor's financial affairs, evaluating and distributing value to the debtor's creditors, and investigating any potential abuses of the bankruptcy system. The CBRA would limit the role of the bankruptcy trustee in chapter 10 cases to focus primarily on distributions to unsecured creditors under confirmed repayment plans.

The Conference discussed the existing bankruptcy trustee system and its strengths and weaknesses, and supports a continued role for bankruptcy trustees in individual bankruptcy cases.

The trustees provide consistency to, and support for, the process, and assist the courts in upholding the integrity of the system. Some Conferees suggested that more uniformity in policy and fees across the trustee system would be beneficial, but still supported the continued use of trustees in individual bankruptcy cases.

In addition, the Conference discussed whether trustees should administer distributions only to unsecured creditors or to secured creditors as well. Under the current system, the use of conduit plans in chapter 13 cases in which the trustee makes payments to the secured creditor on the debtor's mortgage obligation is the exception rather than the rule. Some Conferees noted the potential value of having a third party, such as the trustee, administer the debtor's secured obligations, citing the aggressive behaviors of some creditors and the inadvertent accounting mistakes that can and do happen. Other Conferees, however, expressed concern regarding the fees that might be associated with conduit plans if mandated in every case. ***The Conference generally supported the use of conduit plans at the direction of the Court or the election of the individual debtor.***

C. Bankruptcy Law Should Provide a Discharge to Individual Debtors as Soon as Practicable in any Bankruptcy Case

The timing of an individual debtor's discharge under the Code depends on the chapter governing the bankruptcy case and whether the debtor is eligible to receive a discharge. For example, section 727 of the Code currently requires the court to enter a discharge in a chapter 7 case, subject to the exceptions listed therein and provided that no timely objections to discharge are filed. Considering the applicable deadlines, most individual debtors in a routine chapter 7 case receive a discharge within a matter of three to four months.

In contrast, section 1328(a) of the Code requires a court to issue a discharge in a chapter 13 "as soon as practicable" after completion of all payments under a plan. Thus, a chapter 13 debtor will not receive a section 1328(a) discharge until after completion of a 3- or 5-year plan and only if all payments are made. With the two-year extension allowed for some chapter 13 plans under the CARES Act, the period could even be seven years. If a debtor does not complete all payments, a court may grant a "hardship discharge" under section 1328(b) earlier if certain, somewhat stringent, conditions are met. In addition, some courts deny a debtor her discharge, even after satisfaction of all chapter 13 plan payments, if the debtor has not made all payments on her secured mortgage debt.[9]

The CBRA takes a different approach to the Code, offering an individual debtor a discharge shortly after the filing of the case in all instances. More specifically, the CBRA requires the court to issue a discharge "as soon as practicable" after the confirmation of a repayment plan or after the time for filing a repayment plan has expired if the debtor has no minimum repayment obligation. (Debtors without a minimum repayment obligation do not file a repayment plan.) Thus, the CBRA does not condition the discharge on the debtor's performance of plan payments and contemplates entry of the discharge early in the case.

The Conference discussed the bankruptcy discharge, including the important policy considerations underlying the discharge and the practical implications of the discharge for both debtors and creditors. These discussions focused on, among other things, ensuring the debtor access to the discharge of prepetition unsecured debt while considering appropriate protections for the estate and creditors.

[9] *Compare In re Evans*, 543 B.R. 213, 221 (Bank. E.D. Va. 2016), *aff'd Evans v. Stackhouse*, 564 B.R. 513 (E.D. Va. 2017) (denying discharge) *with In re Gibson*, 582 B.R. 15, 18 (Bankr. C.D. Ill. 2018) (disagreeing with *Evans* and similar cases).

The Conference was able to reach consensus on the timing of the discharge. Specifically, with respect to individual debtors with few or no meaningful assets or income (i.e., NINA and LINA debtors), the Conference supports an almost immediate discharge, subject to adequate time for any objections to discharge but no other meaningful delay to the debtors' fresh start relief. Also, the Conference supports allowing an individual debtor to discharge unsecured debt without performance on secured debt obligations.

With respect to other individual debtors who might have meaningful income or non-exempt assets, the Conference also supports a quick discharge, but identified issues concerning the administration of assets and the payment of creditors' claims after the discharge. For example, a quick discharge for individuals with a repayment obligation might reduce debtors' incentives to cooperate with the bankruptcy trustee or fulfill their obligations in the case. The Conferees offered a variety of ways to mitigate these concerns, including the imposition of a lien in favor of the trustee in the debtor's non-exempt assets (also proposed by the CBRA), an ability to revoke a debtor's discharge upon default, or a more significant bar to filing a future bankruptcy case or receiving a future discharge. All these potential solutions should be considered as means to facilitate a timely discharge for all qualifying individual debtors.

III. Dischargeable Debt and Exemptions

A key consideration in any bankruptcy case is the allocation of value to a debtor's creditors, which necessarily involves a determination of which debts are subject to the bankruptcy discharge and which assets a debtor may exempt from the payment of creditors' claims. The Conference generally supports a broad bankruptcy discharge, which is essential to an individual's fresh start and an opportunity for financial stability after a bankruptcy case. To that end, the Conference did not fully evaluate all aspects of the CBRA, and it encourages further study and review of the limitations on nondischargeable debt set forth in the CBRA.[10] The Conference also believes that an exemption system that provides meaningful options to individual debtors and reflects the economic realities of those debtors based on, among other things, the cost of living and the housing market in their particular geographic region, is needed and better serves a debtor's fresh start relief. Several of these issues are discussed in more detail below.

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[10] For example, the CBRA would delete subsection (C) of section 523(a)(2), which makes certain consumer debts and cash advances presumptively nondischargeable, and section 523(a)(8), which addresses student loans. The bill also would delete subsections (14) and (14A) of section 523, which address loans obtained to pay taxes and certain fines and penalties, and changes the scope of section 523(a)(7) relating to certain fines, penalties, and restitution claims relating to criminal proceedings.

A. Bankruptcy Law Should Allow Individual Debtors to Discharge Student Loan Debt

The Conference previously studied the student loan dischargeability issue, and in 2018 published a position paper recommending that section 523(a)(8) be repealed.[11] Repeal of section 523(a)(8) also was also recommended by the National Bankruptcy Review Commission in its report of October 20, 1997, and is the position taken by the CBRA.

While repeal of section 523(a)(8) has its supporters in Congress, it also has its opponents. Both sides agree that some modification to 523(a)(8) is needed, but it has been difficult for them to reach a consensus as to its scope. Consequently, the Conference took a fresh look at the student loan dischargeability issue as part of the individual debtor reform project.

Problems persist with the implementation of section 523(a)(8). The section's use of the undefined term "undue hardship," the Second Circuit's decision in *Brunner v. N.Y. Higher Educ. Servs. Corp.*, 831 F.2d 395 (2d Cir. 1987), and other statutory ambiguities continue to pose challenges for courts and barriers to effective relief for debtors. Based on the Conference's study, many professionals in the field agree that change is needed and that section 523(a)(8) in its current form is unworkable.

The Conference proposes the following two alternative means to address the student loan dischargeability issue. First, modify section 523(a)(8) to eliminate "undue" from the statute (requiring only "hardship") and clarify that hardship pertains to the debtor or her dependents. Second, modify section 523(a)(8) to provide that student loan debt would be discharged without hardship if the debt was subject to repayment for at least five years prior to the bankruptcy.

B. Bankruptcy Law Should Not Allow States to Opt Out of the Federal Exemption Scheme but Should Leave that Decision to the Individual Debtor

The CBRA includes two alternate exemption schemes, providing debtors the option to choose one or the other. One (CBRA section 522(b)(2)) is a comprehensive list of bankruptcy and other federal exemptions, and the other (CBRA section 522(b)(3)) includes applicable state law exemptions and certain specified federal exemptions. Unlike current section 522(b)(2), states would not be able to opt out of the comprehensive scheme of federal exemptions.

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[11] National Bankruptcy Conference Position Paper June 21, 2018, https://www.nbcconf.org.

The ability to opt out was the result of a political compromise between the House and Senate made in connection with the passage of the Code in 1978. The majority of Conferees believe that affording only the exemption scheme of their respective states—as have the approximately 35 states that have opted out—denies debtors across the country the ability to take full advantage of the fresh start afforded by current law and that would be provided by the CBRA. The small minority of Conferees that favor permitting opt out raised the expected difficulty in Congress eliminating the option. We note that a state may enact a scheme of exemptions that to a given debtor may be *more* attractive than the federal ones, in which case she may choose the exemptions available under section 522(b)(3).

The Conference consensus supports eliminating the ability of a state to opt out of the federal exemption scheme and require debtors in their state to use the state exemption scheme. A state still may adopt its own exemption scheme, but the individual debtor should be allowed to choose either the federal exemption scheme or the state exemption scheme in her bankruptcy case.

C. Bankruptcy Law Should Establish a National Homestead Exemption

The Conference supports the establishment of a national homestead exemption regime even if states are permitted to opt out. The laws of the various states differ widely in the amount of their homestead exemptions, ranging from virtually unlimited (Texas: No limit as to the value of urban or rural homesteads, only to their size - rural homesteads are limited to 200 acres for a family and 100 acres for a single adult, including improvements, and urban homesteads are limited to 10 acres) to a fixed statewide amount ($15,000 in Missouri) to a county-by-county calculation (California: baseline of $300,000, but can increase to up to $600,000 based on the median sale price of homes within a particular county in a particular year) to none at all (Pennsylvania). The Conference believes that no asset is more important to a debtor and her fresh start than her residence, and a federal exemption would enable debtors to retain such asset no matter their state of domicile. A few Conferees disagreed with the consensus position, citing political difficulty in enacting such a provision.

In addition, the consensus of the Conference was that the national homestead exemption should be tied to local values rather than calculated on a national or state-wide basis due to the wide range of housing costs within a state, let alone the nation. Such local valuation metrics could be based on a county, urban, rural, or similarly-targeted approach. The Conference does not take a position on the baseline for calculating the homestead, including on the CBRA's calculation of the local values by reference to the "conforming loan limit", which phrase looks to provisions of the Federal National Mortgage Association Charter Act and the Federal Home Loan Mortgage Corporation Act.

D. Bankruptcy Law Should Establish a National Wildcard Exemption

The CBRA eliminates many of the Code's à la carte exemptions (such as household goods and vehicles) and increases the amount of the federal scheme's wildcard exemption both in the base amount and then by the number of the debtor's dependents. CBRA § 522(b)(2)(A)(iii). The $30,000 base amount is doubled if the debtor has a dependent (unless the dependent filed concurrently or within the last six years). CBRA § 522(b)(2)(C)(i). Any additional dependents increase the amount further pursuant to the formula in section 522(b)(2)(C)(ii). The first additional dependent increases the amount by 25%, the second by an additional 10%, etc. Subsections (iii) and (iv) impose certain conditions on such increases. However, CBRA section 522(b)(2)(B)(i) caps federal exemptions such as certain retirement benefits that are "… manifestly unnecessary for the support of the debtor or the debtor's dependents" and section 522(b)(2)(B)(ii) establishes a rebuttable presumption that the aggregate value of such exemptions in excess of $1.5 million is manifestly unnecessary for such support.

Consistent with its support of a national homestead exemption for states that opt out (assuming that states are permitted to do so), due to the widely varying state exemption schemes, the Conference supports a national wildcard exemption that would provide debtors the tools with which to leverage their fresh start. As with the proposed national homestead exemption, the proposed national wildcard exemption would apply in lieu of any state wildcard exemptions. Nevertheless and regardless of any national wildcard exemption, any federal or state wildcard exemption should not be calculated on an item-by-item basis.

The Conference takes no position on the amount of the wildcard exemption, but believes that any wildcard exemption should account for potential differences in debtors' financial affairs such as whether the debtor is a renter, home owner, or has dependents.[12] To that end, the Conference supports increasing any wildcard exemption amount by some formula based on the number of the debtor's dependents. Such an adjustment would align with bankruptcy's fresh start policy by providing a debtor who bears financial

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[12] The Conference discussed how a lump sum wildcard exemption provides an individual debtor with flexibility in structuring the assets she will retain as part of her fresh start and avoids the need to attribute values to particular categories of assets, which may vary based on circumstances, geographic location, or other factors. The Conference did not take a position on whether or how the amount of the wildcard exemption would be impacted in cases involving a spouse who also is or was a debtor in a bankruptcy case.

responsibility for dependents an appropriate amount of exempt property to support those obligations.

IV. Eligibility and Access to Individual Bankruptcy Cases

The Conference supports reducing barriers to bankruptcy relief for individual debtors. An individual who needs the assistance of the Code should be able to file a bankruptcy case. Although individuals with significant business debt or complex financial affairs may need to proceed under chapter 11, most individuals should be eligible for a streamlined bankruptcy process, such as the single chapter bankruptcy discussed in this paper. The Conference finds little utility in burdensome paperwork or arbitrary financial requirements. It would encourage a simplified process that allows all individuals who need financial relief to file for bankruptcy, with an appropriate mechanism to channel individuals with extensive business debt or complex financial affairs into chapter 11.

A. Bankruptcy Relief Should Be Available to All Individuals

The Code does not require a technical insolvency test for an individual (or entity other than a municipality) in financial distress to file a bankruptcy case. It does, however, regulate the chapter of bankruptcy and relief available to certain individuals based on a calculation of the individual's income and expenses (generally referred to as the "means test") and, in the context of chapter 13, debt caps. Under the means test, individuals with primarily consumer debts[13] who have surplus income under the statutory calculation are presumed not eligible for a chapter 7 discharge absent limited special circumstances. Likewise, individuals with debt above the statutory caps are not eligible for a chapter 13 case. The means test and debt caps may require an individual to file a chapter 11 case.

The CBRA takes a similar but slightly different approach, limiting the eligibility for chapter 10 relief to only those individuals with debt under $7.5 million. Eligible debtors would include those "engaged in business." In addition, chapter 10 would require an individual to file a repayment plan if the individual has a minimum payment obligation (MPO). The MPO is the lesser of (1) the allowed unsecured claims or (2) the sum of the individual's non-exempt equity and a percentage of his income over certain thresholds. If the debtor has an MPO, the court may dismiss the case unless the debtor timely proposes a repayment plan and timely commences payments under the repayment plan.

The Conference evaluated the use of both a means-like test (including the MPO) and a debt cap to regulate an individual's use of the bankruptcy system. It is important to note that these two financial measures serve

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[13] Limited exceptions exclude some individuals with primarily consumer debts from the means test. *See* 707(b)(2)(D) of the Code.

different roles in a bankruptcy system: a means-like test endeavors to determine an individual's ability to repay her debt; and a debt cap is generally used to assess the complexity of an individual's financial affairs.

The Conference opposed the introduction of the means test to the Code in 2005 and continues to believe that such a test imposes unnecessary barriers to, and costs in, individual bankruptcy cases. The Conference's discussion of these issues under the Code and the CBRA uncovered a consensus that all individuals should be able to file a bankruptcy case.

The Conference also acknowledges that a chapter designed for individuals with primarily consumer debt may not be adequate for individuals with significant business debt or complex financial affairs. Those individuals should proceed with a chapter 11 case. The use of a debt cap for individuals with significant debt relating to an operating business is discussed below.

The Conference debated the utility of a means-like test, recognizing the existing expectation that individuals with some ability to repay their debts should do so. Some Conferees argued that the cost and complexity of calculating an individual's ability to pay outweigh any potential benefit to creditors or the system. These Conferees would require only that an individual devote her meaningful non-exempt assets to the payment of creditors' claims. Under such an approach, the law could require higher income individual debtors to file under another chapter, such as chapter 11. Other Conferees voiced concerns that eliminating a repayment requirement for all individual debtors would potentially weaken the integrity of the bankruptcy system, as it might expose the system to abuse and create a perception of people using the system to get out from under debt they could repay.

The Conference also explored other issues and monitoring options in the context of this debate. These are challenging issues that should be considered and appropriately weighed in any legislative reform.

Notably, despite the strongly-held views on these issues, the Conference did agree that this debate does not affect most individual debtors, as those debtors do not have sufficient income or assets to require a repayment obligation under either the Code or the CBRA. These NINA and LINA debtors should have ready access to both the bankruptcy system and the bankruptcy discharge, without burdensome financial tests. The Conference thus also agreed that any means-like or minimum payment test imposed by the Code must avoid complicating the system for, or imposing barriers to, NINA and LINA debtors.

B. Any Bankruptcy Chapter for Individuals Should Limit Its Availability to Individuals with Significant Debt from an Ongoing Business Operation

In working through when the use of a debt cap might be beneficial in individual bankruptcy cases, the Conference considered the complexity that might exist in an individual's bankruptcy case if that individual is engaged in a business or commercial activity. An individual with primarily business or commercial debt—whether from passive or active engagement with a business—might change the nature of the bankruptcy case and warrant the application of more sophisticated tools, such as those available in a chapter 11 case. Most Conferees agreed with this general concept but had different ways of defining an individual with primarily business or commercial debt.

The Conference's discussion evaluated the kinds of business or commercial debt that might exist in an individual's bankruptcy case, from debt relating to the debtor's operation as a sole proprietor, to debt stemming from passive investing or guarantees, to debt incurred for an entity in which the debtor has an active management role. Each of these, and the other possible, scenarios deserve thoughtful consideration and must be factored into any lines drawn to include or exclude individuals from a particular chapter of the Code.

On balance, the Conference reached a consensus that a debt cap would be appropriate for individuals with debt relating to an ongoing business operation. In these circumstances, the fact that the business is operating and the individual is trying to address debt relating to that ongoing business counsel in favor of the chapter 11 tools, rather than a streamlined individual bankruptcy process. Although the Conference did not identify a specific debt cap, it did discuss the $7.5 million cap used by the CBRA and by subchapter V of the Code (under the CARES Act amendments)[14] and found that such a cap might be reasonable for individuals with debt relating to an ongoing business operation.[15]

[14] *See also* Bankruptcy Threshold Adjustment and Technical Corrections Act, Pub. L. No. 117-151, 136 Stat. 1298 (2022) (continuing the debt cap established by the CARES Act for an additional time period).
[15] The Conference is not suggesting any debt or similar requirements for chapter 11 eligibility. Individuals and entities with debt at any level should continue to have access to chapter 11 relief. The Conference's discussion in this regard focused solely on when individuals with certain levels of business or commercial debt might be better served by chapter 11. The Conference's consensus on this issue reflects its general desire to avoid unnecessary complexity and requirements in any individual bankruptcy chapter designed for individuals with primarily consumer debt.

C. Bankruptcy Law Should Allow the Postpetition Payment of Reasonable and Necessary Attorneys' Fees Relating to an Individual's Bankruptcy Case

Developments in the law have limited affordable options for payment of an individual debtor's attorney fees in chapter 7 consumer cases by restricting the ways in which the attorney and individual client can arrange for the payment of fees. These restrictions arise from certain court rulings, including rulings (1) that have interpreted the Code to prohibit allowance of certain fees (*Lamie v. United States Trustee*, 540 U.S. 526 (2004), holding that, under applicable statutory provisions, attorney's fees for postpetition services on behalf of a chapter 7 debtor could not be approved and paid by the estate as administrative expenses when the attorney was not separately retained by the chapter 7 trustee); (2) holding that unpaid prepetition fees were subject to the automatic stay and the bankruptcy discharge (*Rittenhouse v. Eisen*, 404 F.3d 395 (6th Cir. 2005)); and (3) applying overly broad BAPCPA restrictions applicable to "debt relief agencies" to a debtor's attorney, thereby limiting the attorney's ability to adequately discuss fee arrangements with the client (*Cadwell v. Kaufman*, 883 F.3d 1153 (11th Cir. 2018), holding that an attorney may not advise a client to incur debt for legal fees on a credit card).

Chapter 7 debtors must find costly and difficult workarounds to avoid these limitations. Many must pay all attorney fees in advance of filing. Lump sum payments often are unaffordable and "saving up" to pay the fee delays their cases, resulting in delayed bankruptcy relief (by contrast, the Code expressly permits an award of reasonable fees for chapter 13 debtors' attorneys under section 330(a)(4) and permits fees to be paid in installments under a chapter 13 debtor's payment plan). Many chapter 7 debtors forego attorney services altogether and appear *pro se*, risking dismissal of their bankruptcy cases on any number of technical legal grounds which, with the assistance of counsel, could have been avoided. Many debtors who need chapter 7 relief can find themselves pushed into chapter 13 instead, primarily—or perhaps solely—so they can pay their attorney fees in affordable installments, even though their interests would be better served in chapter 7 or their circumstances do not support the chapter 13 requirements of a regular income and ability to maintain a creditor repayment plan. Ultimately, many of these cases fail without a discharge. In short, and as numerous studies have confirmed, the legal rules restricting more affordable options for chapter 7 debtors have worked to impede timely and effective access to the bankruptcy system.

In addition, the fee restrictions imposed by case law and the resulting workarounds have complicated the court's fee oversight process. Under section 329, a debtor's attorney must file a statement that sets forth all compensation paid or to be paid in connection with the case if the payment or agreement to pay was made within one year prior to filing the case. The court reviews the fees to determine if the compensation exceeds the reasonable value of the services. In bifurcated, or "limited service" fee arrangements, which have been devised to avoid the restrictions imposed by *Lamie* and other cases, attorneys split their legal services into separate agreements for pre- and postpetition work. These arrangements have introduced uncertainty and inconsistency into the fee approval process. They are not permitted in some jurisdictions and can raise a host of ethical issues which must be addressed in detail on a case by case basis by the courts as part of the section 329 review process. These fee arrangements also may involve questionable factoring and collection practices where a lawyer will transfer the consumer debtor's fee obligation to a third party factor who will then undertake aggressive collection practices to try to recover the fees from the debtor.

In order to improve effective and affordable access to the consumer bankruptcy system and establish a uniform system for the approval of attorney fees in consumer bankruptcy cases, the Conference supports amendments to the Code that would permit, subject to court approval, more flexible fee arrangements, including optional installment payments, for all attorney fees in connection with a consumer bankruptcy case. Approved fees, including fees for necessary pre-filing work, would become postpetition obligations of the debtor that would survive the discharge. Court review of fee arrangements would focus on expanded disclosures under section 329 and the suitability of the arrangement to the needs of the case and include specific prohibitions, such as factoring of amounts due under the fee arrangement and mandatory arbitration. Once approved, attorney fees would be paid pursuant to the terms of the court's order and enforced by the bankruptcy court during the case.

V. Treatment of Secured Debt

The Conference considered several issues affecting secured creditors in individual bankruptcy cases. For the most part, an individual's secured debt relates either to her home or her motor vehicle. Accordingly, the Code should provide appropriate alternatives for addressing this kind of debt, as the collateral often is necessary to the individual's rehabilitation. At the same time, the Code must respect the secured creditors' rights and provide appropriate protections for the creditors' interests in the collateral. The Conference discussed how best to balance these considerations in the context of both homes and motor vehicles.[16]

[16] In addition, as stated above in Section II.B, the Conference supports allowing the Court to direct, or the individual debtor to request, trustee supervision of payments to secured creditors.

A. Bankruptcy Law Should Allow Individual Debtors to Reduce All Secured Debt (including Mortgages) to the Value of the Underlying Collateral

Most individuals file bankruptcy cases to address debt relating to their homes and motor vehicles. Yet, the Code currently limits the ability of debtors who want to retain under-water homes or motor vehicles to bifurcate a home mortgage or certain secured debts and strip off the unsecured portion of the lender's claim. This limitation necessarily reduces the Code's relief and fresh start provided to individuals.

For example, section 1322(b)(2) bars a debtor from modifying the rights of a holder of a secured claim secured "only by a security interest in real property that is the debtor's principal residence." 11 U.S.C. §1322(b)(2). In chapter 7 cases, *Dewsnup v. Timm*, 502 U.S. 410 (1992) eliminated the possibility of bifurcation, and *Bank of America v. Caulkett*, 575 U.S. 790 (2015), prohibited bifurcation and stripping of totally unsecured, subordinate liens. Similarly, the hanging paragraph in section 1325(a) prevents bifurcation of purchase money security interests in motor vehicles if the debt was incurred within 910 days of the petition date, or in any other thing of value if the debt was incurred within one year of the petition date.

Notably, the treatment afforded under-water homes and motor vehicles differs in the chapter 11 context.[17] Section 1123(b)(5) prevents individuals in chapter 11 cases from bifurcating their home mortgages, but bifurcation is permissible for PMSI motor vehicle and other property loans. In subchapter V cases, an exception is made if the loan proceeds were not used to acquire the home and instead were used primarily in the debtor's business. 11 U.S.C. §§1123(b)(5), 1190.

The CBRA would allow individuals to bifurcate secured claims and strip off the under-secured portion of the relevant lien, even on the debtor's principal residence. *See* CBRA, §§ 1022(b)(1), 1022(c)(1). The one exception is for purchase money security interests in motor vehicles acquired by the debtor within 90 days of the filing of the petition. *Id*. at § 1024(d)(1)(B). A debtor who strips off the unsecured claim may discharge that debt by filing a repayment plan (in addition to the property or residence plan) if a minimum payment obligation is due or if no minimum repayment obligation exists, once the deadline for filing a repayment plan passes (to be set by a new rule). *Id*. at §1031(a). If the debtor does not file a repayment plan or otherwise elect to discharge unsecured debt, the unsecured deficiency claim will not be

[17] Likewise, individuals who are eligible for and file a case under chapter 12 of the Code are afforded more flexible options with respect to the treatment of debt secured by their principal residence or motor vehicle. 11 U.S.C. §§ 1222, 1225.

discharged because there is no discharge provided to debtors who file only residence or property plans. *See* CBRA, §1031.

The Conference reviewed the potential benefits to, and consequences of, eliminating the Code provisions that prohibit bifurcating liens and stripping off any resulting unsecured claim on an individual debtor's home or motor vehicle. ***In the context of home mortgages, the Conference concluded that the secured creditor should receive the same treatment as other secured creditors, which focuses on providing the creditor the value of the collateral at the time of the bankruptcy case. As discussed below, valuation is an important aspect of ensuring the fair treatment of creditors' claims. With an appropriate valuation standard, the Conference believes that individual debtors should be able to bifurcate a home mortgage under section 506 of the Code, thereby allowing the debtor to strip off and discharge any unsecured deficiency claim.***

The Conference also supports modifying the current 910-day rule for PMSIs in motor vehicles, which the Conferees agreed is too long. The Conference did not, however, identify a specific period during which modification should be prohibited. Many Conferees found the 90-day rule proposed by the CBRA reasonable. Some Conferees were concerned that such a significant downward adjustment would meet political opposition. ***Ultimately, the Conference concluded that a reduction in the anti-modification period for motor vehicles is needed and should serve the original goal of preventing debtors from purchasing motor vehicle with the intent of seeking immediate modification of the debt.***

B. Bankruptcy Law Should Impose a Separate Valuation Standard For Homes and Motor Vehicles in Individual Cases

Valuation is an important concept in most every bankruptcy case. Prior to the 2005 amendments to the Code, the rule applicable to all debtors and all property was that the valuation standard was to be determined in light of the purpose of the valuation and of the proposed disposition or use of the property, with the proposed use or disposition of the property being of "paramount importance." *Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997). Thus, whether the debtor intended to surrender the collateral or retain it made a difference to the standard used to value the property. *Id*. *Rash* held that for personal property, bankruptcy courts must determine whether the replacement value is the equivalent of retail, wholesale, or some other value based on the type of debtor and the nature of the property. *Id*. at 965 n.6.

The 2005 amendments to the Code changed that approach for personal property held by individuals in chapter 7 and 13 cases. Section 506 was amended to add subsection (a)(2). This subsection established that personal property held by consumer debtors would be valued "based on the replacement value of such property as of the date of the filing of the petition without deduction for the costs of sale or marketing." 11 U.S.C. §506(a)(2). If the personal property was acquired for personal, family, or household purposes, replacement value "shall mean the price a retail merchant would charge for property of that kind considering the age and condition of the property at the time value is determined." *Id*. Thus the standard that was implemented for personal property held by individual debtors following the 2005 amendments always focused on the debtor and assumed continued use of the property.

Valuation of personal property in consumer cases comes up in a variety of contexts—adequate protection and stay relief (§§361, 362), exemptions (§522), lien avoidance (§522(f)), abandonment (§554), redemption (§722) and plan confirmation (§1325)—and most frequently with respect to how to value a debtor's motor vehicle. Section 506(a)(2) is somewhat contradictory in two respects: it refers to both what a retail merchant would charge for the property and the age and condition of the property. It also provides in the first sentence of the subsection that valuation is as of the date of the filing, while the second sentence refers to the "time value is determined."

The CBRA would completely rewrite Section 506(a)(2), shifting valuation from a debtor-focused to a more creditor-focused standard. If amended, section 506(a)(2) would apply to all property, not just personal property. *See* CBRA, § 104(bb)(2). Like the current section 506(a)(2), the proposed provision would apply only to individual debtors in cases under chapter 10. *Id*. Instead of valuing property based on its "replacement value," the new provision would value property based on its "realizable value as of the date of the filing of the petition." *Id*. Section 101 would be amended to include a definition of "realizable value." *Id*. at §104(a)(1)(I). That term would mean "the value, as of the relevant date, that could be obtained for the relevant property in a lawful foreclosure, repossession, or execution sale, less the costs of such sale." *Id*. No change is proposed for Section 506(a)(1).

The Conference discussed the different approaches to valuation in individual cases. From a policy perspective, most Conferees supported the change in valuation focus proposed in the CBRA because it reflects the creditor's actual economic interest in the collateral. In addition, it furthers the debtor's fresh start by potentially making it easier for a debtor to retain property, such as a motor vehicle or a home. Other Conferees supported abolishing the different valuation standards for individual debtors and applying current section 506(a)(1) in individual cases, arguing that the valuation standard should not be manipulated to game the system for either the debtor or the creditor. These Conferees noted that the 2005 amendments sought to game the system for creditors in consumer cases, while the CBRA would game the system for consumer debtors, and this flip-flopping of viewpoints would be avoided if an economically "neutral" standard were adopted.

The Conference's consensus was that, for most kinds of property, an economically neutral approach might work. This consensus approach would, however, create a separate standard applicable only to homes and motor vehicles in individual bankruptcy cases under any chapter. Such an approach would allow bankruptcy law to tailor a valuation standard for homes and motor vehicles to the economic realities of debtors and creditors in individual bankruptcy cases, without impacting well-developed valuation standards for other property or in other kinds of bankruptcy cases. ***The Conference explored multiple valuation options for homes and motor vehicles and generally agreed that any such valuation standard should value the home or motor vehicle based on what the creditor would receive if required to sell the collateral outside of the bankruptcy case following modification of the automatic stay.***

VI. Automatic Stay Issues

The automatic stay is a core protection provided debtors under the Code. It stops most prepetition collection actions and litigation against a debtor, allowing the debtor to catch her financial breath and focus on her financial rehabilitation. In the context of individual debtors, it also serves the important role of protecting individuals from creditor harassment and aggressive collection practices. The Conference thus undertook a review of certain issues involving the automatic stay, one of which relates specifically to individual bankruptcy cases and two that would apply in all cases under the Code.

A. The Automatic Stay Should Remain in Place Unless the Individual Debtor Has Had Two or More Prior Cases Pending in a Year

Congress amended section 362 of the Code in 2005 to address serial bankruptcy filings by individual debtors. Specifically, section 362(c)(3) limits the protection of the automatic stay if the debtor had one other bankruptcy case pending (and dismissed) in the past 12 months. Section 362(c)(4) then eliminates the protection of the automatic stay if the debtor had two or more other bankruptcy cases pending (and dismissed) in the past 12 months. Both subsections are subject to adjustment by the court under appropriate circumstances. In addition, section 362(d)(4) allows a court to grant in rem relief with respect to a debtor's real property.

The implementation of section 362(c)(3) has proven problematic. The courts are split concerning whether the section terminates the automatic stay as to only the debtor and her property or, alternatively, as to the debtor, her property, and property of the bankruptcy estate. The section also poses potential barriers to debtors who have filed their cases in good faith but need to file a second bankruptcy case because of technical deficiencies in the prior case or other circumstances completely unrelated to an abusive purpose. The question thus becomes whether the potential benefit of section 362(c)(3) outweighs the costs it imposes on the system and individuals in need of bankruptcy relief.

To that end, any evaluation of section 362(c) should be considered in the context of section 362(c)(4) and (d)(4), as well as the Code's other protections against abusive filings. For example, the court can dismiss a bankruptcy case filed in bad faith under sections 707 and 1307 of the Code. In addition, sections 349 and 109(g) of the Code seek to mitigate abusive serial filings by limiting a debtor's eligibility for discharge or to refile a case. Commentators have noted that these provisions overlap with each other, and certainly appear somewhat duplicative of section 362(c)(3).

On balance, and considering the other tools available to prevent abusive filings, the Conference endorses the approach of the CBRA in deleting section 362(c)(3), retaining sections 362(c)(4) and (d)(4), and refining sections 109(g) and 349(a).

B. Actions Taken in Violation of the Automatic Stay Should be Void and Subject to Authorization by the Bankruptcy Court

The Circuits are split as to whether an act taken in violation of the automatic stay is void or voidable, although the overwhelming majority hold that such acts are void. The CBRA does not address the issue. Eight Circuits have held that stay violations are void *ab initio* and the lower courts in another appear to agree that such acts are void. One Circuit has held that actions in violation of the stay are neither voidable nor void, but "invalid" and subject to cure, and one has held that the acts are voidable.

The distinction makes a difference. If the act is voidable, the burden is on the party seeking to void it. That usually will be the debtor and places a particularly heavy burden on a consumer debtor. If the act is void, the burden is on the stay violator to seek relief from the stay, either prospectively or to annul the stay.

Current Section 362(d) authorizes the court to grant relief from the stay "… such as by terminating, ***annulling***, modifying, or conditioning such stay… (emphasis added)." The CBRA does not amend such language. Parties nevertheless often seek *nunc pro tunc* relief from the stay rather than annulment. However, a recent Supreme Court decision casts doubt on the scope of *nunc pro tunc* relief, and therefore we believe that annulment is the proper remedy.

The Conference believes that bankruptcy law should provide that stay violations are void and that parties seeking retroactive relief

from the stay should be able to rely on the annulment power included in Section 362(d), which provision is not amended by the CBRA. The Conference further supports an amendment to Section 362(d) that would authorize retroactive relief in appropriate cases for cause shown. We note that the foregoing would apply to both individual and business cases, regardless of chapter.

C. A Creditor in Possession of Property of the Estate Should Turn Over the Property Upon the Filing or Seek Appropriate Relief from the Court

Under current law, debtors have a right to the return of repossessed collateral. *United States v. Whiting Pools, Inc.*, 462 U.S. 198 (1983). For their part, secured creditors have a right to adequate protection and other relief. This much is uncontroversial. The working group addressed the procedures appropriate to vindicate each of these rights.

The Supreme Court held in *City of Chicago v. Fulton*, 141 S. Ct. 585 (2021), that a creditor who merely retains possession of collateral does not violate section 362(a)(3)'s prohibition against "any act . . . to exercise control over the property." The Court did not reach the question of how the turnover obligation of section 542 operated and whether it was self-enforcing. Thus, as matters stand, whenever a creditor does not relinquish collateral, the debtor may no longer file a motion requesting that the creditor be held in violation of the stay and instead must start the more cumbersome and time-consuming process of instituting an adversary proceeding. An adversary proceeding is required because seeking return of estate property is "a proceeding to recover money or property" within the meaning of Bankruptcy Rule 7001, and none of the exceptions apply.

Although *Fulton* involved the retention by Chicago of a vehicle impounded on account of unpaid parking tickets, the turnover problem arises most commonly when a financer repossesses an individual debtor's car. However, it also can arise with many other types of collateral and with respect to any type of debtor. Consider a creditor that garnishes a bank account prepetition. After *Fulton*, the creditor need not take any affirmative steps to extinguish the garnishment order, and it falls to the debtor to bring an adversary proceeding if it wishes to use its own bank account. *See In re Stuart*, 632 B.R. 531 (B.A.P. 9th Cir. 2021). Under *Fulton*, the creditor does not violate the automatic stay as long as it leaves the status quo undisturbed.

The question in the first instance is which of the two parties must go to court and under what procedures. ***In the view of the Conference, the most sensible approach is to place this burden on the creditor who is obliged to turn over property under section 542.*** The creditor will have the option of returning the property after the debtor makes a demand or, alternatively, bringing a timely motion in which the creditor requests adequate protection or other relief in advance of the turnover.

The Conference believes that the question of how much time the creditor has to choose between returning collateral or filing a motion is best left to the FRBP and local rules. It is possible, for example, that the amount of time that a creditor has to make its choice might vary. A creditor might face a different deadline when an individual debtor asks for the return of a repossessed car than when a corporate debtor demands return of stock certificates in chapter 11.

Consistent with the Conference's support of a change in the rules in the wake of *Fulton* that would allow the recovery of property under section 542 by motion,[18] the recommendation has the effect of simplifying the process relative to the status quo, given that the creditor's request for adequate protection or other relief also is done by motion. It also better effectuates the intent of section 363(e) which places the burden on the creditor to request adequate protection and section 542(a) which requires turnover except in limited exceptions.

In addition, to ensure that a creditor either files a motion seeking adequate protection or turns over the property, the Conference supports statutory changes that would (i) protect creditors whose lien rights or priority rest on retention of the property itself and (ii) provide a private right of action against an offending creditor for damages or other appropriate sanctions. The Conference believes such an integrated response to *Fulton*, which identifies when a creditor must act under section 542 of the Code and the consequences for any failure to so act, affords the parties certainty in the process and will reduce unnecessary costs and delay in bankruptcy cases when third parties are in possession of estate property on the petition date.

VII. Conclusion

The Conference believes that its study process has identified several areas of individual bankruptcy law that can and should be improved, as well as issues that require further exploration and evaluation. The Conference hopes that this paper contributes to the ongoing dialogue concerning individual bankruptcy reform.

[18] National Bankruptcy Conference Letter dated May 17, 2021, https://www.nbcconf.org.