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COMMENTS ON THE CONSUMER FINANCE INDUSTRY'S PROPOSALS TO IMPROVE THE POSITION OF SECURED CREDITORS IN CONSUMER BANKRUPTCY CASES*

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Creditors who sell and finance the purchase of consumer goods are extremely unhappy with the Bankruptcy Reform Act of 1978[1] (Code). They feel that the new Code is a debtor protection law that has tilted the risk of loss to them more than necessary for nonpayment on consumer sales.[2] One of their primary complaints is that certain novel aspects of the Code unfairly jeopardize purchase money liens on consumer goods. Creditors point to the redemption section as impairing their security since it permits the debtor to buy these goods for less than the contract

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[1] Bankruptcy Reform Act of 1978 (Code), Pub. L. No. 95-598, 92 Stat. 2549, 11 U.S.C. §§ 101-15132d (Supp. III 1979) [hereinafter cited as B.R.A.].

[2] *See* Papers delivered at the Consumer Bankruptcy Seminar—Public Policy Choices, sponsored by the National Retail Merchants Association and the National Consumer Finance Association in Washington, D.C. (Feb. 1981); W. MAPOTHER, CREDITORS AND THE NEW BANKRUPTCY CODE 5 (2d ed. 1980) ("of all the legislation imposed on the consumer credit industry, none has had such an immediate and changing impact as the new [bankruptcy] code"). *Record Statement of Claude Rice, Esq., Alvin O. Wiese, Jr., Esq., and Professor Jonathan M. Landers On Problems of Consumer Creditors Under the Bankruptcy Reform Act*, in 35 PERSONAL FINANCE L. Q. R. 158, 165-66 (1981) [hereinafter cited as Rice, Wiese, and Landers].

[3] In addition to their criticism of the Code's treatment of purchase money liens, creditors decry the narrowing of the fraudulent financial statement exception, B.R.A. § 523(a)(2), and its companion, B.R.A. § 523(d), which grants attorneys fees and costs to a winning debtor under B.R.A. § 523(a)(2); the "excessive" federal exemption B.R.A. § 522(d); and the failure of the preference section, B.R.A. § 547, to permit creditor retention of all funds paid to them for consumer debts under $5000 within six months of bankruptcy. Although they object to the innovations made within the traditional bankruptcy scheme, the creditors offer a more fundamental complaint. They assert that the discharge for consumers does not properly reconcile the interests of consumer debtors and creditors. They argue that the discharge of all eligible debtors for virtually all debts runs counter to the fundamental premise of the consumer credit industry that consumer debt will be repaid out of future income rather than present assets except in the last resort. The creditors think that a form of mandatory Chapter 13 should be enacted for consumer cases. This position is succinctly stated by Young, *The "Straight" Bankruptcy Ripoff*, 34 PERSONAL FINANCE L. Q. REP. 131 (1981).

price.[4] They are equally displeased by the Code's impediments to reaffirmation agreements.[5] Quite correctly, they assert that these changes impose an additional risk of nonpayment.[6]

A related complaint concerns the increased expense of protecting secured claims on consumer debts[7] in the bankruptcy process. Creditors view the Code as a lawyer's employment relief act.[8] Under the Bankruptcy Act of 1898 (Bankruptcy Act),[9] professional creditors ordinarily took care of their own affairs in consumer cases without continued recourse to a lawyer.[10] Once properly briefed, most of them were quite capable of handling mundane legal business such as filing a proof of claim for unsecured debts[11] or protecting a secured claim on consumer goods.[12] When negotiations with the debtor concerning the secured property were necessary, the creditors performed quite competently. In the case of the secured creditor this has changed. No longer is he able to protect himself. As one creditor's attorney recently emphasized, the "use of an

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[4] B.R.A., *supra* note 1, § 722 (as construed). *See* text accompanying notes 42-51 *infra*. From the creditors' perspective, B.R.A. § 1325(a)(5)(B)(ii), the Chapter 13 "cram-down" provision, causes a difficulty similar to the increased expense of protecting secured claims on consumer debts. For a description of the working of § 1325(a)(5)(B)(ii), *see* Comment, *Bankruptcy Reform Act of 1978: Chapter 13 Cramdown of the Secured Creditor*, 1981 WIS. L. REV. 333 [hereinafter cited as *Chapter 13 Cramdown*].

[5] B.R.A., *supra* note 1, § 524(c) & (d) (as construed). *See* text accompanying notes 29-38 *infra*.

[6] A starting point in the strategy of all creditors' attorneys is that their client can best protect themselves against a discharge by becoming a secured creditor in particular property of the debtor. *See* A. COHEN, DEBTOR-CREDITOR RELATIONS UNDER THE BANKRUPTCY ACT OF 1978 1-2 (1979) [hereinafter cited as COHEN]. The Code alters this view, for secured status does not offer the protection it once did. *See* notes 42-51 *infra* (use of standard other than replacement cost to determine value of goods reduces value of security interest).

[7] B.R.A., *supra* note 1, § 101(7).

[8] Commenting on the Code in a Congressional hearing Representative Drinan observed, "I realize it is a full employment bill for lawyers." *Proposed Bankruptcy Revision: Hearings on H.R. 31 & H.R. 32 Before the Subcommittee on Civil and Constitutional Rights of the House Committee on the Judiciary*, 94th Cong., 2d Sess. 1861 (1976) [hereinafter cited as *House Subcommittee Hearing*]. One cannot help but wonder, however, how much of the creditors' unhappiness is due to the existence of a new set of rules which has altered their past procedures.

[9] Bankruptcy Act of 1898 (Bankruptcy Act), 11 U.S.C. §§ 1 - 1103 (1976) (superceded by B.R.A., *supra* note 1).

[10] Mapother, *Bankruptcy Strategies for Representing Creditors in Chapter 7 and Chapter 13 Cases*, 86 COM. L.J. 133 (1981) [hereinafter cited as Mapother]. My discussions with lawyers for professional creditors throughout Virginia are in accord in Mapother's statement.

[11] Under the Act a briefing on bankruptcy procedures by a lawyer was necessary for a creditor. *See* Schrag & Ratner, *Caveat Emptor—Empty Coffer: The Bankruptcy Law Has Nothing to Offer*, 72 COLUM. L. REV. 1147, 1168-76 (1972) (description of difficulty encountered by nonlawyer creditors in comprehending forms and properly filing a proof of claim in bankruptcy).

[12] *See generally* Kennedy, *The Secured Lender and the Bankruptcy Act*, 3 U.C.C. L.J. 13 (1970) (secured creditor's rights under the Bankruptcy Act).

attorney by a secured creditor cannot be considered a luxury, it is an economic necessity dictated by good business judgment."[13] The creditors assert that such "necessary" legal fees increase the cost of bankruptcy unnecessarily.

As one would expect, the creditors have not suffered in silence. In addition to lobbying against many of the novel provisions of the Code prior to and after its passage,[14] they have offered legislation to amend the new statute. The Consumer Bankruptcy Improvements Act of 1981 (CBIA) is one example.[15] The CBIA is the product of the consumer finance industry.[16] Many of its provisions are aimed at enhancing the secured creditors' post-bankruptcy position. In examining these provisions, I will look first at the ways the Code affects the rights of creditors holding consensual liens on consumer goods, and second, indicate how the CBIA would alter the present law. Only then may the merits of the CBIA be explored.

Bankruptcy's Effect on the Secured Creditor in Chapter 7[17]

To understand better the creditors' complaint, it will be helpful to describe the continuing relations between a consumer debtor and secured creditors in a Chapter 7[18] case under the Code from the creditors perspective.[19] Assume that Dunn files for relief under Chapter 7 on January 15, 1981. Dunn "owns" a one-year old Ford automobile which she purchased from Carr and a one-year old washer/dryer combination purchased from Mees. Both Carr and Mees hold purchase money security interests on the goods they sold, and both are authorized by their

[13] Mapother, *supra* note 10, at 133.

[14] *See, e.g., House Subcommittee Hearings, supra* note 8, at 1359-69 (statement of Alvin O. Wiese, Jr., on behalf of the National Consumer Finance Association); Rice, Wiese, and Landers, *supra* note 2, at 162-72 (statement of Alvin O. Wiese, Jr. and others, on behalf of the bankruptcy discussion group).

[15] Consumer Bankruptcy Improvements Act of 1981 (CBIA), H.R. 4786, 97th Cong., 1st Sess. (1981) [hereinafter cited as C.B.I.A.]. The text of the CBIA is set out in the Appendix.

[16] The consumer finance industry includes retailers, oil companies, consumer bankers, finance companies, and credit unions. The industry is represented by various associations, formal and informal. Among these associations are the National Retail Merchants Association, the National Consumer Finance Association, the Bankruptcy Discussion Group, and the National Association of Credit Management. The Personal Finance Law Quarterly Report is probably the most prominent organ of these organizations.

[17] Chapter 13, which governs adjustment on debts, presents almost identical problems for the secured creditor of consumer goods as those discussed in the Chapter 7 context. *See* C.B.I.A., *supra* note 15, §§ 16-19. The changes suggested for Chapter 7 should be mirrored in Chapter 13.

[18] Chapter 7 governs liquidation under the Code. For an excellent discussion of all the essential aspects of Chapter 7, see Rendleman, *Liquidation Bankruptcy under the '78 Code*, 21 WM. & MARY L. REV. 575 (1980) [hereinafter cited as Rendleman].

[19] The text is based upon those decisions which have placed creditors in the worst possible position. Decisions more favorable to creditors are indicated in the notes.

security agreements to repossess their collateral on default.[20] As of January 15, Dunn was behind in her payments to both, but neither creditor had repossessed as of that date.[21]

Once bankruptcy occurs, neither Carr nor Mees may repossess their collateral because of the automatic stay of collection activity.[22] Nor may either creditor get in touch with the debtor to discover what she intends to do with the collateral.[23] While creditors may communicate with Dunn's attorney,[24] there is no obligation on her attorney's part to indicate Dunn's plans with regard to these goods.[25] Thus, unless Dunn breaks the silence, there is no contact between the parties until the first creditors'

[20] While default is an extremely significant concept under Article 9, default is not defined in the Uniform Commercial Code (U.C.C.). The omission was intentional, for the U.C.C. draftsmen assumed that the security agreement would define default. *See* Honeywell Information Sys., Inc. v. Demographic Sys. Inc., 396 F. Supp. 273, 276-77 (S.D.N.Y. 1975). *See generally* Davenport, *Default, Enforcement and Remedies under Revised Article 9 of the Uniform Commercial Code*, 7 VAL. U. L. REV. 265 (1973) [hereinafter cited as Davenport]. For an example of the default terms commonly written into a security agreement, see D. EPSTEIN & J. LANDERS, DEBTORS & CREDITORS, CASES AND MATERIALS 174-81 (1978), especially paragraphs IV through VI.

[21] For the secured creditors rights authorized by the U.C.C. on default, see R. HENSON, HANDBOOK ON SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE 357-81 (2nd ed. 1979); Davenport, *supra* note 20, at 267-97.

[22] B.R.A., *supra* note 1, § 362a(3) & (5); *In re* Cruseturner, 8 B.R. 581, 592 (D. Utah 1981). The B.R.A. § 362 automatic stay precludes collection activity against the property in the debtor's possession until the case is either dismissed or closed. B.R.A., *supra* note 1, § 362(c). If a creditor with a valid lien desires to have the stay lifted before this time, he must file an adversary proceeding. B.R.A., *supra* note 1, § 362(e); INTERIM BANKR. R. 4001(a).

[23] With reference to permissible communication between the bankrupt and her creditors, the Judiciary Committee report on the B.R.A. notes:

> The commencement of a case under Chapter 7, Liquidation, operates as a stay of all creditor action against the debtor or his property. The stay is the first part of bankruptcy relief, for it gives the debtor a respite from the forces that led him to bankruptcy. Frequently, a consumer debtor is severely harassed by his creditors when he falls behind in payments on loans. The harassment takes the form of abusive phone calls at all hours, including at work, threats of court action, attacks on the debtor's reputation, and so on. The automatic stay at the commencement of the case takes the pressure off the debtor. Once the debtor has commenced the case, all creditors' rights against the debtor become rights against the estate. Creditors must seek satisfaction of their claims from the estate. The automatic stay recognizes this by preventing creditors from pursuing the debtor.

H.R. REP. NO. 95, 595, 95th Cong., 1st Sess. 125-26, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5963, 6086-87 [hereinafter cited as House Report] (citations omitted).

[24] *See* Womack v. City Bank & Trust Co. (*In re* Womack), 4 B.R. 632, 633-34 (E.D. Tenn. 1980) (creditor may contact debtor's attorney about collateral without risking charge of harassment in violation of B.R.A. § 362).

[25] There are real pressures on the debtor's attorney to contact the debtor concerning collateral. The attorney's refusal to cooperate with the creditor could result in the creditor becoming more antagonistic to the debtor than otherwise. If the debtor is injured as a result, the attorney's fees could be reduced by the court. B.R.A., *supra* note 1, § 329(b). Thus, failure to cooperate in this setting could be seen as a breach of the attorney's ethical responsibilities. Furthermore, a debtor's attorney who gets a reputation as a recalcitrant is likely to find that his intransigency will come back to haunt him and his clients in future cases.

meeting.[26] This means that the bankrupt retains possession and use of the collateral free for at least several weeks.[27] During this period the value of the property inevitably will decline, adversely affecting the interests of Carr and Mees.[28]

At the first creditors' meeting on, say, February 15, the creditors may lawfully inquire of Dunn as to her intentions. Dunn has the following options: she may enter into a reaffirmation agreement with the creditors, voluntarily turn the collateral over to her creditors, seek to redeem the property, or do nothing at all. From the creditors' standpoint the first and second alternatives would seem preferable. Yet, even these two present problems. Let us consider each in turn. Assume that Dunn enters negotiations to reaffirm her contract on the car, and agreement is reached. Congress did not favor reaffirmations in the Code, because such arrangements often proved to be a principal cause of repeat bankruptcy.[29] Thus, even after the parties work out an agreement satisfactory to themselves, the bankruptcy court at the discharge hearing[30] might void the new bargain as not being in the best interest of the debtor.[31] In addition, the debtor has 30 days after the judge's approval to

[26] For a description of the purposes of the first creditor's meeting, see 2 W. COLLIER, COLLIER ON BANKRUPTCY ¶ 341.01 (15th ed. 1981) [hereinafter cited as COLLIER]. *See also* DeNatale, *The Creditors' Committee under the Bankruptcy Code— A Primer*, 55 AM. BANKR. L.J. 43, 43-44 (1981) (first creditors' meeting is far more significant in reorganization cases than consumer bankruptcy). Creditors holding liens on the debtor's automobile do attend these meetings for the purpose of seeking reaffirmations. Creditors with liens on less valuable items ordinarily do not.

[27] Interim Bankruptcy Rule 2003(a) provides that the "court shall call a meeting of creditors to be held not less than 20 nor more than 40 after the order for relief." INTERIM BANKR. R. 2003(a).

[28] *See* Mitchell v. W.T. Grant Co., 416 U.S. 600, 607-08 (1974) (value of merchandise declines steadily as buyer's use continues).

[29] A primary purpose of consumer bankruptcy is a fresh start for the debtor through a discharge. Reaffirmation agreements thwart the discharge. *See* REPORT OF THE COMMISSION ON THE BANKRUPTCY LAW OF THE UNITED STATES, H.R. DOC. No. 137, 93rd Cong., 1st Sess. 177 (1973) [hereinafter cited as BANKRTUPCY COMMISSION REPORT]. The Commission recommended that reaffirmations be made unenforceable. BANKRUPTCY COMMISSION REPORT, *supra*, Recommended Bill § 4-507. H.R. 8200, § 524(b) adopted the Commission position. *See also* House Report, *supra* note 23, at 163-64, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 366. The Senate would have permitted all reaffirmations. Thereafter the two bodies worked out a compromise. B.R.A., *supra* note 1, § 524(c), (d) (reaffirmations permited in limited situations). The compromise is described in the Informal Committee Report at 124, *reprinted in* CONG REC. H. 11096 (daily ed. Sept. 28, 1978). A comprehensive discussion of the legislative history of B.R.A. § 524(c) and (d) may be found in *In re* Blount, 4 B.R. 92, 93-97 (M.D. Tenn. 1980).

[30] One of the duties of the bankrupt is to "appear at the hearing required under section 524(b) of this title." B.R.A., *supra* note 1, § 521 (4). The B.R.A. § 524(4) discharge hearing has two purposes. First, to inform the debtor that a discharge has been granted or the reasons why it has not been granted; second, to counsel the debtor concerning any reaffirmation agreements which have been made. The second matter is more significant. *See* note 31 *infra*.

[31] One commentator has predicted that B.R.A. § 524(d) will eliminate reaffirmations except in a very limited number of situations. That commentator has stated:

unilaterally reject this contract.[32] These uncertainties make reaffirmation agreements less attractive to creditors than they were under the Bankruptcy Act.[33] Furthermore, if the reaffirmed contract subsequently is rescinded or the debtor defaults, the debtor still retains possession of the property for an extended period without paying for it.[34] To reclaim the property after rejection or default, the creditor must file an adversary proceeding at a cost of sixty dollars[35] to lift the stay.[36]

> Since it is difficult to conceive of a reaffirmation agreement which is in the best interest of the debtor except, perhaps, when actually further credit would not be available to the debtor in the absence of a reaffirmation, it seems quite likely that a court would approve only those reaffirmation agreements which are in settlement of nondischargeability actions or which provide for redemption.

Ahart, *Obtaining Reaffirmations of Individual Debts Under the New Bankruptcy Code*, 97 BANKING L.J. 153, 156 (1980). Such decisions as *In re* Hinkle, 9 B.R. 283 (D. Md. 1981); *In re* Delano, 7 B.R. 72 (D. Me. 1980); *In re* Berkich, 7 B.R. 483 (E.D. Pa. 1980); American Express Co. v. Griffin (*In re* Griffin), 13 B.R. 591 (S.D. Ohio 1981); and *In re* Jenkins, 6 B.C.D. 471 (E.D. Va. 1980), bear out Ahart's prediction.

[32] B.R.A., *supra* note 1, § 524(c)(2). The thirty day period is the analogue to the cooling off period found in § 429.1 of the Home Solicitation Sales Act, which has been adopted in some states. *See, e.g.*, CONN. GEN. STAT. ANN. § 42-134a to -143 (West. Supp. 1980); VA. CODE §§ 9.1-21.1 to -21.7 (1973). That Act provides that a contract may be rescinded anytime before midnight of third business day after the transaction. *See also* 16 C.F.R. § 429 (1981).

[33] A reaffirmation of a pre-bankruptcy debt was valid under the Act if permitted under state law. *See In re* Thompson, 416 F. Supp. 991, 996 (S.D. Tex. 1976). For developments under prior law, see 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).

[34] The B.R.A. § 362 automatic stay must be distinguished from the stay found in B.R.A. § 524. *See* text accompanying notes 22 & 23 *supra*. After the debtor receives a discharge at the discharge hearing and the court validates all reaffirmations, the case is closed. B.R.A. § 362(c). The § 524(a)(2) stay permanently enjoins creditors from the employment of any process to collect a discharged debt. In the example in the text, the debtor is relying on § 524(a)(2). Some courts have held that § 524(a)(2) requires the creditors enforcing valid liens to seek to have the stay lifted. *See* C.B.I.A., *supra* note 15, § 10; Recommending Notes to Proposed Consumer Bankruptcy Improvement Act of 1981 32 (April 1, 1986) (copy on file in WASHINGTON AND LEE REVIEW office) [hereinafter cited as Recommending Notes], 3 COLLIER, *supra* note 26, ¶ 524.01[3], argues, however, that the § 524(a)(2) stay was never intended to "prevent post-discharge enforcement of a valid lien on property of the debtor existing at the time of the entry of the order for relief, providing such lien was not avoided under the Code."

[35] Filing fees are set by the Judicial Conference of the United States pursuant to 28 U.S.C. § 1930(b) (Supp. III 1979). The current fee of sixty dollars was set at the Judicial Conference Session held March 7-9, 1979. *Id.*, app. § 1930. Thus, each plaintiff filing an adversary proceeding must pay the sixty dollar fee, even if the matter is prefunctory. Adversary proceedings are defined by Bankruptcy Rule 701 and Interim Bankruptcy Rule 7001. Bankruptcy Rule 701(6) provides that actions to lift an automatic stay are adversary proceedings. There is authority that no fee need be paid in this setting. *See* note 40 *infra*. For an adequate protection hearing pursuant to B.R.A. § 363, one of the most complicated and time consuming proceedings under the Code, no filing fee is required.

[36] B.R.A. § 362(e) provides that the stay shall be terminated 30 days after the request for relief is first made unless a party in interest objects. On the tactics involved, see 2 W. COLLIER, BANKRUPTCY PRACTICE GUIDE ¶ 38 (1981). Notwithstanding § 362(d), typical litigation over lifting a stay is protracted. As a result, creditors engage in litigation over the stay only as a last resort. *See also* note 34 *supra*.

Consider a variation on this theme. Dunn does not formally reaffirm but continues to make payments to Carr and Mees pursuant to the original contract. One might call this an "implied reaffirmation"[37] agreement. Dunn pays under the contract for five months and then defaults. Under the Code the creditors may not repossess their collateral until the stay is lifted, which requires an adversary proceeding.[38] Again, substantial use without payment occurs.

In the alternative, suppose Dunn chooses to release the automobile. At least two hurdles still must be cleared before Carr obtains possession of the Ford. First, the trustee must abandon the property.[39] Second, the creditor must file an adversary proceeding to lift the automatic stay.[40] At the resulting hearing the debtor might indicate the intention to redeem, for her right to do so has not been extinguished.[41] This calls for a valuation hearing. All of this causes delay and increases expenses.

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[37] Discussion with Virginia lawyers specializing in bankruptcy indicates that "implied reaffirmation" is a common occurrence.

[38] *See* text accompanying notes 34-36 *supra*. Where the reaffirmation fails because the debtor rescinds or defaults, three additional questions come to mind. First, may the creditor keep any payments received under the reaffirmation before the contract is terminated? The Code is silent. Second, does the debtor have any right of redemption? *See* note 41 *infra*. And third, where the debtor fails to keep the collateral insured, what can the creditor do? Must the creditor seek adequate protection under B.R.A. § 363? Again, the Code does not say.

[39] B.R.A., *supra* note 1, § 554; BANKR. R. 608. The trustee will only abandon property if it is of no value to the estate. Once abandoned, the property passes to whomever has a right to possess it, and the trustee may not reclaim it. If the trustee refuses to abandon the property, a hearing is necessary. B.R.A., *supra* note 1, § 554(b). If the trustee and the bankruptcy clerk's office act expeditiously to close the typical estate, the stay may be lifted automatically within 90 days of filing. *See id.* § 362(c), § 704(1).

[40] *See, e.g.*, *In re* Loving, Chapter 7 No. 7-80-00961 (W.D. Va. 1980) (B.R.A. § 362 stay remains in full force and effect pending filing of adversary proceeding even though trustee abandoned property). Five of Virginia's six bankruptcy judges agree with *Loving*. The bankruptcy judge in *In re* Mullins, 7 B.R. 1 (C.D. Cal. 1980) concurred with the approach taken in *Loving*, but this decision was reversed on appeal. *In re* Mullins, 10 B.R. 346 (9th Cir. 1980) ($60 fee not necessary where parties stipulate for abandonment).

What causes the dispute in this area? Once the property is abandoned and, therefore, no longer part of the estate, why can't the creditor accept the property? Part of the problem stems from the cryptic language found in the House Report relating to B.R.A. § 362:

> Subsection (c) of § 362 specifies the duration of the automatic stay. Paragraph (1) terminates the stay of an act against property of the estate when the property ceases to be property of the estate, such as by sale, abandonment, or exemption. It does not terminate the stay against property of the debtor if the property leaves the estate and goes to the debtor.

House Report, *supra* note 23, at 343, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6299. In addition bankruptcy judges have an obvious incentive to characterize all possible proceedings as adversary proceedings, for the amount of money allocated to each bankruptcy court for administration expenses depends on this count. *Cf.* note 29 *supra*.

[41] B.R.A. § 722 does not state when the right to redeem terminates. As yet, the cases have not decided the question. Apparently, the period for redemption is left to the discretion of the court. Dictum from *Baskins v. Household Finance Corp.* (*In re* Baskins), 14 B.R. 110 (E.D.N.C. 1981) states that "a debtor may redeem certain property pursuant to 11

Redemption was an innovation for bankruptcy.[42] It is also the hub of the secured creditors' complaint.[43] The bankrupt may redeem household consumer goods subject to consensual security interests by paying the creditor an amount equal to the item's value. If the parties cannot agree on value, it is determined by the judge in an adversary proceeding. Obviously, the meaning of "value" is crucial. The Code, however, furnishes no specific standard for value:[44] instead, it provides that "value shall be determined in light of the purposes of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use on a plan affecting the creditor's interest."[45] The legislative history indicates that the context for the valuation will be all important.[46] For redemption the measures at the two extremes are replacement[47] cost and forced sale price.[48] While the courts have used many yardsticks,[49] the majority have leaned toward the forced sale stan-

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U.S.C. § 722 after the discharge has been granted and, if necessary, as case may later be reopened by the court 'to accord relief to the debtor.'" *Id.* at 111. *See also* Catholic Credit Union v. Siegler (*In re* Siegler), 5 B.R. 12, 15 (D. Minn. 1980) (court ordered secured creditor to notify debtor of impending the sale of repossessed collateral after debtor failed to exercise right to redeem within time specified by court). The court's action in *In re* Siegler amounts to a second right of first refusal for the debtor.

[42] The right of redemption found in B.R.A. § 722 was borrowed from the Uniform Commercial Code § 9-506. For the operation of this section, see 4 COLLIER, *supra* note 26, ¶ 722.

[43] *See* text accompanying notes 50-55 *infra*.

[44] *Cf.* B.R.A., *supra* note 1, § 522(a)(2) (definition of value for purpose of exemptions).

[45] B.R.A., *supra* note 1, § 506(a). The general standard of value contained in the Code also is used to value assets in business reorganization cases.

[46] House Report, *supra* note 23, at 356, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6312.

[47] Replacement value is that which the debtor would have to pay to replace the collateral, that is, the depreciated retail price. This is the standard employed in CBIA § 6.

[48] A forced sale will produce liquidation value; the amount recoverable upon prompt resale of separate assets at a judicial sale. An intermediate measure of value would be what the property would be worth to the debtor, that is, what would the debtor pay to keep the property. Presumably, the debtor would pay less for her used property than new items, but more for the goods than the forced-sale price. For example, under the Act the trustee quite often sold household goods back to the debtor rather than sell them at a judicial sale, since the debtor would pay more for them than an ordinary purchaser. *See* Shuchman, *Little Bankruptcies in New England*, 56 B.U.L. REV. 685, 697 (1976). Such a measure of value would be subjective. Yet, since courts often find value to lie somewhere between replacement cost and forced-sale price, such findings may indicate that the judges are attempting to approximate this intermediate standard.

[49] In *Catholic Credit Union v. Siegler* (*In re* Siegler), 5 B.R. 12 (D. Minn. 1980), the parties presented six appraisal figures to the court. After discussing the six separate formulas, the court decided upon "the lien redemption value" as the amount which the debtor "would have to pay a willing seller like the plaintiff in cash or equivalent to purchase property of like kind and quality in its present condition" the court said that figure represented the same amount plaintiff would obtain "after deliberate sale" and deduction of repair expenses. *Id.* at 14. The end result was closer to forced sale than replacement cost. *In re* Stumbo, 7 B.R. 939, 939-40 (D. Colo. 1981) (forced-sale); *In re* Beranek, 9 B.R. 864, 865-66 (D. Colo. 1981) (open market value); *In re* Klein, 10 B.R. 657, 659-60 (E.D.N.Y. 1981) (commercially reasonable value); Chrysler Credit Corp. v. Cooper (*In re* Cooper), 11 B.R. 391, 394 (N.D. Ga.

dard.[50] Given that most consumer goods decline substantially in value on sale, use of a standard other than replacement cost inevitably reduces the value of the security interest. A specific example indicates how, to varying degrees, the redemption innovation as presently interpreted allows the debtor to benefit in this setting. Assume that Dunn purchased her washer/dryer for $800, with payments to be made over four years with interest. Nine months after the purchase she filed bankruptcy and thereafter elected to redeem. Using a forced sale standard the court finds the washer/dryer to be worth $250 and orders Dunn to pay Mees $250 cash within thirty days or give up possession. Assuming Dunn has paid $100 prior to bankruptcy; redemption enables her to purchase the washer/dryer for $350, $450 below the market price. Moreover, when value is determined as of date of the hearing rather than bankruptcy,[51] the creditor's security interest, as measured by the property's intrinsic value, is worth less after bankruptcy than before regardless of which yardstick is used.

Notice how redemption affects the post-bankruptcy negotiations of the parties.[52] It should be a crucial element of the debtor's bargaining

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1981) (wholesale value); *In re* Damron, 8 B.R. 323, 325-26 (S.D. Ohio 1980) (commercially reasonable value); *In re* Walsh, 6 B.C.D. 793, 794 (D.D.C. 1980) (forced-sale); McQuinn v. Dial Finance Co. (*In re* McQuinn), 6 B.R. 899, 900 (D. Neb. 1980) (replacement value).

In valuation hearings much depends on who the creditor is and the market in which he offers the goods for resale. For example, an automobile dealer probably could show a higher value for an automobile than a financial institution since the latter does not sell goods at retail. Chrysler Credit Corp. v. Cooper (*In re* Cooper), 7 B.C.D. 24, 25 & n.1 (E.D. Ga. 1980).

[50] *See* cases cited in note 49 *supra* except *McQuinn*. *See also Chapter 13 Cramdown*, *supra* note 4, at 338-43 (cases dealing with valuations of consumer items in Chapter 13). The principles for valuing consumers property for either Chapter 7 or Chapter 13 should be the same.

One certainly could argue that the forced-sale standard is appropriate in the context of redemption. When the debtor defaults, the creditor is entitled to repossess the property and resell it. Where the resale price does not cover the debt, the creditor ordinarily would be entitled to a deficiency decree. In bankruptcy, of course, the debt usually will be discharged. B.R.A., *supra* note 1, § 727(b). Thus, the debtor comes out of bankruptcy with those goods that are necessary to his fresh start at a reduced price, and the creditor subsidizes the debtor to that extent. *See* text accompanying note 154 *infra*.

[51] The Code does not dictate the date on which value should be determined. The bankruptcy courts have not agreed on timing for valuation. *See, e.g.*, Pierce v. Industrial Savings Co. (*In re* Pierce), 5 B.R. 346, 347 (D. Neb. 1980) (date of valuation hearing); Virginia Nat'l Bank v. Jones (*In re* Jones), 5 B.R. 736, 739-40 (E.D. Va. 1980) (date of proceedings requesting valuation); General Motors Acceptance Corp. v. Willis (*In re* Willis), 6 B.R. 555, 557-58 (N.D. Ill. 1980) (date of filing of petition). The *Willis* decision asserted that the choice of date was not significant since the fluctuations in value would be small and within the usual margin of error in initially establishing value. The court further indicated that this rule for valuation would apply to cases under both Chapter 7 and Chapter 13 since the choice of dates was similar in both sets of cases.

[52] The close connection between reaffirmation and redemption is evident. The Bankruptcy Commission would have abolished all reaffirmations but permitted redemptions. BANKRUPTCY COMMISSION REPORT, *supra* note 29, Recommended Bill § 4-504 & 4-507; *see* note 29 *supra*.

strategy. Assume Dunn decides to retain her washer/dryer. She, or more probably her attorney, negotiates with Mees over the terms of a reaffirmation. When Mees offers to reaffirm the original contract of sale, Dunn counters by pointing out that she can redeem for far less. This compels the creditor either to accept terms less favorable than the original contract or take his chances with the judge's decision as to value. Mees does have some leverage, for the debtor must pay cash to redeem.[53] Thus, there is pressure upon both parties to work out a new arrangement which lies somewhere between these extremes.[54] Nonetheless, the redemption section places the bankrupt in a position to improve her position against creditors holding valid-in-bankruptcy liens.[55]

Assume now that Dunn and Mees cannot reach a new agreement, and Dunn chooses to redeem. If Dunn and Mees cannot agree as to the collateral's value for this purpose, the court does this for them in an adversary proceeding. At such a hearing both parties need be repre-

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[53] GMAC v. Stewart (*In re* Stewart), 3 B.R. 24, 24-25 (N.D. Ohio 1980); *In re* Zimmerman, 4 B.R. 739, 740-41 (S.D. Cal. 1980). General Motors Acceptance Corp. v. Miller (*In re* Miller), 4 B.R. 305, 307 (E.D. Mich. 1980). *Cf.* D. EPSTEIN, DEBTOR-CREDITOR LAW 169 (2d ed. 1980) ("it is unclear whether the payment under § 722 must be a cash payment"). B.R.A. § 524(c)(4)(B)(II) seems to contemplate redemption by means of a promissory note. B.R.A. § 524(c) appears to authorize the court to approve a reaffirmation agreement which facilitates redemption by the debtor. Where the parties agree on the value of the collateral to be paid by installment with interest, the court may permit this form of reaffirmation at the discharge hearing. Interest is allowed only where there is redemption by installment. In installment cases, the contract rate of interest is employed. *See, e.g.*, Montgomery Ward v. Hall (*In re* Hall), 11 B.R. 3, 5 (W.D. Mo. 1980); *In re* Caroll, 7 B.R. 907, 909-10 (D. Ariz. 1981); Clark v. Ford Motor Credit Co. (*In re* Clark), 10 B.R. 605, 606-07 (C.D. Ill. 1981), *rev'd on other grounds*, 11 B.R. 729 (9th Cir. 1981).

[54] The parties often agree on value. *See* Hobson v. Rich's Employee's Credit Union (*In re* Hobson), 11 B.R. 220, 221 (N.D. Ga. 1981); General Motors Acceptance Corp. v. Miller (*In re* Miller), 4 B.R. 305, 307 (E.D. Mich. 1980); Credithrift of Am., Inc. v. Meyers (*In re* Meyers), 2 B.R. 603, 604 (E.D. Mich. 1980). Bankruptcy judges always encourage the parties to settle this matter. *See, e.g.*, Virginia Nat'l Bank v. Jones (*In re* Jones), 6 B.C.D. 965, 966-67 (E.D. Va. 1980).

There are creditors who do not wish to deal with debtors after bankruptcy. Professor Morris points out that in Atlanta the General Motors Acceptance Corporation would not enter reaffirmations. Because debtors seldom have free cash, they seldom redeemed. As a result, debtors often used a low percentage Chapter 13 plan of reorganization. In addition, Professor Morris and others have indicated that many creditors do not like reaffirmations of amounts under $300 because of their high administrative costs. Where the debtor has a bad credit history, creditor reluctance to continue their relations is even stronger. This too may push debtors into Chapter 13. *Cf.* Comments of U.S. Trustee Frank Dicello, note 62 *infra*.

[55] The word "lien" is defined in B.R.A. § 101(28) as a "charge against or interest in property to secure payment of a debt or performance of an obligation." Some liens that are valid outside of bankruptcy may be avoided in a bankruptcy proceeding. Thus, B.R.A. § 522(f) empowers the debtor to invalidate certain liens on exempt property, and B.R.A. §§ 544, 545, 547, 548, and 549 enable the bankruptcy trustee to strike down certain transfers that create liens. *See generally* Rendleman, *supra* note 18, at 609-46.

sented by counsel,[56] and each may call experts.[57] Considering the small amount which often is at stake, this is a relatively expensive process.[58] Moreover, there is always the possibility that, after the court determines value, Dunn might forego redemption.[59] This does not mean that Dunn would turn over the property immediately to Mees; rather, Mees still must pay sixty dollars to file an adversary proceeding to lift the automatic stay. Since the collateral remains in Dunn's possession without charge until the automatic stay is lifted, Dunn's "free ride" continues.

Finally, the debtor may do nothing. Because of the automatic stay, the creditor cannot immediately compel the debtor to release the goods.[60] No doubt the debtor's attorney will explain to her client that the creditor's costs of seeking court assistance to enforce his rights to possession may be charged to the debtor. Nonetheless, unnecessary delay and expense may arise. To this extent, therefore, the Code encourages stalling by Dunn. She retains the collateral without cost, until the creditor is in a position to force its return. Proper maneuvering can extend this process well beyond the first meeting of creditors.[61] The loss to the creditor includes not only the inevitable reduction in value of the collateral but also the various costs of reclamation of the collateral from the debtor.[62]

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[56] Bankruptcy Rule 7001 defines "adversary proceeding" as: "A proceeding before a bankruptcy judge for legal, equitable or declaratory relief which arises under nonbankruptcy law is an adversary proceeding governed by part 7 of the bankruptcy rules." INTERIM BANKR. R. 7001. The note to Rule 7001 points out that the Rule acts as a supplement to the adversary proceeding rules in Rule 701. Part VII of the bankruptcy rules is an adaptation of the Federal Rules of Civil Procedure to bankruptcy. Despite certain modifications intended to speed up bankruptcy litigation, an adversary proceeding is much like any other lawsuit and therefore requires legal advice.

[57] The creditor's statement of the value of the collateral in his proof of claim is prima facie evidence. *In re* Busman, 5 B.R. 332 (E.D.N.Y. 1980) (citing House Report, *supra* note 23). The debtor may rebut by offering testimony, including her own, as to value. *In re* Damron, 8 B.R. 323, 325-26 (S.D. Ohio 1980). Expert opinion can also take the form of appraisers' valuations or reference to industry standards, such as the National Automobile Dealers Association Blue Book. *See* General Motors Acceptance Corp. v. Willis (*In re* Willis), 6 B.R. 555, 557 (N.D. Ill. 1980) (present value of automobile is equal to average trade-in value as shown in Blue Book).

[58] *See* note 49 *supra*.

[59] Dunn might not be able to pay cash or may have discovered a better alternative.

[60] Technically, the trustee should take possession of the debtor's property. In fact, trustees ordinarily do not.

[61] *See, e.g.*, First Bank & Trust Co. v. Hart (*In re* Hart), 8 B.R. 1020, 1021 (N.D.N.Y. 1981) (seven month retention of collateral).

[62] The fees the creditor encounters in trying to take possession of the property include those for an attorney, experts, payment for the adversary proceeding, and, in most cases, time away from work for the creditor or his employees. For creditors, moreover, these fees may be incurred every time collateral is in the debtor's possession on the date of bankruptcy.

The CBIA Proposals

The consumer finance industry's proposals contemplate both procedural and substantive effects. Their procedural proposals are aimed at preventing delay in determining what happens to collateral following bankruptcy. Their substantive proposals are intended to limit the debtor's alternatives to either accepting the original contract terms thereby maintaining the value of the security interest or voluntarily returning the property to the creditor shortly after the petition is filed.

a. *The Procedural Changes: Speeding up the Process.*

Rather than give the debtor until the first meeting of creditors to decide upon a course of action, the CBIA would impose upon her the duty to notify a secured creditor within ten days of bankruptcy of her plans concerning the collateral.[63] Thus, she must indicate quickly whether to claim the collateral as exempt, redeem, reaffirm, or return it to the creditor.[64] To facilitate these choices, the CBIA would permit the creditor to communicate with the debtor about this one matter only.[65] If the debtor fails to notify creditors of her intentions by the first meeting of creditors, the stay will be lifted automatically, and the creditor may enforce his lien.[66] When a debtor does give notice and a dispute subsequently develops, the stay remains until the matter is resolved, with the resolution occurring shortly after the first creditors' meeting.[67] Thus, if the debtor's claim of exemption is challenged, the judge would resolve the issue immediately. Similarly, if the debtor seeks to redeem but the parties disagree as to price, a valuation hearing would be held at, or shortly after, the first creditors' meeting.[68] In sum, the final disposition

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Disruption of business relations increases costs. Simply accepting funds out of the ordinary course of business may generate administrative expenses. The United States Trustee for the Eastern District of Virginia, Frank Dicello, states that on several occasions he has called up creditors to inform them that he is able to pay them a percentage of their debt in installments as the debtor's estate is settled. The creditors often respond that where the amounts are small, less than forty dollars per month, it is administratively more expensive for them to accept the money than to write off the debt completely. Consumer Bankruptcy Conference, Frances Lewis Law Center, Washington and Lee University (Oct. 26, 1981) [hereinafter cited as Washington and Lee Bankruptcy Conference] (transcript on file in WASHINGTON AND LEE LAW REVIEW office). *Cf.* note 54 *supra.*

[63] *See* C.B.I.A., *supra* note 15, § 7 which amends B.R.A. § 521. *Cf.* BANKR. R. 13-201(a) (requirement that Chapter 13 debtor file proposed plan within 10 days of filing her petition).

[64] *See* C.B.I.A., *supra* note 15, § 7.

[65] *Id.*

[66] *Id.*

[67] *Id.*

[68] In the recommending note to § 7 of the CBIA, the creditors indicate that in those "situations where there is a dispute over the respective rights of debtor and secured creditor, or in the rare case where the trustee will assert an interest of the estate in such property, the court may order the status quo to be maintained until any disputed matters are resolved." Recommending Notes, *supra* note 34, at 2-3.

of the collateral would be determined far more quickly than under the Code. The creditors' proposal, of course, requires that the bankruptcy judge preside at the first creditors' meeting in consumer cases to decide the disputes which will inevitably arise.[69] To offset this expanded workload, the creditors would delete the discharge hearing.[70]

Plugging the CBIA proposals into our hypothetical case, Dunn must make her intentions known to the interested creditor much more quickly. She, or her attorney, will need to decide within ten days of filing her petition whether to retain the collateral and the best method to accomplish this result.[71] The CBIA proposal probably will weaken Dunn's bargaining position in negotiating a reaffirmation agreement, since the creditor will be able to repossess the property more quickly and inexpensively.[72] Under the Code the redemption hearing comes some period after the first creditors' meeting, possibly as much as seven months later,[73] while under the creditors' proposals this opportunity for delay is substantially reduced, forcing the parties to the bargaining table more quickly. Dunn knows that she cannot keep her consumer goods for long without payment. Since the creditor possesses the same information, the settlement, if worked out, ought to be more favorable to the creditor than under the Code. Finally, if Dunn either fails to notify her creditors or for one reason or another is not entitled to retain the collateral because she neither reaffirms nor redeems, Carr and Mees are entitled to an order directing Dunn to turn over the property without filing, and paying for, an adversary hearing.[74]

b. *Substantive Changes: Maintaining the Value of the Creditor's Security Interest.*

The substantive changes offered by the creditors would limit the effect of several of the innovations favorable to consumers found in the Code. Three of these seem especially significant:

(1) Purchase money security interests[75] currently are valued on a case by case basis in redemption cases.[76] In this setting the bankruptcy

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[69] *See* C.B.I.A., *supra* note 15, § 4.

[70] *Id.* § 10.

[71] *See* note 63 *supra*. To the extent that the new duty to decide promptly whether to keep collateral would compel the debtor's attorney to become more involved with working out the debtor's post-bankruptcy lifestyle, this change could be beneficial to the debtor. Many debtors who go through straight bankruptcy merely obtaining a discharge are no better prepared to meet their financial problems than they were before. Unless the attorney explains to the debtor how to avoid financial problems in the future, the debtor will likely be back in six years.

[72] *See* text accompanying notes 34-36 *supra*.

[73] *See* note 61 *supra*.

[74] *See* note 35 *supra*.

[75] *See* U.C.C. § 9-107 (1978 version) (definition of purchase money security interest).

[76] A debtor may redeem consumer goods subject to either purchase money or nonpurchase money security interests. Since most nonpurchase money security interests are void-

judge has much discretion in choosing the yardstick by which collateral will be valued.[77] The creditors' proposal calls for a more "objective" or concrete standard for valuation in which value is established by simple arithmetic as of the time the debtor files the petition:

> The value of consumer goods which the debtor seeks to redeem . . . shall be the greater of an established resale market price or the original purchase price reduced by straight line depreciation over the life of the property, which is presumed to be eight years.[78]

(2) Under the Code the bankruptcy judge must approve reaffirmations, and the debtor is permitted to rescind the agreement within thirty days of the discharge hearing.[79] The creditors would delete the necessity of court approval for reaffirmations and require notice to debtors of their right to rescind the reaffirmation at any time within sixty days.[80]

(3) The Code provides in section 522(f)(2) that nonpurchase money security interests on certain goods claimed as exempt are voidable by the debtor.[81] The creditors would reject this rule. Instead they propose that a debtor could redeem such property by paying the creditor its "fair market value" (forced sale) in installments.[82]

When Dunn's attorney plans Dunn's bankruptcy under these changes, the attorney will realize that her client will have to pay more for the car and the household goods. When consumer goods are sold, their market value declines substantially upon sale. To varying degrees the redemption innovation as presently interpreted allows the bankrupt

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ed under B.R.A. § 522(f)(2) or are protected by state exemption acts, such as VA. CODE § 34-26 (Supp. 1981), redemption hearings ordinarily will involve purchase money creditors who are undersecured. The primary exception will be cases where the nonpurchase money security interest is upon an automobile.

[77] *See* note 49 *supra*. At a recent consumer bankruptcy conference held at Washington and Lee, several Virginia judges made it quite clear that B.R.A. § 506 gave them latitude of decision in this area. Washington and Lee Bankruptcy Conference, *supra* note 62, at 69-72. *supra* note 62, at 69-72.

[78] *See* C.B.I.A., *supra* note 15, § 6.

[79] B.R.A., *supra* note 1, § 524(c) & (d).

[80] C.B.I.A., *supra* note 15, § 10. Where the debtor defaults after the sixty day period on a reaffirmation contract, the creditors would amend B.R.A. § 524(a) to provide that it "does not operate as an injunction against the enforcement of a lien that has not been avoided under provisions of this title." C.B.I.A., *supra* note 15, § 10(a)(4); see note 34 *supra* for an explanation of the reason for this change.

[81] B.R.A. § 522(f)(2) voids all nonpurchase money liens on a variety of items including household consumer goods, professional tools of the trade, or professionally prescribed health aids. B.R.A. § 522(f)(2) does not operate automatically. Such relief can be obtained only by filing an adversary proceeding. *See, e.g.*, *In re* Adkins, 6 B.C.D. 997 (S.D. Cal. 1980); *In re* Dardar, 6 B.C.D. 352 (E.D. Va. 1980).

[82] *See* C.B.I.A., *supra* note 15, § 13. Redemption for goods subject to purchase money security interests would remain unchanged, but value would be determined by the new standard. *See* text accompanying note 78 *supra*.

to benefit from this fact. As indicated by a prior example,[83] the Code allows Dunn to make use of this decline in value to obtain these goods at well below the original sale price, i.e. Dunn pays $250 to redeem an $800 washer/dryer. For the same situation, the creditors' method[84] requires Dunn to pay $700 to redeem.[85] In addition to increasing the value of the security interest by $450, the creditor avoids hiring an attorney to represent him, an expert witness to testify as to value, and since the case is determined more quickly, the risk of harm to the collateral is reduced.[86]

The above scenario indicates how the CBIA's proposals protect the value of the security interest. This protection becomes even clearer when one views the modification in the debtor's strategy caused by the proposals. Redemption becomes a less attractive alternative than under current practice. Dunn must pay the entire sale price immediately. For most debtors this makes reaffirmation more attractive, since the parties ordinarily agree to payment by installment.[87] Increased use of reaffirmations is the industry's goal, of course. They wish to return as closely as possible to the situation which existed before bankruptcy. Rather than a renegotiation post-bankruptcy, they prefer that the rights of the parties be spelled out by the original contract which they drafted. Once reaffirmation becomes so attractive that it tends to be the norm, the judge's capacity to void the arrangement must be abrogated. Thus, the CBIA proposals abolish the reaffirmation hearing.[88]

Finally, the creditors' contrasting treatment for nonpurchase money security interests should be noted. The creditors suggest that nonpurchase money security interests in consumer household goods, tools of the trade, and health aids be permitted but be valued by a forced sale standard with the debtor allowed to pay in installments.[89] Acceptance of such a position reduces the value of bankruptcy relief to the debtor significantly. As a practical matter, a bankrupt family must have these household items. If these are lost, they must be replaced, and such repur-

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[83] *See* text accompanying note 51 *supra*.

[84] In redemption cases, the creditors call for use of the "established resale market price" if one exists. C.B.I.A., *supra* note 15, § 6. This standard seems to apply only to vehicles because of the industry "Blue Book". See note 57 *supra*.

[85] *See* text accompanying note 78 *supra*. Clearly, one can manipulate the redemption price by varying the depreciation period. If four years were the presumed depreciation period, then Dunn would have to pay $600 instead of $700 to redeem. The eight year presumption assures creditors that the value will be set as high as the contract price.

[86] I realize that C.B.I.A. § 6 only creates a presumption of value, and that the debtor may rebut the presumption. Moreover, present Bankruptcy Rule 306(b) provides that the amount of security is deemed binding unless someone objects. The gains to creditors are two-fold: first, as amended by C.B.I.A. § 6, § 506(a) calls for a contract price standard of valuation which would prevent use of forced sale price yardstick; second, the presumption of value ought to be more difficult to overcome.

[87] *See* text accompanying notes 53-54 *supra*.

[88] *See* C.B.I.A., *supra* note 15, § 10.

[89] *See* C.B.I.A., *supra* note 15, §§ 8 & 13; text accompanying notes 81-82 *supra*.

chases may start the bankrupt on the way to more financial problems. The debtor does not start fresh. If bankruptcy is viewed as a debtor's remedy, as part of her arsenal of remedies in pre-bankruptcy negotiations with harassing creditors, the deletion of section 522(f)(2) lessens the value of this option.[90]

Evaluation of the CBIA Proposals

Consumer bankruptcy ought to implement three fundamental goals: first, it should encourage efficient administration of the bankruptcy process; second, foster the debtor's effort to obtain a fresh start; and third, interfere with the rights of creditors as little as possible.[91] Efficient administration requires that the system should implement the policies it was created to promote, that the costs of its operation should be minimized, and that cases should be disposed of quickly.[92] Most people would argue that society benefits from the efficient administration of the bankruptcy process.[93] Where a suggested change increases efficiency as defined, it merits careful consideration.

Inevitably the latter two goals will conflict to some degree. The redemption section of the Code, for example, offers a reconciliation of this conflict by Congress favoring the debtor's interest more than in the past. The debtor can buy back her consumer household goods for less than the retail price. In effect, Congress permits the debtor to renegotiate the contract of sale. That redemption concomitantly makes the creditor's lien less valuable seems indisputable.[94] The creditors not

[90] Describing the importance of B.R.A. § 522(f)(2), one commentator writes:

> . . . [T]he insolvent debtor is faced with a potentially endless series of execution sales and may quickly conclude that any gainful employment in which he is engaged will be largely for the execution creditor's benefit. What hope is there for the debtor who finds himself in a financial morass from which he cannot escape on his own? The quick answer is bankruptcy.
>
> Bankruptcy is the process by which a debtor straightens himself up, dismisses his creditors with a wave of his hand, and is reborn—albeit usually at the price of disposing of the bulk of his property.
>
> Accordingly, a debtor, faced with the unpleasant possibility of continuous creditor action, and with no reasonable hope of extricating himself from his financial predicament, may elect to start fresh and eliminate his creditors by availing himself of the bankruptcy remedy.

COHEN, *supra* note 6, at 1-2.

[91] House Report, *supra* note 23, at 3-5 *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 5964-65; BANKRUPTCY COMMISSION REPORT, *supra* note 29, at 81, *reprinted in* COLLIER, *supra* note 26, app., at 81.

[92] *See* Katchen v. Landy, 382 U.S. 323, 326-27 (1966).

[93] Those parties who would be adversely affected by my definition of efficiency may not favor it as a goal of the bankruptcy process. For example, debtors might not wish for evaluation cases to be disposed of quickly. Under the prior Act, creditors generally did not wish to expand the summary jurisdiction of the bankruptcy court because doing so would reduce their power to delay. Katchen v. Landy, 382 U.S. 323, 325 (1966) (by implication).

[94] *See* text accompanying notes 42-62 *supra*.

only challenge this congressional policy choice by characterizing it as undue interference with liens, but also assert that the redemption section as construed goes beyond that necessary to promote the fresh start policy.

In evaluating the CBIA's proposed amendments to the Code one must focus upon the three goals of the bankruptcy process. Where the debtor's fresh start conflicts with the rights of secured creditors, efficiency considerations may indicate how to avoid an impasse. In this regard, experience under the Bankruptcy Act and the Code is extremely valuable, for it indicates how the parties operate under different sets of rules. As I shall attempt to demonstrate, when the CBIA's procedural amendments are viewed in terms of their effect on the parties' strategy in the bankruptcy process, they appear to be superior to the Code both in promoting efficient administration and in reconciling the conflict between the debtor's fresh start and protection of secured creditors. The case for the substantive changes proposed is far less clear cut.

a. *Procedural Changes*

Enactment of the CBIA proposals would improve the administration of consumer bankruptcy cases by reducing both time and money spent to resolve conflicts between debtors and secured creditors over consumer goods. In this regard, the recommendations that the judge preside at the first creditors' meeting in consumer cases and that the discharge hearing be abolished seem particularly compelling.[95] Removing the judge from the first creditors' meeting was a Code innovation. The reason for this change is easy to understand. One goal of the Code was to raise the status of bankruptcy judges.[96] A judge ought to do judicial work, not tend to administrative details.[97] The judge, moreover, should not become too closely associated with the case in any capacity; the judge may hear so much information at the first meeting of creditors that he no longer appears sufficiently impartial.[98] The theory appears sound. Yet, it seems

[95] *See* text accompanying notes 69-70 *supra*.

[96] *See* House Report, *supra* note 23, at 15-18, 22, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 5976-80, 5983. *See also* Jackson, *Bankruptcy Then and Now*, 45 AM. BANKR. L.J. 249, 270 (1971). Mr. Jackson reasons that:

> It is important that the image of the bankruptcy court be favorable and one that will inspire confidence in the Bankruptcy Act and in the administration of it. The bankruptcy bar is equally as concerned as the public with the image of the bankruptcy court, its facilities, its efficiency, and the competence of the personnel of the court, including the referees, who carry the burden of the current heavy caseload.

Id.

[97] House Report, *supra* note 23, at 89-91, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6050-53; BANKRUPTCY COMMISSION REPORT, *supra* note 29, at 92-93, *reprinted in* COLLIER, *supra* note 26, app., at 92-93.

[98] House Report, *supra* note 23, at 88-89, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6049-50; BANKRUPTCY COMMISSION REPORT, *supra* note 29, at 93-94, *reprinted in* COLLIER, *supra* note 26, app., at 93-94. *Cf.* note 159 *infra*.

applicable primarily to reorganization cases, not to consumer bankruptcies.[99] One must recall that under the Bankruptcy Act, the judge performed vital judicial functions as well as administrative functions at the first creditors' meeting.[100] As the creditors note, these judicial functions should be performed at that early stage:

> Typically, the debtor will have possession of property subject to secured claims, and only the judge can direct the debtor to return the property, or can resolve questions regarding redemption. In this connection, the present recommendation should be considered with the proposal that the debtor file the statement indicating his intended disposition of collateral which is subject to security interests. . . . This proposal contemplates that many disputes regarding the statement and the debtor's proposed retention or surrender of the collateral, will be resolved at the meeting of creditors. In contrast, such disputed matters must now be resolved in separate contested or adversary proceedings.

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[99] The Brookings Institute Report (D. STANLEY & M. GIRTH, BANKRUPTCY: PROBLEM, PROCESS, REFORM (1971)) and the BANKRUPTCY COMMISSION REPORT, *supra* note 29, made parallel attacks on the old Act's workings in the area of consumer bankruptcy. The former greatly influenced the latter, and the Code descends directly from these two predecessors. Both reports had their critics. *See* Presson, *Let's Talk Some Common Sense About the Administration of Consumer Bankruptcies*, 49 AM. BANKR. L.J. 263, 277 (1975) [hereinafter cited as Presson]; Cyr, *The Bankruptcy Act of 1973: Back to the Drafting Board*, 48 AM. BANKR. L.J. 45 (1974) [hereinfter cited as Cyr]. Presson argued that neither study documented any of its findings in the consumer area, nor did either group contain any one who could qualify as an expert in the consumer bankruptcy field. Presson, *supra*, at 267-71. Judge Cyr asserted that the Commission's failure to perceive the flaws in the Brookings Report and those inherent in its own proposals were due to the fact that its members primarily were interested in business bankruptcies. Cyr, *supra*, at 46-47. Judge Cyr stated:

> The problem in this regard is not with the Congress. Rather, the fact is that those *most concerned* with bankruptcy law and practice are *concerned most* with its economic consequences, whether on an individual or societal scale. The economic consequences are most substantial for all concerned in a so-called business or commercial insolvency case than in a non-business or consumer case.

Cyr, *supra*, at 48 (emphasis in original). Cyr pointed out how much faster legislation is passed to take care of business bankruptcy problems than consumer bankruptcy problems. For instance, it took Congress 36 years to correct the problem manifested by the Supreme Court's decision in *Local Loan Co. v. Hunt*, 292 U.S. 234 (1934), concerning the most significant aspect of consumer bankruptcies, the effect of a discharge. On the other hand, it took only 11 years for legislation to overrule a decision forbidding fees to counsel working for an informal credit commission, a comparatively insignificant change, but one significant to those most concerned with business bankruptcies. Cyr, *supra*, at 49. For a criticism of the Code based on similar considerations, see Aaron, *The Bankruptcy Reform Act of 1978: The Full-Employment for Lawyers Bill*, 1979 UTAH L. REV. 1, 20-28 [hereinafter cited as Aaron].

[100] As the creditors point out, under the old Act the judge resolved disputes over the scope of the debtor's examination at the first creditors' meeting. In addition, the judge used the first creditors' meeting to deal with the alleged deficiencies in the debtor's petition, schedule, and exemption claims. *See* C.B.I.A., *supra* note 15, § 4; Recommending Notes, *supra* note 34, at 4.

> Such proceedings impose an additional cost upon both creditors and debtors, without any corresponding benefit.[101]

Of particular significance is the fact that debtors' attorneys in general agree with creditors on this matter of judicial involvement for similar reasons. Representatives of both debtors and creditors assert that the bankruptcy judge should be available to make routine decisions early in the proceedings, thus saving both sides time and money. Apparently, neither side fears judicial bias on matters that subsequently might arise.[102]

If the judge presides at the first creditors' meeting, the benefits of deleting the discharge hearings seem evident. First, as several recent bankruptcy decisions indicate, requiring the debtor always to appear at the discharge hearing is burdensome and serves no beneficial purpose.[103] Second, the hearing increases expenses for the debtor and the court. Debtors' attorneys, especially those living in rural areas, note that they often refuse to take bankruptcy cases because they must make two trips to court, one to the first creditors' meeting and a second to the discharge hearing. This repetition necessarily doubles their costs and increases their fees. If the bankruptcy judge presided at the first meeting of creditors and if the discharge hearing were abolished, there would be only one trip in most instances and, correspondingly, lower expenses and fees.

The third argument in favor of judicial presence at the first creditors' meeting is that the judge could better fulfill his counseling function at an earlier point in the process. One purpose for the creation of the discharge hearing was to impress upon the debtor the seriousness of the bankruptcy process as well as explaining her rights and responsibilities. The hope was that the aura of a federal court would impress

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[101] *Id.* at 4, 5.

[102] Statements of debtors' attorneys Richard Harman (Norfolk, Va.) and Harry Shaia (Richmond, Va.) and creditors' attorneys George Fralin (Lynchburg, Va.) and David Adams (Norfolk, Va.). *See also House Subcommittee Hearings, supra* note 8, at 1359-69 (testimony of Alvin O. Wiese, Jr.).

[103] *E.g., In re* Keefe, 7 B.R. 270, 271 (E.D. Va. 1980) (debtor's absence excused due to mental breakdown); *In re* Killett, 2 B.R. 273, 275 (E.D. Va. 1980) (debtor's nonattendance excused because of military service abroad); *In re* Garber, 4 B.R. 684 (C.D. Cal. 1980) (court held that there is no duty for debtor to appear at discharge hearing). In *Garber*, Judge Elliott had the following comments concerning the "requirement" that the debtor appear in person at the discharge hearing:

> This is an unusual requirement, to say the least. I am in full accord that reaffirmation agreements should not be enforceable unless approved by the court. However, the reason for requiring a debtor, who does not propose to reaffirm any debt, to appear in court to be informed of his right escapes me, especially when we consider that the debtor has already lost one day away from work to attend the meeting of creditors. . . .

4 B.R. at 685.

upon the debtor the duty to make use of this opportunity to become a useful, productive citizen. The first meeting of creditors would appear to be the more appropriate time to make such an impression.[104] The discharge hearing is most often a perfunctory affair, but the debtor has every reason to be alert at the first creditors' meeting.[105] Abolishing the discharge hearing also affects the Code's treatment of reaffirmations.[106]

Beyond question the CBIA proposals to speed up the process of resolving disputes over collateral would lessen the effect of bankruptcy on the secured creditor. The Code procedure, as it has developed, grants the bankrupt a free ride for a lengthy period. Allowing the debtor to retain free possession ignores the fact that the purchase money seller of consumer goods has a substantial, perhaps a paramount, interest in the collateral. Under current practice, however, his lien loses value steadily as time passes, even though it is his only claim that ordinarily survives discharge.

Did Congress intend to offer the debtor the strategy of delay to bolster her fresh start?[107] Dilatory tactics would be advantageous to the

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[104] If the judge were present, as the CBIA recommends in § 4, he could "provide whatever counseling is deemed appropriate. Indeed, this might have more impact since the bankruptcy experience will still be fresh and real. Such an approach would further emphasize judicial nature of a bankruptcy proceeding." *See* Rice, Wiese, & Landers, *supra* note 2, at 169; *cf.* C.B.I.A., *supra* note 15, § 10.

Of course, if one feared that the judge might acquire too much information, it is well worth pointing out that the judge need not preside at the entire meeting but could leave when the judicial phase ends or when the creditors question the debtor. Trustees have indicated that they have had some problems getting debtors or their attorneys to comply with the trustees' requests made at the first creditors' meeting. If the judge gave the order to the debtor, the debtor or the debtor's attorney doubtless would comply.

[105] The problems raised by the creditors regarding valuation of the debtor's assets could be handled in an alternative manner. The judge could set up a separate calendar for valuation cases and other matters arising at the first creditors' meeting. This alternative meeting precludes the possibility of the judge hearing prejudicial evidence. This alternative has been adopted by one court. *See* General Motors Acceptance Corp. v. Willis (*In re* Willis), 6 B.R. 555 (N.D. Ill. 1980). This would free the court, moreover, from the mundane matters which often arise at the first meeting.

[106] *See* text accompanying notes 157-162 *infra*.

[107] *See* Local Loan Co. v. Hunt, 292 U.S. 234 (1934). In *Local Loan*, the Court stated:

> One 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" .... This purpose of the act has been again and again emphasized by the courts as being of public as well as private interest, in that it gives to the honest but unfortunate debtor who surrenders for distribution the property which he owns *at the time of bankruptcy*, a new opportunity in life and a clear field for future effort, ...

Id. at 244 (citations omitted, emphasis in original). Debtor rehabilitation, especially consumer debtors, was emphasized by Congress in passing the Code. In describing the proposed Code, the House Report noted that it "makes bankruptcy a more effective remedy for the unfortunate consumer debtor." House Report, *supra* note 23, at 4, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 5965-66. While the discharge is the most important aspect of the fresh start, Congress was well aware that other benefits must be given to the debtor to insure the adequacy of the bankruptcy law for consumer debtors. *See* note 111 *infra*.

debtor, since filing the petition grants her free use of the property until the automatic stay is lifted. Furthermore, the capacity to maintain the status quo for an appreciable period would aid the debtor in negotiations over reaffirmation. Nonetheless, I doubt that Congress intended to favor the debtor in this manner. Admittedly, the fresh start of the consumer bankrupt was a dominant consideration for Congress in revising the bankruptcy laws. The House Report emphasized that the Bankruptcy Act was not designed to provide adequate relief to the consumer debtor.[108] Creditors had developed methods to limit the benefit of bankruptcy to the debtor so that she was no better off than before. "Overbroad security interests on all of a consumer's household and personal goods, reaffirmations, limited state exemption laws, and litigation over dischargeability of certain debts have all contributed to the consumer debtor's post-bankruptcy plight."[109] Correcting these and other shortcomings was necessary for adequate post-bankruptcy relief designed to grant the consumer bankrupt a fresh start.[110] The Code incorporates a number of innovations designed to achieve this goal.[111]

The novel redemption provision was a part of the fresh start policy. This section attempted to reconcile the conflict between the debtor and the secured creditor, according to the House Report, by allowing "the debtor to retain his necessary property and avoid high replacement costs, [without preventing] the creditor from obtaining *what he is entitled to under the terms of his contract.*"[112] Significant delay does impair the secured creditor's position. Unless delay is a necessary incident to the debtor's fresh start, amendments to speed up the process seem appropriate.

Do the CBIA proposals overly inhibit the debtor's effort to begin again? The proposal that the debtor notify secured creditors within 10 days about her plans for collateral in her possession does not seem unduly burdensome. In choosing bankruptcy the debtor's attorney should have considered which items her client would need and have planned accordingly.[113] In Dunn's case, for example, if her fresh start depends

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[108] In reviewing the provisions of the Act, the House Report stated: "The primary thrust of the 1938 revision [of the Act] was toward business bankruptcies, because consumer bankruptcy was not a significant factor in the 1930s. The Bankruptcy Act has not kept pace with the modern consumer credit society." House Report, *supra* note 23, at 116-17, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6076-78.

[109] *Id.* at 117, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6077-78.

[110] *Id.* at 117-18, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6077-79.

[111] *See* B.R.A., *supra* note 1, § 722 (redemption §), § 524(c) (discharge hearing), § 362(a) (automatic stay provision derived from BANKR. R. 401 & 601), § 524(a) (discharge injunction), § 525 (prohibition against discriminatory treatment of bankrupt), § 1325(a) ("cramdown" provisions), § 1328 (discharge provisions).

[112] House Report, *supra* note 23, at 127, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6088.

[113] *See* Rendleman, *supra* note 18, at 584-86; Wickham, *Bankruptcy or Not? Advice for Attorneys who Counsel Consumer Debtors*, 41 TENN. L. REV. 667 (1974) (dealing with 1898 Act).

on owning an automobile, her attorney should have worked out the best method to achieve this result. If keeping the present vehicle is the better option, the lawyer should test the reaffirmation possibilities before deciding precisely how to proceed. Requiring that the decision making process start shortly after bankruptcy does nothing to defeat the congressional policy favoring the fresh start. It merely places upon the debtor's attorney the duty to plan her client's estate immediately, one similar to that found in Chapter 13.[114]

Adoption of the creditors' approach means that the first creditors' meeting becomes the time of decision.[115] If the parties have been unable to work out a new agreement by that time, the debtor's choice is redemption or abandonment of the property. The debtor still holds the property free for at least 30 days, and probably more. The period is ample for the debtor both to get her affairs in order and to work out a settlement with creditors. More delay threatens substantial impairment of the creditor's security. If the debtor can show cause why more time is justified, the court could order an extension.

The possibility of creditor harassment does not significantly lessen the merit of these proposed changes. One of the purposes of the automatic stay is to prevent creditors from importuning debtors after bankruptcy about pre-bankruptcy debts until the debtor has the opportunity to get her affairs in order.[116] The debtor's remedy if the creditor oversteps is clear: several courts have granted debtors relief from various forms of collection activities before the automatic stay has been lifted.[117] Whether the debtor will inform her attorney about creditor harassment is unclear.[118] Conceding the problem exists, the change still seems preferable.[119]

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[114] BANKR. R. 13-201(d).

[115] *See* C.B.I.A., *supra* note 15, § 7.

[116] *See* note 23 *supra*; House Report, *supra* note 23, at 169-70, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6130-32; *see also* note 22 *supra*.

[117] *See, e.g.*, GMAC v. Miller, 13 B.R. 110, 118 (S.D. Ind. 1981) (damages and fees); *In re* Elder, 12 B.R. 491, 494 (M.D. Ga. 1981) (attorney's fees); *In re* Womack v. City Bank & Trust Co., 6 B.C.D. 543, 544 (E.D. Tenn. 1980) (court costs and attorneys fees).

[118] The communication between the debtor and her attorney will depend on the relationship which develops between them. Quite often in a Chapter 7 case the debtor's attorney, or a paralegal, fills out the forms, explains to the debtor the benefits of the discharge, takes a fee and then lets the debtor fend for herself. Such is the role of the attorney painted by several studies of the bankruptcy process. *See generally* D. STANLEY & M. GIRTH, BANKRUPTCY: PROBLEM, PROCESS, REFORM 41-106 (1971). Whether the debtor will realize there is something that she can do about the abuse, or have enough confidence in the attorney to tell of harassment, is another question. Under the system proposed by the creditors, however, there is more pressure on the attorney to plan out the entire bankruptcy for the debtor, and for this reason a better relationship between attorney and client may develop. Alternatively, the new procedure may result in an increase of fees rather than services, reducing even further the relief for the debtor. Predictions of which would result are difficult.

[119] Some debtors file bankruptcy *pro se*. Whether such people are entitled to extra protection seems debatable. While we should not require everyone to hire a lawyer, we must

Although many of the procedural changes proposed by the creditors have much to recommend them, the suggested method of change can be improved. Where possible these changes should be implemented through the new Bankruptcy Rules rather than by altering the statute. The function of the Rules is both to standardize and improve the administration of the system.[120] All of the suggested changes except the revision requiring the judge to preside at the first meeting of creditors could be implemented through the Rules.[121] This change could be accomplished by following the lead of Judge Merrick who, in *General Motors Acceptance Corp. v. Willis (In re Willis)*,[122] established a separate contested calendar to decide all questions relating to disputes concerning collateral in the bankrupt's possession. Such a rule could lead to increased efficiency for all concerned. Finally, since most bankruptcy judges have ignored the duty imposed on the debtor to appear at the discharge hearing unless reaffirmation agreements are involved,[123] a rule to this effect would codify present practice. Implementing such changes through the Rules rather than the legislative process would undoubtedly be easier and occur more quickly.[124]

b. *The Substantive Changes*

Throughout their proposals the creditors sharply distinguish between purchase money and nonpurchase money security interests on consumer goods, desiring greater protection for the former.[125] Congress also recognized this traditional distinction, predicating section 522(f)(2)'s avoidance powers upon it. This difference in treatment was based upon

assume that they understand the risk. The bankruptcy process is very complicated even for attorneys, and I can see no reason why we should make a special rule for *pro se* cases, if the rule suggested is generally beneficial.

[120] Suggested Interim Bankruptcy Rules have been promulgated. These rules were revised due to the changes made in the Code.

[121] *See generally*, Kennedy, *The Proposed Bankruptcy Rules and Official Forms*, 46 AM. BANKR. L.J. 53 (1972). A Bankruptcy Rule may not directly overturn a substantive command of Congress.

[122] 6 B.R. 555 (N.D. Ill. 1980); *see* note 105 *supra*.

[123] *See* note 103 *supra*.

[124] Only Congress can alter the Code. As Congressman Butler pointed out at the recent Washington and Lee Bankruptcy Conference, Congress is in no mood to change a statute so recently enacted. Washington and Lee Bankruptcy Conference, *supra* note 62, at 14-15. In fact, one reason the present Code passed through Congress so slowly was that body's indifference to it. Compare Coogan, *The New UCC Article 9*, 86 HARV. L. REV. 477 (1973), in which the author discusses changes made in Article 9 to coordinate it with the Federal Tax Lien Act. He points out that the "sponsors of the new Article 9 in effect have decided that it may be easier to change the Code through action of at least fifty legislatures than to correct the federal tax lien provisions by one act of Congress." *Id.* at 514. In contrast, a small body of bankruptcy experts formulates the Rules. *See generally* W. BROWN, FEDERAL RULEMAKING: PROBLEMS AND POSSIBILITIES (1981).

[125] *See* C.B.I.A., *supra* note 15, §§ 6, 8, & 13. Purchase money creditors occupy a similar favorable position in the UCC. *See* U.C.C. §§ 9-301(2), 9-302(d), & 9-312(5) (1978 version).

substantial evidence which indicated that creditors take nonpurchase money security interests in tangible personal property, other than an automobile, for their "in terrorem" effect.[126] Professional creditors know that such items have little resale value. The creditor does not rely upon the value of the property subject to his lien to prevent loss on default. Rather, he would prefer to threaten the debtor with repossession in order to compel preferential treatment for his obligation.[127] This tactic is standard operating procedure for many creditors.[128] Unless the creditors demonstrate more than the loss of their power to coerce, no reason for change comes to mind. As Congress and others have stressed, avoidance of nonpurchase money liens on consumer goods is a crucial part of the debtor's fresh start.[129] The creditors tacitly admit the weakness of their position by agreeing that valuation in non-purchase money cases ought to be on the basis of forced-sale standard, with payment by installments permitted.[130] Acceptance of this standard, of course, would reintroduce the evils Congress desired to nullify.[131]

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[126] House Report, *supra* note 23, at 171-72, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6132-33.

[127] Describing creditor psychology with regard to taking security interests in debtor property unrelated to the debt, the House Report on the Code states:

> Frequently, creditors lending money to a consumer debtor take a security interest in all of the debtor's belongings, and obtain a waiver by the debtor of his exemptions. In most of these cases, the debtor is unaware of the consequences of the forms he signs. The creditor's experience provides him with a substantial advantage. If the debtor encounters financial difficulty, creditors often use threats of repossession of all the debtor's household goods as a means of obtaining payment.
>
> In fact, were the creditor to carry through on his threat and foreclose on the property, he would receive little, for household goods have little resale value. They are far more valuable to the creditor in the debtor's hands, for they provide a credible basis for the threat, because the replacement costs of the goods are generally high. Thus, creditors rarely repossess, and debtors, ignorant of the creditors' true intentions, are coerced into payments they simply cannot afford to make.

Id. at 127, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6088.

[128] According to legal aid lawyers, it is common practice in Virginia for lenders to extract from the debtor not only a security interest in all of the debtor's household goods, but also a waiver of exemption. Many household goods are exempt in Virginia from all but purchase money liens, and this exemption may not be waived. VA. CODE §§ 34-26, 34-28 (Supp. 1981). *Cf.* VA. CODE § 34-22 (Supp. 1981) (waiver of the homestead exemption permitted). While creditors are well aware that nonpurchase money security interests are void in Virginia, they still threaten to levy on such property. It is not unusual for the creditor to bring a sheriff to threaten the debtor, and the sheriff, knowing no better, willingly cooperates. When the sheriff comes to the door, the debtor, if possible, finds some way to make payment on these debts. In this manner the creditors gain a preference.

[129] House Report, *supra* note 23, at 127-28, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6088-89.

[130] C.B.I.A., *supra* note 15, § 5.

[131] Discussion with attorneys for creditors who take nonpurchase money security interests indicates that they do not wish to repossess. One attorney told me that his client had a strict policy against repossession of household goods. In addition, those who obtained non-

In contrast to non-purchase money situations, Congress continued to recognize purchase money liens on the consumer goods listed in section 522(f)(2).[132] Why not also permit the debtor to avoid the purchase money lien on these items? Recognition of any lien on these items will adversely affect the debtor's fresh start. As Congress clearly recognized the debtor must replace items such as her furniture, kitchen stove, or clothing regardless of whether they are subject to a purchase money or nonpurchase money lien.[133] The difference in treatment of the two, however, must be predicated upon a traditional view of the relative equities of the parties.[134] The seller's interest in the goods is paramount until the purchase price is paid. The debtor's interest is comparatively limited. If the debtor defaults, the owner is entitled to reclaim his goods. In addition, Congress failed to find evidence of those evil creditor practices which served as the policy basis for section 522(f)(2).[135] Thus, the purchase money creditor remains a favorite of the law.[136]

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purchase money interests prior to Oct. 1, 1979, the effective date of the Code, need not be concerned with B.R.A. § 522(f)(2). *See* Rodrock v. Security Indus. Bank (*In re* Rodrock), 3 B.R. 629, 633-34 (D. Colo. 1980), *aff'd*, 642 F.2d 1193 (10th Cir. 1981); Adams v. Parker (*In re* Parker), 10 B.R. 562, 566 (M.D. Ala. 1981); *In re* Woods, 9 B.R. 325, 329 (E.D. Mich. 1981).

[132] B.R.A. § 522(f) permits the debtor to void judicial liens and nonpurchase money security interests. B.R.A. § 522(e) nullifies the effect of a waiver of exemption.

[133] The House Report at 128 quotes the following conclusion of the Bankruptcy Commission in explaining the need for redemption:

> The Commission's recommendation furthers the policy underlying the recommendations as to exemption. For example, it does little good to allow the debtor an exemption of wearing apparel, household goods, or health aids subject to an indefeasible security interest securing a purchase-money obligation, if the debtor must pay more than the property is worth for the privilege of continuing to use the property. The fair market value of such property is often substantially less than the amount owed and little if anything can be realized upon forced disposition of the property. What the creditor really has is leverage to force payment under the present Act, since continued use is conditioned on forebearance by the creditor and forebearance is exacted at a higher price.

House Report, *supra* note 23, at 128, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6089.

[134] The traditional justification for the favored position of the purchase money lien is ably set forth in 4 AMERICAN LAW OF PROPERTY § 16.106E (A. Casner ed. 1952). A somewhat different rationale justifying the privileged position of this creditor is delineated in J. WHITE & R. SUMMERS, UNIFORM COMMERCIAL CODE 920, 1042-45 (2d ed. 1980). The distinction is so well ingrained in most lawyers that even the Treasury, during the heyday of the "choateness" doctrine, conceded the priority of the purchase money lien against the government's claims. *See* W. PLUMB & L. WRIGHT, FEDERAL TAX LIENS 80 (1972). Nonetheless, purchase money liens are not sacrosanct. *See* Fuentes v. Shevin, 407 U.S. 67 (1972), *modified by* Mitchell v. W. T. Grant Co., 416 U.S. 600 (1974). These decisions indicate that some limits on purchase money creditors are permissible. How much, if any, of the philosophy of *Fuentes* carried over into the Code is unknown.

[135] *But see* note 133 *supra*. Retail merchants, however, seldom take security interest in other goods of the debtor as other lenders often do. *See* notes 126 & 127 *supra*.

[136] One might question the rationale for sustaining any liens on consumer goods. Certain kinds of creditors, such as grocers, hardwaremen, doctors, often grant credit but the character of the product sold prevents their taking a security interest. In constrast, auto

Yet, the Code does make definite inroads on this favored position. As previously indicated[137] the redemption section has enabled the debtor to purchase her household consumer goods usually for an amount below, sometimes substantially below, the original contract price. The varying standards used reflect the bench's inability to define congressional intent in this area. While the legislative history of redemption evinces a purpose to allow the debtor to keep these goods for something less than the going rate, how much less is not indicated.[138] Congress deliberately wrote a vague standard for all valuation situations into the Code,[139] informing the judges that they must "determine value on a case-by-case basis, taking into account the facts of each case and the competing interests in the case."[140] The principal benefit of the present method is flexibility. The judge has discretion to set value for each case, and such decision will have little precedential value. The principle appears sound. Each case is treated individually.[141] Yet, such a full blown inquiry is expensive relative to the dollar amount at stake. To illustrate, let me again return to Dunn's redemption of her washer/dryer.[142] On my figures there was a $450 variation depending on whether a forced sale or a replacement measure of value was used. The difference is quite significant but one must consider the other costs to the debtor. Attorneys' fees, possible expert witness fees, the debtor's loss of pay due to missing employment and court costs could reduce this amount considerably.[143] And, of course, the

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dealers and furniture stores who take indefeasible security interests obtain preferential treatment to some extent solely on the basis of the nature of the product sole. In a consumer case, should not all of the debtor's creditors share the loss pro rata? Is it more than tradition which leads to favoring certain creditors? The justification may lie in the comparatively high investment in the particular item sold. The automobile is a clear example. Yet, as the consumer finance industry itself indicates, sellers, including those with purchase money liens, do not want to repossess if they can avoid it. *See* C.B.I.A., *supra* note 15, § 7 and accompanying recommending notes. Possibly, the traditional view is retained because Congress was not certain how such a radical change would affect consumer sales, an area of great importance to the health of the economy generally.

[137] *See* text accompanying notes 42-51.

[138] In two places the House Report describes redemption as giving "a right of first refusal to the debtor" for consumer goods. House Report, *supra* note 23, at 127, 381, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6088, 6337. Arguably, this language means that "value" is determined by the amount the creditor could realize through his normal resale procedures. Some judges have attempted to use this as a yardstick. *See* note 49 *supra*.

[139] B.R.A., *supra* note 1, § 506(a).

[140] House Report, *supra* note 23, at 356, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6311-12. *See* Aaron, *supra* note 99, at 13 n.94.

[141] Several bankruptcy judges have indicated to me that they like the current practice for just this reason. *See* Washington and Lee Bankruptcy Conference, *supra* note 62, at 71-72.

[142] *See* text accompanying notes 51, 84-85 *supra*. In my illustration an extreme case was intentionally chosen. Had the guidelines set forth by Judge Merrick been used, the washer and dryer would have been valued at $640. *See* note 133 *supra*.

[143] B.R.A., *supra* note 1, § 330, which deals with the compensation of attorneys, was intended to overrule cases such as Moshein v. Beverly Crest Convalescent Hospital, Inc. (*In re*

debtor might lose (or "win" less). Creditors, too, bear the same risks and costs.[144]

From this experience under the Code, I conclude that using this process to measure the value of consumer goods[145] is unsatisfactory. Some judges, who apparently share this view, have established guidelines for future valuation contests involving consumer goods on the assumption that it is not crucial to have a finely-tuned valuation standard in this area.[146] On this point I emphasize that neither debtors' nor creditors' at-

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Beverly Crest Convalescent Home, Inc.), 548 F.2d 817 (9th Cir. 1976), and *In re* Spisak, 2 B.C.D. 1952 (N.J. 1977) which limited fees "on notions of conservatism of the estate and economy of administration." House Report, *supra* note 23, at 329-30, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS at 6286. To prevent first rate attorneys from leaving the bankruptcy field, attorneys are entitled to compensation based on the value of the services rendered. *Id.*; Neville v. Eufaula Bank & Trust Co. (*In re* U.S. Golf), 639 F.2d 1197, 1201 (5th Cir. 1981). Of course attorneys are not paid the legal rate of compensation for performing nonlegal services. *See In re* Jones, 13 B.R. 192, 194 (E.D. Va. 1981); *In re* Underground Utilities Construction Co., 13 B.R. 735, 738 (S.D. Fla. 1981).

The attorneys' fees for any case depend on the time spent and the standard charge of the attorney for the work. For example, in *In re* Cipriano, 8 B.R. 697 (D.R.I. 1981), the attorney for a secured creditor was allowed to collect $350 (5 hours at $75) for services rendered in connection with the valuation of an automobile in a Chapter 13 case, after the attorney conceded that the time spent to prepare, execute and file a proof of claim could not be recovered at his usual rate. *Id.* at 698-99. My discussions with several Virginia attorneys indicate that collateral hearings usually take somewhat less than five hours of billable time. As these cases become more routine, bankruptcy judges may decide that attorneys fees for such cases ought to be awarded at a lower rate. *Cf.* Neville v. Eufaula Bank & Trust Co. (*In re* Golf), 639 F.2d at 1201 (12 factors to be considered in setting attorney's fees).

[144] Some experts argue that adverse decisions in the bankruptcy courts are due to a failure to hire competent attorneys and, therefore, the creditors' problems are of their own making. One would think that economic considerations would compel the opposite result, but several debtors' lawyers have also indicated that for the most part the creditors have been poorly represented. These lawyers opined that very often not enough was at stake for the better-heeled creditors to use their counsel on retainer.

[145] My comments are not aimed at business reorganization matters where larger dollar amounts are involved.

[146] *See* General Motors Acceptance Corp. v. Willis (*In re* Willis), 6 B.R. 555 (N.D. Ill. 1980). In *Willis*, Judge Merrick set out guidelines for valuations and his reasons for doing so. *Id.* at 556-57. The guidelines were promulgated both to save court time and to explain to the attorneys what was involved in such proceeding. *Id.* at 556-59. The judge created several guidelines for particular types of property. For example, furniture would be valued according to the following schedule:

Less than one year old 75%
One year to two years old 50%
Two to three years old 20%
More than three years old 0

Id. at 557. Appliances would be treated a little differently.

Less than one year old 80%
One year to two years old 65%
Two years to three years old 50%
Three years to four years old 25%
More than four years old 10%

Id. Carpet and draperies would be valued by another schedule:

Less than one year old 25%

torneys favor the present experiment on the ground that it is unduly expensive for their clients. Rather, both groups would prefer a standard as precise as that of the CBIA's proposal or the judges' guidelines.[147]

Deciding upon the standard which ought to be adopted is a more difficult, although less significant, question. The CBIA proposal incorporates a depreciated cost measure unless a "recognized market" for second hand goods exists.[148] A recognized market exists apparently only for automobiles.[149] For other goods the creditors suggest that value should be equal to the "original purchase price reduced by straight line depreciation over the life of the property which is presumed to be eight years."[150] Assuming "original price" means the amount that a cash customer would pay, then the eight year depreciation standard pre-

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One to two years old 10%
More than two years old 0

Id. at 558.

Finally, Judge Merrick created a docket for valuation hearings so that the attorneys would not have to sit around his courtroom for a long time waiting for their case to be called. *Id.*; *see* note 122 *supra.*

[147] Many Virginia attorneys have told me that when valuation cases, as well as other kinds, are decided against their clients, the bankruptcy judges suggest an appeal. Presumably this matter evenutally will reach the courts of appeals. While our system resolves many legal questions in this fashion. I have difficulty believing this is the optimum solution in this context. Appeals are not costless to either side. The amount involved is often small, although it may be significant to the parties. Few bankrupts can afford to litigate. For similar reasons most creditors do not want to. Even in those cases that do go up on appeal, I am not sure that valuation questions are the kind that a court of appeals could resolve satisfactorily. A most significant task of any appeals court is to construct rules which can be easily administered by trial judges. In a collateral valuation case, what kind of rule may an appeals court offer? It might direct bankruptcy judges to use a particular yardstick, but most such yardsticks still would require a hearing of some kind. Or, the court might create its own guidelines for use in bankruptcy courts throughout its circuit similar to those developed by Judge Merrick. *See* note 146 *supra.* Yet, I wonder if a court of appeals is in a position to know what is appropriate. Moreover, this alternative undoubtedly will create conflicts among the circuits, leading to nonuniformity in the area of bankruptcy. While some observers consider lack of uniformity tolerable as to exemptions, B.R.A. § 522(b)(2), similar considerations do not seem applicable in this area. The best decision for an appeals court would be to direct trial judges to develop their own guidelines.

[148] C.B.I.A., *supra* note 15, § 6. *Cf.* text accompanying notes 46-50 *supra.*

[149] Several judges have adopted the National Automobile Dealers Used Car Guide (NADA Blue Book) to value cares presumably because "it covers a broad series of transactions between willing buyers and willing sellers, and the sellers (of the traded-in cars) are consumers similar to the debtors before the court." General Motors Acceptance Corp. v. Willis (*In re* Willis), 6 B.R. 555, 559 (N.D. Ill. 1980). *See* note 57 *supra.* Yet, most used car dealers pay absolutely no attention to the NADA Blue Book in purchasing cars themselves. While mileage is not irrelevant, it is comparatively unimportant. For the dealer who plans to resell the vehicle, the question is how much will it cost to recondition the car in relation to its potential resale value. For this reason, the NADA Blue Book probably seldom will be determinative. Furthermore, since a good deal of money is often at stake, the dealers will show up to defend their interest.

[150] C.B.I.A., *supra* note 15, § 6.

cludes the debtor from taking advantage of the normal decline in value which always occurs on the sale of consumer goods. Nonetheless, since the "original price" can be determined easily,[151] I think such a standard is appropriate, for it closely approximates the value of the goods to the debtor.[152] This standard seems preferable to one based on a forced sale yardstick. Such a yardstick cannot be applied automatically. Nor does it necessarily reflect what most creditors could get for the goods if repossessed.[153] Finally, I can find no good reason why retail merchants ought to subsidize bankrupts to this additional degree.[154]

Let me suggest an alternative method, one which retains some of the benefits of the present practice but should lower its costs. By creating the redemption section, Congress undoubtedly assumed that the parties generally would settle on value. Where the parties settle outside of the judicial forum, they should be more willing to accept the terms of the settlement than if it is imposed from the bench. Any suggestion, therefore, ought to foster settlement. Where the parties are not able to settle, each party should submit a final offer to the court. The property should then be valued by an appraiser, appointed from a panel by the judge. The appraiser's decision would be final. The cost of the appraisal would be paid for by the party whose final offer was most at variance with that of the appraiser.[155] This alternative has several benefits: first,

[151] The Truth in Lending Act requires that the base price be clearly stated. *See* 15 U.S.C. § 1638(a) (1976).

[152] One could certainly argue that the retail price measures the value of the use of the collateral to the debtor. When consumers purchase an item, its value to them is at least its retail price, if one assumes that the debtor knows exactly what he is buying and how much utility the good will yield. There are cases where lack of information about the particular good and its market make this assumption untenable, but in the case of automobiles as well as most consumer goods, one must assume that consumers have adequate information available to them.

Of course, one could manipulate the value of these goods under this standard by simply presuming a shorter depreciation period. If one assumes, for example, that the depreciation period is 4 years instead of 8, one lowers the presumed value of the goods. *See* note 85 *supra*. In the alternative, one might say that the presumed depreciation period will be either the length of time of the installment contract or the length of warranty granted by the seller. Such a rule might foster purposes external to the Bankruptcy Code.

[153] *See* note 49 *supra*.

[154] The debtor's creditors subsidize the fresh start provided by bankruptcy in several ways. The exemption laws might be viewed "as legalized frauds on creditors, in the sense that they declare a public policy of having debtors retain certain essential aids to their support in preference to the satisfaction of creditors' claims." J. MACLACHAN, HANDBOOK OF THE LAW OF BANKRUPTCY 161 (1956). The discharge of most pre-petition debts granted to most bankrupts under B.R.A. § 727(b) has a similar affect. *See* Rendleman, *supra* note 18, at 679-81. Retail sellers, moreover, often operate in highly competitive markets which make it difficult for them to spread this loss over other sales.

[155] The suggestion for determining which party should pay the appraisal costs is a simplified version of final offer arbitration in labor settlements. *See generally*, Finille & Long, *Final-Offer Arbitration: "Sudden Death" in Eugene*, 27 INDUS. AND LAB. REL. REV.

each case is treated individually; second, the debtor gets some of the benefit of the decline in value which occurs on sale; third, settlement should be encouraged; fourth, the judicial time is saved; fifth, this procedure can be adopted by an appropriate bankruptcy rule.[156]

If valuation for redemption is determined by a concrete standard, the reaffirmation problem should be less bothersome. The suggested methods for valuation tighten up the present rather loose framework for the redemption, thereby reducing uncertainty. Reducing uncertainty should encourage the two sides to enter an arrangement satisfactory to both, rather than one dictated by the court.

Finally, there is a question of whether the judge should continue to determine the wisdom of the reaffirmed contract.[157] Where the debtor and her attorney work out the terms with the creditor, the answer would seem to be no. So long as the debtor's counsel endorses the reaffirmation, this should be sufficient assurance that the debtor's interests have been considered.[158] The 60 day period to rescind might be retained to determine whether the arrangement will work as the debtor anticipated.[159] If counsel does not sign the reaffirmation, the debtor may

186 (1974); Howlett, *Contract Negotiation Arbitration in the Public Sector*, 42 U. CIN. L. REV. 47, 71-74 (1973). One might accomplish the same result by having the expense of the appraiser be part of the bankruptcy system, but this could lead to excessive use since the parties would not bear this cost.

[156] *See* text accompany notes 119-24 *supra*. The CBIA proposals would require several amendments to the Code.

[157] *See* text accompanying notes 32-34, 87-88 *supra*.

[158] When I wrote the accompanying textual sentence, I did not have the benefit of the comments of Professor Morris who served on the trustee's panel in Atlanta for several years. He writes:

> I wish that I had the time to tell you about all of the ridiculous reaffirmations debtors' counsel have proposed to the bankruptcy judges in Atlanta. Not only are many of the attorneys who represent debtors incompetent to handle reaffirmations problems, but even more are simply unwilling to do so. Your proposal seems to put them in the "judges" shoes, deciding what is in the debtor's best interest. In addition to the difficulties just noted, you are inviting animosity between the debtor and her attorney in many cases.

Letter from Professor Jeffrey Morris to author (Dec. 15, 1981).

If Professor Morris' remarks accurately reflect the level of attorney competence in this area, the underpinning for my suggestions certainly is flawed. Some responsible person must decide this matter and if neither the debtor nor her attorney is competent, that leaves the judge by default. This conclusion seems like an invitation to the judge to act as the debtor's attorney which may have ramifications beyond this particular matter. A better solution might be for the judge to affirm the agreement that has been approved by counsel, and then, if the agreement turns out badly, place the extra costs on the attorney as an incentive to do better in the future.

[159] Considering the difficulties that reaffirmation arrangements have caused in the past, a period for rescinding reaffirmations seems appropriate. Since it is hoped that the debtor's attorney will remain involved, the 60 day period will give the attorney time to see how the contract works and whether it is in the debtor's best interest to rescind. Assuming that the attorney is involved, his advice, as opposed to that of the judges, seems preferable. *See* note 158 *supra*.

need the protection designed into the reaffirmation hearing. In that case the judge should review the agreement at the first creditors' meeting, and if the terms are not as good as the debtor could obtain in some other fashion, the reaffirmation ought to be rejected.[160]

The "implied reaffirmation"[161] should be treated similarly. Only if counsel endorses such an arrangement by the first meeting of creditors should it become binding on the debtor. This rule would place an increased burden on the creditor to make sure that all implied reaffirmations were called to the court's attention at the first meeting of creditors, but this duty is correlative with the increased responsibility imposed on the debtor. The purpose of this obligation is to force the parties to formalize the arrangement, guaranteeing for the debtor the protection that Congress thought necessary for reaffirmations.[162]

Conclusion

The treatment of creditors holding purchase money security interests on consumer goods has caused problems apparently unforseen by the Code's draftsmen. The CBIA's proposals are helpful in pointing to methods by which these difficulties may be corrected. The good news is that the more serious flaws can be corrected through the Bankruptcy Rules. This should lead to quicker relief.

For me this experience points to a broader conclusion. The difficulties stemming from redemption and related innovations may be traced in large part to Congress' decision to have the bankruptcy judges evolve a common law for this area. As all lawyers know, litigation is expensive. Moreover, the common law generally develops slowly. On some consumer bankruptcy matters, litigation cannot be avoided. Determining whether a particular debt should be discharged[163] or whether a specific

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[160] While the Code's position does seem paternalistic, the creditors' position ignores past history. Congress found substantial evidence that reaffirmation agreements have harmed debtors. Furthermore, cooling off periods or notice provisions to the debtor in other contexts alone have not provided a remedy against abuses. My proposal should encourage creditors to keep the debtor's attorney involved, thereby benefiting all concerned.

[161] *See* text accompanying note 38 *supra*.

[162] Suggested Interim Bankruptcy Rule 4002 provides that upon the debtor's request the court "shall defer the entry of an order granting a discharge for 45 days, . . ." and a further delay can be obtained for cause shown. INTERIM BANKR. R. 4002. The purpose of the extension is to authorize time for the debtor to settle dischargeability litigation through reaffirmation agreements. Under Bankruptcy Rule 404(a), the court may fix a time not less than 30 or more than 90 days after the first creditor's meeting to file an objection to discharge, and Rule 404(d) authorizes awarding the discharge immediately if no challenge to the discharge is filed within this period. Finding Rule 404(d) inconsistent with B.R.A. § 524(c), the Interim Rule 4002 authorizes the debtor 45 days extra to enter into reaffirmations. The Interim Rule suggests its own limitation; the period for reaffirmation may be extended to settle dischargeability questions. INTERIM BANKR. R. 4002. This special case should be treated differently from reaffirmations generally. *See* note 31 *supra*. Otherwise, the reaffirmation should be voidable by the debtor.

[163] B.R.A., *supra* note 1, § 523(a).

piece of property fits into a category of exemptions are examples.[164] On the other hand, litigating the value of consumer goods for redemption and other purposes seems a poor choice *a priori*. Congress failed to decide how much of a benefit was intended, thereby aggravating the situation.[165] The same difficulties have developed in Chapter 13 as judges attempt to put a gloss on the phrase "good faith" in disputes involving confirmation of the debtor's plan.[166]

The lesson, if there is one, is that innovations for consumer bankruptcy cases should contain definite standards *where these are possible*. More definite standards are possible in this area. To ignore the process by which these standards will evolve is largely to nullify the benefits anticipated from the innovation.

[164] *See, e.g.*, B.R.A. § 522(d)(2)-(4). Even the categories of possible exemptions seem unnecessarily vague. B.R.A. § 522(d)(10)(D) exempts "alimony, support, or separate maintenance, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor." Does this mean that the bankruptcy judge overrides the decision of the trial judge as to amount? *See* COHEN, *supra* note 6, at 104.

[165] *See* text accompanying notes 137-40 *supra*.

[166] B.R.A., *supra* note 1, § 1325(a)(3). *See generally What Creditors Need to Know About Chapter 13 Under the Bankruptcy Reform Act of 1978, Consumer Bankruptcy Seminar, Public Policy Choices* (1981).

Appendix

Consumer Bankruptcy Improvements Act

A BILL

To amend title 11, United States Code, to establish an improved basis for providing relief under chapter 7, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Bankruptcy Improvements Act of 1981".

SEC. 2. Section 109 of title 11, United States Code, is amended by inserting after subsection (e) the following new subsection:

"(f) An individual may be a debtor under chapter 7 of this title only if such individual cannot pay a reasonable portion of his debts out of anticipated future income.".

SEC. 3. Section 305 of title 11, United States Code, is amended by inserting after subsection (c) the following new subsection:

"(d) The court may dismiss a case under chapter 7 of this title upon the motion of any party in interest made not later than thirty days after the meeting of creditors, and after notice and a hearing, if the debtor is ineligible for relief under the provisions of section 109(f).".

SEC. 4. Section 341(c) of title 11, United States Code, is amended—

(1) by striking out "(c) The" and inserting in lieu thereof "(c)(1) Except as provided in paragraph (2) of this subsection, the", and

(2) by adding at the end thereof the following new paragraph:

"(2) The court shall convene the meeting of creditors in a case involving a consumer debtor under chapter 7 or chapter 13 of this title and shall adjudicate any matters appropriate for resolution.".

SEC. 5. Section 342 of title 11, United States Code, is amended by adding at the end thereof the following new sentence: "The notice shall include a copy of the statement of income and expenses specified in section 521(2)."

SEC. 6. Section 506(a) of title 11, United States Code, is amended—

(1) by striking out the last sentence,

(2) by inserting "(1)' "after "(a)", and

(3) by adding at the end thereof the following new paragraph:

"(2) The value of the creditor's interest in the estate's interest in such property shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest. The value of consumer goods which the debtor seeks to redeem pursuant to section 722 of this title or which are to be retained pursuant to section 1325(a)(5)(B)(ii) of this title shall be the greater of an established resale market price or the original purchase price reduced by straight line depreciation over the life of the property, which is presumed to be eight years.".

SEC. 7. Section 521 of title 11, United States Code, is amended—

(1) in paragraph (4) by striking out "hearing" and inserting in lieu thereof "meeting",

(2) by redesignating paragraphs (2), (3), and (4) as paragraphs (4), (5), and (6), respectively.

(3) by inserting after paragraph (1) the following new paragraphs:

(2) if the debtor is an individual, file a statement of income and expenses setting forth—

(A) the debtor's current income;

(B) an estimate of the debtor's current expenditures for living expenses and the support of his family;

(C) All income which the debtor reasonably expects to receive within the two years following the petition; and

(D) all expenditures which the debtor reasonably anticipates he will have to make within the two years following the petition which are not included in subparagraph (B) above;

"(3) if the debtor's schedule of assets and liabilities includes consumer debts which are secured by property of the estate, file and serve, within ten days after filing the petition, upon each creditor holding such security and the trustee, a statement expressing the debtor's intention with respect to retention or surrender of the collateral and, if applicable, specifying that the collateral is claimed as exempt, that the debtor intends to redeem the collateral, or that the debtor intends to reaffirm debts secured by the collateral;"

(4) by inserting "(a)" before "The debtor", and

(5) by adding at the end thereof the following new subsection:

"(b) At or before the meeting of creditors provided for by section 341 of this title, the debtor shall perform his intention with regard to secured creditors, as specified by subsection (a)(3), by surrendering such property to the creditor or the trustee, redeeming such property by paying the redemption price, or reaffirming the debt. The creditor may communicate with the debtor to facilitate such performance without being held to have violated section 362 of this title. If the debtor has not fully performed his obligations under subsection (a)(3) and this subsection at or before the meeting of creditors, the stay imposed by section 362 shall terminate with respect to the enforcement of liens against such property, unless the courts order otherwise.".

SEC. 8. (a) Section 522(b) of title 11, United States Code, is amended—

(1) by striking out paragraph (1),

(2) by striking out, "other than subsection (d) of this section," in paragraph (2)(A), and

(3) by redesigning paragraphs (2)(A) and (2)(B) as paragraphs (1) and (2), respectively.

(b) Section 522 of title 11, United States Code, is amended by striking out subsection (d).

(c) Section 522(f) of title 11, United States Code, is amended by striking out "lien is" and all that follows through the period and inserting in lieu thereof "lien is a judicial lien.".

SEC. 9. (a) Section 523(a) of title 11, United States Code, is amended—

(1) in paragraph (2)(A) by striking out "or actual fraud" and inserting in lieu thereof "actual fraud, false credit history, or falsification of other facts reasonably related to the debtor's incurring liability for the debt,", and

(2) in paragraph (3) by striking out "section 521 (1)" and inserting in lieu thereof "section 512(a)(1)".

(b) Section 532(d) of title 11, United States Code, is amended—

(1) by striking out "shall" and inserting in lieu thereof "may",

(2) by striking out ", unless granting judgment would be clearly inequitable" and inserting in lieu thereof "if it finds that the proceeding was not brought by the creditor in good faith", and

(3) by redesignating such subsection as subsection (e).

(c) Section 523 of title II, United States Code, is amended by inserting after subsection (c) the following new subsection:

"(d) For purposes of subsection (a)(2) of this section, any debt which is incurred on or within ninety days before the date of filing a petition under this title, is presumed to be nondischargeable under such subsection."

SEC. 10. (a) Section 524(a) of title II, United States Code, is amended—

(1) in paragraph (2) by striking out "and" at the end thereof,

(2) in paragraph (3)—

(A) by striking out the period and inserting in lieu thereof "; and", and

(B) by striking out "523(d)" and inserting in lieu thereof "523(e)",

(3) by inserting after paragraph (3) the following new paragraph:

"(4) does not operate as an injunction against the enforcement of a lien that has not been avoided under the provisions of this title."

(b) Section 524(c) of title 11, United States Code, is amended—
(1) in paragraph (1) by inserting "and" at the end thereof,
(2) by striking out paragraphs (2), (3), and (4), and
(3) by adding at the end thereof the following new paragraph:
"(2) such agreement contains clear and conspicuous statement which advises the debtor that the agreement may be rescinded at any time prior to discharge or within 60 days after it is entered into, whichever occurs later, by giving a written notice of rescission to the creditor."
(c) Section 524(d) of title 11, United States Code, is amended to read as follows:
"(d) At the meeting of creditors provided by section 341(c) of this title, the court shall inform the debtor of the nature and effect of a discharge."
SEC. 11. Section 547(b) of title 11, United States Code, is amended—
(1) in paragraph (4) by—
(A) amending subparagraph (B) to read as follows:
"(B) between 90 days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider;", and
(B) by striking out "and" at the end thereof, (2) in paragraph (5) by deleting the period at the end of the paragraph and inserting in lieu therefore "; and", and
(2) in paragraph (5) by deleting the period at the end of the paragraph and inserting in lieu thereof "; and", and
(3) by adding at the end thereof the following new paragraph:
"(6) if such creditor at the time of such transfer had reasonable cause to believe the debtor was insolvent at the time of such transfer.".
SEC. 12. Section 544(c) of title 11, United States Code, is amended by striking out "section 521(1)" and inserting in lieu thereof "section 521(a)(1)".
SEC. 13. Section 722 of title 11, United States Code, is amended—
(1) by inserting "(a)" before "An", and
(2) by adding at the end thereof the following new subsection:
"(b) upon notice and hearing, the court may require a creditor to accept payments in redemption of the value of a claim secured by a nonpossessory, nonpurchase money security interest in tangible personal property, over a reasonable period not to exceed five years, if such tangible personal property is—
"(1) household furnishings, household goods, wearing apparel, appliances, books, animals, crops, musical instruments,

or jewelry that are held primarily for the personal, family, or household use of the debtor or a dependent of the debtor;

"(2) implements, professional books, or tools, of the trade of the debtor or the trade of a dependent of the debtor; or

"(3) professionally-prescribed health aids for the debtor or a dependent of the debtor."

SEC. 14. Section 1106(a)(2) of title 11, United States Code, is amended by striking out "section 521(1)" and inserting in lieu thereof "section 521(a)(1)".

SEC. 15. Section 1111 of title 11, United States Code, is amended by striking out "section 521(1)" and inserting in lieu thereof "section 521(a)(1)"

SEC. 16. (a) Section 1301(a) of title 11, United States Code, is amended—

(1) by inserting "and to the extent that" after "unless",

(2) by striking out "and (c)" and inserting in lieu thereof "and (d)",

(3) in paragraph (1) by striking out "or" at the end thereof,

(4) by redesignating paragraph (2) as paragraph (4), and

(5) by inserting after paragraph (1) the following new paragraphs:

"(2) as between the debtor and the individual protected under this subsection, such individual received the consideration for the claim held by such creditor;

"(3) the debtor has filed a plan pursuant to section 1321 of this title and such plan does not propose to pay the principal of and interest on such claim in full; or".

(b) Section 1301(c) of title 11, United States Code, is amended to read as follows:

"(d) on request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided by subsection (a) of this section with respect to a creditor for the reasons specified in paragraph (1), (2), (3), or (4) of subsection (a) of this section, or to the extent that such creditor's interest would be irreparably harmed by such a stay.".

(c) Section 1301 of title 11, United States Code, is amended by inserting after subsection (b) the following new subsection:

"(c) A creditor who proposes to act pursuant to subsection (a) shall notify the debtor and codebtor of such intention. The debtor or codebtor shall then have 10 days to file and serve a written objection to the taking of the proposed action. If the debtor or codebtor does not file and serve a timely written objection, then the creditor's action taken in accordance with its notice shall not violate subsection (a)".

SEC. 17. Section 1321 of title 11, United States Code, is amended—

(1) by inserting "(a)" before "The", and

(2) by adding at the end thereof the following new subsection:

"(b) Payments under the plan shall be commenced at the time of the filing of the plan. The payments shall be made to the trustee, and shall be retained by the trustee until a plan is confirmed or not confirmed. If any paln is confirmed, the trustee shall then distribute the funds in accordance with the plan. If no plan is confirmed, the funds shall be returned to the debtor after deducting the costs of administration".

SEC. 18. (a) Section 1322(a) is amended—

(1) in paragraph (2) by striking out "and" at the end thereof,

(2) by redesignating paragraph (3) as paragraph (4), and

(3) by inserting after paragraph (2) the following new paragraph:

"(3) provide for payment, in deferred cash payments, of the amount which could reasonably have been collected upon the claims specified in section 523(a) within the period of the plan as specified by subsection (c) of this section, as if this proceeding had not been brought; and".

(b) Section 1322(b) of title 11, United States Code, is amended by amending paragraph (1) and paragraph (2) to read as follows:

"(1) designate a class or classes of unsecured claims, as provided in section 1122 of this title, but may not discriminate unfairly against any class so designated but may treat claims which are specified in section 523(a) or involve a codebtor differently than other unsecured claims;

"(2) modify the rights of holders of secured claims, other than a claim fully secured by a security interest in real property that is the debtor's principal residence, or of holders of unsecured claims;".

(c) Section 1322(c) is amended to read as follows:

"(c) the plan may not provide for payments over a period of more than five years."

SEC. 19. Section 1325(a) of title 11, United States Code, is amended —

(1) in paragraph (3) by inserting ", and the plan represents a bona fide effort which is consistent with the debtor's ability to repay his debts, after providing support for himself and his dependents," before the semicolon,

(2) in paragraph (5)—

(A) by amending subparagraph (B) (ii) to read as follows:

"(ii) the value, as of the date of filing the plan, of property to be distributed under the plan is not less than the value determined under section 506(a) of this title and, if such value is to be paid in installments, interest is to be paid at the rate specified in the consumer's contract; or", and

(B) in subparagraph (C) by striking out "and",

(3) by redesignating paragraph (6) as paragraph (7), and

(4) by inserting after paragraph (5) the following new paragraph:

"(6) the plan extends for a period of five years or the plan provides for payments of at least 70 percent of all allowed unsecured claims; and".

SEC. 20. Section 1328(c)(2) of title 11, United States Code, is amended to read as follows:

"(2) of a kind specified in section 523(a) of this title to the extent such claims were not proposed to be paid as part of the plan.".

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