# CHAPTER 13 PLANS AND THE EFFECT OF CONFIRMATION

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## I. INTRODUCTION

Chapter 13 of Title 11 was enacted by Congress in order to provide an alternative to chapter 7. Chapter 13 offers two major incentives to encourage individuals to choose chapter 13. These incentives are allowing chapter 13 debtors to keep their assets upon filing for bankruptcy relief, and the "super discharge" available to chapter 13 debtors, which is much more liberal than in chapter 7.[1] To qualify for chapter 13, a debtor must "have regular income," which is broadly defined and includes social security payments, unemployment, and welfare benefits.[2] Under 11 U.S.C. §109(e), chapter 13 relief is only individuals that owe, on the date of filing, less than $307,675 in noncontingent, liquidated, unsecured debts and noncontingent, liquidated, secured debts amounting to less than $922,975.

After filing, the chapter 13 debtor must present to the Bankruptcy Court and all creditors and parties in interest a chapter 13 plan. The plan must satisfy various requirements. The plan must be proposed in good faith, and pay the unsecured creditors not less than as much as they would receive in a chapter 7 liquidation. The plan must commit all of the chapter 13 debtor's disposable income over the duration of the plan.[3]

While a chapter 13 plan may separately classify unsecured claims, the plan must not unfairly discriminate against any class.[4] It is up to the bankruptcy court to determine whether a proposed chapter 13 plan unfairly discriminates.

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[1] Seth J. Gerson, *Separate Classification of Student Loans in Chapter 13*, 73 Wash. U. L.Q. 269, 275 (Spring 1995).

[2] *Id*. (citing S. Rep. No. 989, 95th Cong., 2d Sess. 24, *reprinted in* 1978 U.S.C.C.A.N. 5787, 5810).

[3] 11 U.S.C. §1325(a) and (b).

[4] 11 U.S.C. §1322(b)(1).

If a chapter 13 plan is confirmed, the confirmation order is a binding determination of the rights and liabilities of the various interested parties. Typically, confirmation has a *res judicata* effect. The binding effect of the confirmation order normally extends to all issues that were or could have been determined at the confirmation hearing. Creditors should review plans prior to the deadline to object to confirmation, in order to determine whether they are being unfairly treated under the proposed plan. If so, they should object. An objection to confirmation initiates a contested matter. If an objection is not filed, and a plan is confirmed, the plan may be binding, even if it discriminates unfairly.

## II. SEPARATE CLASSIFICATION AND UNFAIR DISCRIMINATION IN A CHAPTER 13 PLAN FOR CO-SIGNED DEBTS

### (A) SEPARATE CLASSIFICATION

The original version of 11 U.S.C. §1322(b)(1) provided in part, that a chapter 13 plan may "designate a class or classes of unsecured claims, . . . but may not discriminate unfairly against any class so designated." Congress amended this section in 1984, by adding "however, such plan may treat claims for a consumer debt of the debtor if an individual is liable on such consumer debt with the debtor differently than other unsecured claims." Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub.L. No. 98-353, 98 Stat. 333 (1984). Prior the amendment, courts routinely disallowed chapter 13 debtors from separately classifying co-signed debt in chapter 13 plans under section 1322(b)(1).[5]

Section 1322(b)(1) states:

> [s]ubject to subsections (a) and (c) of this section, the plan may—
> (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, however, such plan may treat claims for a consumer debt of

[5] *In re Ramirez*, 204 F.3d 595, 599 (5th Cir. 2000), Benavides, J., specially concurring (citing *In re Montano*, 4 B.R. 535 (Bankr. D.D.C. 1980); *In re Utter*, 3 B.R. 369 (Bankr. W.D.N.Y. 1980)).

> the debtor if an individual is liable on such consumer debt with the debtor differently than other unsecured claims...."[6]

Despite what appears to be the plain language of the statute, courts are split as to whether this subsection allows chapter 13 plans to treat co-signed debt differently and whether such treatment is subject to the unfair discrimination test. The majority of courts however, have permitted chapter 13 debtors to separately classify co-signed debt, but only if such treatment does not unfairly discriminate against other general unsecured creditors. Specifically, courts are split as to "whether the 'however' clause is a carve-out from the unfair discrimination test."[7] Most courts recognize that section 1322(b)(1) is awkwardly stated.[8] Based on the statute's phrasing, courts must look at the language and construction for guidance and if this does not help, then courts should look at the legislative history to determine Congress's intent regarding this section.[9]

When dealing with the meaning of statutory language and construction, courts first look to the literal meaning of the words used by Congress.[10] "It is well established 'that a statute must, if possible, be construed in such fashion that every word has some operative effect.'"[11] By definition, however is the equivalent of "but" or "on the other hand."[12] While some courts hold

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[6] Section 1322(b)(1).

[7] *In re Battista*, 180 B.R. 355, 357 (Bankr. D.N.H. 1995).

[8] *In re Cheak*, 171 B.R. 55, 57 (Bankr. S.D. Ill. 1994); *Battista*, 180 B.R. at 357 (citing *In re Easley*, 72 B.R. 948, 956 (Bankr. M.D. Tenn. 1987).

[9] *Ramirez*, 204 F.3d at 598 (Circuit Judge Benavides, specially concurring).

[10] *Id.* at 598-99 (5th Cir. 2000) (citing *Flora v. United States*, 357 U.S. 63, 65 (1958)). *United States v. Ron Pair Enterprises, Inc*., 489 U.S. 235, 242 (1989).

[11] *Ramirez*, 204 F.3d at 599 (Circuit Judge Benavides, specially concurring) (quoting *United States v. Nordic Village, Inc*., 503 U.S. 30 (1992)).

[12] *Ramirez*, 204 F.3d at 599 (Circuit Judge Benavides, specially concurring) (quoting Webster's Third International Dictionary 1097 (1981)).

that amended section 1322(b)(1) discussing co-signed consumer debt was to expressly allow separate classification of such debt, it would appear that if this was Congress's intent, Congress would not have started the provision with "however."[13] "However" typically is used in a sentence as a way to contrast one phrase from the phrase before it.[14] As Judge Benavides points out in Ramirez, if Congress had intended that co-signed debts to receive identical treatment as other unsecured debts, including both being subject to the unfair discrimination test, then there would have been no reason for Congress to "separately address the manner in which co-signed debts are treated."[15]

The legislative history of section 1322(b)(1), provides guidance on why Congress amended the section. According to the legislative record:

> [a]lthough there may be no theoretical differences between co-debtor claims and others there are important practical differences that must be recognized. Because codebtors are often relatives or friends, the debtor may feel a great need to pay the debt in full, even if that is not permitted within the Chapter 13 plan. If the debtor can be required to devote all disposable income to the plan, the conflicting desire to voluntarily make payments outside the plan on a co-signed debt may spell failure for the plan by leaving insufficient income to keep up plan payments, If, as a practical matter, the debtor is going to pay the codebtor claim, he should be permitted to separately classify it in Chapter 13.[16]

A majority of courts have interpreted the "however" clause in section 1322(b)(1) and the section's legislative history as permitting chapter 13 debtors to separately classify co-signed

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[13] *Ramirez*, 204 F.3d at 599.

[14] *Id*.

[15] *Id*.

[16] *In re Dornon*, 103 B.R. 61, 61 (Bankr. N.D.N.Y. 1989) (quoting **5 COLLIER ON BANKRUPTCY**, ¶ 1322.05 at 1322-9 to 1322-10 (15th ed. 1989) (citing S. REP. No. 65, 98th Cong., 1st Sess., 17-18 (1983) [S. 445]).

debt, but that the "unfair discrimination test" must still be applied to such classification.[17] Under most circumstances, this is the most sensible result.

### (B) UNFAIR DISCRIMINATION

The unfair discrimination test is a four factor test applied by courts to determine whether a chapter 13 plan unfairly discriminates against a class of creditors.[18] The debtor has the burden of proof here. The four factors of the unfair discrimination test are:

(1) whether there is a reasonable basis for the discrimination or separate classification;

(2) whether the debtor can carry out the plan without the discrimination;

(3) whether such discrimination is proposed in good faith;

(4) the treatment of the class discriminated against.[19]

In order for the separate classification of co-signed debt provided for in a chapter 13 plan to be approved, the debtor must show that the separate classification does not in fact unfairly discriminate against other classes of creditors, including other unsecured creditors.[20]

A minority of courts disagree with applying the unfair discrimination test to the separate classification of co-signed debts in a chapter 13 plan. For example, in the Eleventh Circuit, the bankruptcy courts for both the Northern and Southern Districts of Georgia have held that the unfair discrimination test should not be applied when a chapter 13 debtor has proposed separate

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[17] *See, e.g., In re Chacon*, 202 F.3d 725 (5th Cir. 1999); *In re McNichols*, 249 B.R. 160, 176 (Bankr. N.D. Ill. 2000); *In re McNichols*, 255 B.R. 857 (Bankr. N.D. Ill. 2000); *Easley*, 72 B.R. 948 (concluding that cosigned consumer debt is subject to the unfair discrimination test).

[18] *See, e.g., In re Bradley*, 109 B.R. 182 (Bankr. E.D. Va. 1990); *In re Perkins*, 55 B.R. 422, 425-26 (Bankr. Okla. 1985); *Cheak*, 171 B.R. at 58.

[19] *Bradley*, 109 B.R. at 183.

[20] *See, e.g., In re Lewman*, 157 B.R. 134, 136-37 (Bankr. S.D. Ind. 1992) (concluding that chapter 13 debtors proposing separate classification for co-signed debt bear the burden of establishing that the separate classification and treatment of unsecured claims does not unfairly discriminate.); *Battista*, 180 B.R. at 357 (holding that "the unfair discrimination standard applies to plans that separately classify co-signed consumer debts.")

classification for co-signed debts in his chapter 13 plan.[21] These courts have held that the "however" clause contained in section 1322(b)(1) acts as a carve-out to the unfair discrimination standard typically applied to separate classification schemes in a chapter 13 plan. These courts conclude that the language of section 1322(b)(1) provides an exception to the unfair discrimination rule. The Bankruptcy Court for the Southern District of Georgia stated "since section 1322(b)(1) was amended to include the language regarding co-signed debts, the 'unfair discrimination' test has lost its significance in dealing with the issue of the special classification of co-signed debts."[22] Therefore, provisions providing for separate classification of co-signed debt are excepted from the unfair discrimination rule.[23]

## III. SEPARATE CLASSIFICATION OF STUDENT LOAN DEBTS IN A CHAPTER 13 PLAN

11 U.S.C. §1322(a) requires equal treatment for each claim or interest within a particular class in a chapter 13 plan. Specifically, section 1322(a)(3) provides that if a plan classifies claims, the plan must also provide the same treatment for each claim within a particular class. Section 1322(b)(1) in turn provides that a chapter 13 plan may designate a class or classes of unsecured claims, but may not discriminate unfairly against any class that is so designated.

Bankruptcy courts are split as to whether a chapter 13 plan may classify differently and provide for disparate treatment of unsecured debts. Some bankruptcy courts have narrowly read section 1322(b)(1), holding that chapter 13 plans may only designate those classes of unsecured

[21] *See, e.g., In re Monroe*, 281 B.R. 398 (Bankr. N.D. Ga. 2002); *In re Thompson*, 191 B.R. 967 (Bankr. S.D. Ga. 1996).

[22] *Monroe*, 281 B.R. at 399 (quoting *Thompson*, 191 B.R. 967).

[23] *Dornon*, 103 B.R. at 64.

claims expressly created or considered by the Bankruptcy Code.[24] Other courts have interpreted the statute more broadly, allowing for chapter 13 plans to provide separate classification and treatment for unsecured debt.[25] Finally, other courts have held that chapter 13 plans may provide for separate classification and treatment of unsecured debt, as long as this does not "unfairly discriminate."[26]

In *Leser*, the Eighth Circuit Court of Appeals laid out a four part test to determine whether a plan that separately classifies and unequally treats like claims discriminates unfairly.[27] The four factors to look at in determining whether a plan unfairly discriminates are: (1) whether the discrimination has a reasonable basis; (2) whether the plan can be carried out without the discrimination; (3) whether the discrimination is proposed in good faith; and (4) whether the degree of discrimination is directly related to the basis for the discrimination.[28] Other courts do not apply the four part test, but simply inquire as to whether the proposed classification demonstrates "legitimate interests of the debtor."[29] Other courts ask whether the discrimination is necessary for the plan to succeed.[30]

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[24] *See, e.g., In re Smalberger*, 157 B.R. 472 (Bankr. D. Ore. 1992); *In re Chapman*, 146 B.R. 411 (Bankr. N.D. Ill. 1992).

[25] *See, e.g., In re Brown*, 151 B.R. 232 (Bankr. N.D. Ill. 1993); *In re Dodds*, 140 B.R. 542 (Bankr. D. Mont. 1992); *In re Freshley*, 69 B.R. 96 (Bankr. N.D. Ga. 1987).

[26] *See, e.g., In re Leser*, 939 F.2d 669 (8th Cir. 1991).

[27] *Id*. at 672. This test is also referred to as the *Kovich, Hosler, Wolff, Dziedzic, Storberg*, or *Husted* test. *See* Stephen L. Sepinuck, Rethinking Unfair Discrimination in Chapter 13, 74 Am. Bankr. L.J. 341, 354 (Fall 2000). The author has chosen to call the test the *Leser* test in these materials because in cases it seems to be often referred to as this. Regarding this test, one commentator has noted, "[d]espite having embraced it, courts and commentators have leveled almost nonstop criticism of this approach, not to mention making numerous slight alterations to it. It is doubtful any other legal standard has been so frequently criticized by the same authorities that adopt it." *Id*. at 355-56.

[28] *Leser*, 939 F.2d at 672; *see also In re Cronk*, 131 B.R. 710, 712 (Bankr. N.D. Ga. 1990).

[29] *Brown*, 152 B.R. at 327-28; *see also Boggan*, 125 B.R. 533.

[30] *James v. Moore (In re James)*, 150 B.R. 479, 485 (Bankr. M.D. Ga. 1993).

Of particular concern for bankruptcy courts is whether chapter 13 plans that propose separately to classify student loan obligations[31] from other unsecured debt should be confirmed. While numerous courts have addressed this issue, there is no agreement among the courts regarding whether such provisions are permissible. When a chapter 13 plan provision is objected to on the basis of unfair discrimination, the chapter 13 debtor bears the burden of proving that the classification does not discriminate unfairly in contravention to section 1322(b).[32]

Bankruptcy courts do not automatically strike down chapter 13 plans that contain a provision that calls for disparate treatment of non-dischargeable student loan debt. Rather, the courts review the provision, along with the rest of the chapter 13 plan, to see whether such treatment is fair, in light of how other unsecured debt is treated and generally based upon the totality of the circumstances. In making this fact specific determination, bankruptcy courts employ a number of tests, including the above cited test laid out in *Leser*. Other courts employ a balancing test, which involves the balancing of the benefits and detriments allocated to the debtor and creditors from the proposed classification and treatment.[33] Finally, other courts employ the "base-line test" laid out by the First Circuit Bankruptcy Appellate Panel in *In re Bentley*.[34] Pursuant to the base-line test, bankruptcy courts look to four guiding principles of chapter 13 for what is the norm, from which departures can be assessed for fairness.[35] The four factors considered include: (1) equality of distribution; (2) non-priority of student loans; (3) mandatory versus optional

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[31] Pursuant to 11 U.S.C. §523(a)(8), student loan obligations are non-dischargeable, meaning that a chapter 13 debtor may not typically discharge this type of debt, but instead must continue to pay it off.

[32] *In re Groves*, 39 F.3d 212, 214 (8th Cir. 1994).

[33] *See, e.g., In re Colfer*, 159 B.R. 602 (Bankr. D. Me. 1993).

[34] 266 B.R. 229 (1st Cir. BAP 2001); *In re Crawford*, 324 F.3d 539, 542 (7th Cir. 2003).

[35] *Bentley,* 266 B.R. at 240.

contributions; and (4) the debtor's fresh start.[36] If, under the base-line approach, the disparate treatment offers each class benefits and burdens that are the same as those it would receive at the baseline, then the proposed discrimination is fair. If the proposed discrimination alters the allocation of benefits and burdens to the detriment of one class (*i.e.*, the unsecured creditors), the proposed discrimination is unfair and not allowed.[37]

Typically, if a chapter 13 plan proposes to pay the non-dischargeable student loan debt in full, but calls for a lower percentage payment on the debtor's remaining unsecured debt, such plan will not be confirmed.[38] Recently, three different bankruptcy courts have considered whether chapter 13 plans proposing to pay non-dischargeable student loan debt in full, while only making minimal payments towards the remaining unsecured obligations of the debtors, should be confirmed. Each one held that the plans could not be confirmed.[39]

In *Simmons*, the Bankruptcy Court for the Northern District of Texas, Fort Worth Division, considered whether various chapter 13 plans, all of which proposed to pay student loan obligations in full, while only making meager payments to dischargeable general unsecured obligations, should be confirmed. The Court framed the issue before it as whether "section 1322(b)(1) prohibits a chapter 13 debtor from treating nondischargeable unsecured student loan obligations more favorably than dischargeable general unsecured debt?"[40] In order to answer

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[36] *Id*. at 240-42.

[37] *Id*. at 240.

[38] *See, e.g., In re Mason*, 300 B.R. 379 (Bankr. D. Kan. 2003); *In re Simmons*, 288 B.R. 737 (Bankr. N.D. Tx. 2003); *In re Belda*, 315 B.R. 477 (N.D. Ill. 2004).

[39] *See In re Mason*, 300 B.R. 379; *In re Simmons*, 288 B.R. 737; *In re Belda*, 315 B.R. 477.

[40] *Simmons*, 288 B.R. at 744.

this question, the Court explained that the meaning of unfair discrimination must be explored.[41] The Court noted that when dealing with unfair discrimination, the focus is upon the class discriminated against.[42] The test to determine if there is unfair discrimination must be applied among equal classes.[43] However, the Court stressed that "necessarily inherent in the term 'unfair discrimination' is the notion that there may be 'fair' discrimination in the treatment of classes of creditors."[44] For example, different treatment of equal classes that results in equal return for the classes would be an acceptable type of discrimination.[45]

After concluding that certain discrimination in the treatment of equal classes may be fair in certain circumstances, the Court then considered whether Congress had demonstrated an intent to allow discrimination on the part of a chapter 13 debtor in favor of student loan creditors in a plan.[46] The Court concluded Congress did not, and next considered whether disparate treatment of equal classes could ever be fair, and thus permissible.

The Court noted that some bankruptcy courts have held that disparate treatment of equal classes could be fair.[47] Courts holding that disparate treatment of equal classes may be fair have applied the tests discussed earlier, including the four factor test applied in *Leser*.

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[41] *Id*. at 747-48.

[42] *Id*. at 747.

[43] *Id*. (concluding that "'unfair discrimination' provides a horizontal requirement of fairness.")

[44] *Simmons*, 288 B.R. at 747-48.

[45] *Id*. at 748.

[46] *Id*. Other bankruptcy courts have concluded that Congress did intend to allow chapter 13 debtors to discriminate in favor of non-dischargeable debts, such as student loans, in chapter 13 plans. *See, e.g., In re Labib-Kiyarash*, 271 B.R. 189 (9th Cir. BAP 2001); *In re Williams*, 253 B.R. 220, 227-28 (Bankr. W.D. Tenn. 2000).

[47] *See, e.g., Thompson*, 191 B.R. at, 971; *Ramirez*, 204 F.3d at 598 (Circuit Judge Benavides, specially concurring.

A few courts applying the four factor test have modified the fourth factor, looking instead at the proposed treatment of the class discriminated against.[48] Other courts consider whether the class discriminated against will receive any meaningful payment by the chapter 13 debtor.[49]

The *Simmons* Court discussed another test applied by some bankruptcy courts in determining whether disparate treatment of equal classes can be fair. This test considers whether there is a legitimate reason for such discrimination and whether the proposed discrimination favors the class benefiting from the discrimination.[50] The *Simmons* Court adopted this test, concluding that "for discrimination to be fair, the amount to be received by the class discriminated against must not be less than the class would have been entitled to receive had there been no discrimination among classes."[51] The Court noted that a chapter 13 debtor who separately classifies student loans from other unsecured debt has a legitimate purpose in such discrimination.[52] The problem facing the chapter 13 debtor, however, is whether the second element has been met. The *Simmons* Court concluded that the debtor's chapter 13 plan must provide the class discriminated against the amount of payments that at least equal what the class would have received if there were no discrimination and thirty-six months of the debtor's disposable income were applied to make payments under the plan.[53] The practical answer to this is to perform a calculation to determine what unsecured creditors would receive under a 36 month plan (assuming such a plan

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[48] *See, e.g., In re Martin*, 189 B.R. 619, 627 (Bankr. E.D. Va. 1995).

[49] *See, e.g., In re Strausser*, 206 B.R. 58, 60 (Bankr. W.D.N.Y. 1997).

[50] *Simmons*, 288 B.R. at 751. *See also Brown*, 152 B.R. at 327-28; *In re Boggan*, 125 B.R. 533.

[51] *Simmons*, 288 B.R. at 751.

[52] *Id*. at 752.

[53] *Id*. at 753. The Court explained, "[p]ut another way, having calculated three years of the debtor's disposable income, the total of senior debt (secured and priority) to be paid under the plan should be deducted. The balance must be shared pro rata among student loan and other creditors. To the extent of payments to be made under the plan in excess of three years' disposable income, the student loan claim may be preferred." *Id*. at n. 55.

would be confirmable) and "stretch" the plan to provide the same distribution over the life of the plan. This, of course, ignores the time value of money.

Another recent case, *In re Mason*[54], also considered whether disparate treatment between equal classes can ever be fair, and therefore permissible, where the proposed discrimination involved separate classification and treatment of non-dischargeable student loan debt. The chapter 13 debtors in *Mason* proposed in their amended plan to classify separately nondischargeable unsecured student loan debt in the amount of approximately $31,000 and partially to pay this debt ahead of other general unsecured debt.[55] The chapter 13 trustee objected, arguing that the proposed plan unfairly discriminated against general unsecured creditors in violation of §1322(b)(1).[56] The Bankruptcy Court for the District of Kansas applied all of the tests previously discussed, including the four part test, the balancing test, and the baseline test. The *Mason* Court held that the chapter 13 plan failed the *Leser* test because the proposed discrimination failed the first part of the test, regardless of whether the discrimination had a reasonable basis.[57] According to *Mason*, the fact that student loans are non-dischargeable is not sufficient basis for the proposed discrimination.[58] Next, the Court applied the balancing test, weighing the benefits and detriments to the debtors, the student loan creditors and the general unsecured creditors.[59] Applying the balancing test, the *Mason* Court concluded that the "debtors' burden for the nondischargeable student loan debt has been unfairly shifted to the

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[54] 300 B.R. 379 (Bankr. D. Kan. 2003).

[55] *Mason*, 300 B.R. at 381.

[56] *Id*.

[57] *Id*. at 385.

[58] *Id*.

unsecured creditors and that the treatment afforded the student loan creditors discriminated unfairly against the unsecured creditors.[60] Finally, the *Mason* Court applied the baseline test. When applying the baseline test courts consider: (1) equality of distribution; (2) nonprioirty of student loans; (3) mandatory vs. optional contributions; and (4) the debtor's fresh start.[61] When considering these factors, the *Mason* Court concluded that the debtors' proposed disparate treatment could not be approved, primarily because the general unsecured creditors would receive nothing during the life of the chapter 13 plan, while the student loan creditors would receive all of the distribution.[62] After applying each test, the *Mason* Court noted that the baseline test "is most loyal to the objective goals and motivations of chapter 13 and the Bankruptcy Code."[63] In the Court's opinion, it is the most objective test and "fairly easy to implement."[64]

The latest case discussing whether disparate treatment involving student loan debt and other unsecured debt in a chapter 13 plan should be approved is *In re Belda*[65]. In *Belda*, the chapter 13 debtor proposed to continue with his monthly payments towards his student loan in the amount of $68.50 per month, which while not paying the loan in full during the life of the plan, would result in the student loan creditor recovering 62% of its loan during the life of the plan.[66] The debtor's other unsecured creditors, on the other hand, would receive only 10% of the amounts

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[59] *Id*. at 386.

[60] *Mason*, 300 B.R. at 386.

[61] *Id*. at 384 (citations omitted).

[62] *Id*. at 386.

[63] Id. at 387.

[64] *Id*.

[65] 315 B.R. 477 (N.D. Ill. 2004).

[66] *Id*. at 478.

owed to them over the life of the plan.[67] The chapter 13 trustee objected to confirmation of the debtor's plan, arguing that the proposed treatment violated section 1322(b)(1)'s prohibition against unfair discrimination.[68] The Bankruptcy Court for the Northern District of Illinois, Eastern Division disagreed and confirmed the plan, and the trustee appealed.[69]

The District Court for the Northern District of Illinois reversed the bankruptcy court's decision, concluding that the proposed treatment and classification violated section 1322(b)(1)'s provision prohibiting unfair discrimination. In so holding, the District Court joined the majority of courts in concluding that student loan debt is subject to the limitations of section 1322(b)(1)'s provision regarding unfair discrimination.[70] The District Court found the reasoning by the Bankruptcy Court for the Southern District of Illinois in the *Coonce* decision persuasive in its conclusion that "student loans constituting long-term debt under § 1322(b)(5) must comply with § 1322(b)(1)'s prohibition against unfair discrimination."[71]

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[67] *Id*.

[68] *Id*. The Bankruptcy Court reasoned that the discrimination was not unfair because "'[i]f Debtor does not maintain his current monthly payments owed to the Department of Education he will be liable upon completion of his Chapter 13 plan for a substantial lump sum of past due payments. The lender would be free to initiate collection proceedings, thereby eliminating in large part the fresh start to which the debtor is entitled in bankruptcy.'" *Id*. at 486 (citing Tr. at 10).

[69] *Belda*, 315 B.R. at 486.

[70] *Id*. at 486. *See, e.g., In re Coonce*, 213 B.R. 344 (Bankr. S.D. Ill. 1997); *In re Kolbe*, 199 B.R. 569 (Bankr. D. Md. 1996); *In re Colley*, 260 B.R. 532 (Bankr. M.D. Fla. 2000). A minority of courts, on the other hand have concluded that student loans are exempted from the limitations of section 1322(b)(1). *See, e.g., In re Benner*, 156 B.R. 631 (Bankr. D. Minn. 1993); *In re Cox*, 186 B.R. 744 (Bankr. N.D. Fla. 1995).

[71] *Belda*, 315 B.R. at 486. In *Coonce*, the Bankruptcy Court considered whether the remaining length of the student loan debt should provide the basis for separate classification. The *Coonce* Court stated that separate classification of student loans based solely on their duration could produce "anomalous results." *Coonce*, 213 B.R. at 348. By concluding that the *Coonce* reasoning was persuasive, it can be deduced that the Bankruptcy Court for the Southern District of Illinois agrees that the remaining length of student loan debt should not provide the justification for separate classification of nondischargeable student loan debt.

Reviewing the case law regarding whether a chapter 13 plan may separately classify and treat differently student loan debt from other unsecured debt reveals a split between the bankruptcy courts whether such disparate treatment is: (1) ever allowed; (2) allowed only if such treatment is proven not in contravention of section 1322(b)(1); or (3) allowed in almost all circumstances without consideration to section 1322(b)(1)'s provision regarding unfair discrimination. Bankruptcy courts determine whether such treatment is permissible on a case by case basis applying one of several tests discussed above. The test that is applied could determine the outcome of whether such disparate treatment will be approved, and therefore whether a plan containing such treatment will be confirmed.

Some courts, such as the Bankruptcy Court for the District of Minnesota, have confirmed chapter 13 plans that treat student loan debt as long-term debt similar to a home mortgage.[72] By treating student loans in this manner, separate classification may be appropriate. In *Benner*, the chapter 13 debtor's student loan balance was paid outside of the plan, but the arrearages on the loan were cured within the plan.[73] By treating student loan debt as long-term debt, a chapter 13 debtor may be allowed to separately classify the student loan debt and not be guilty of unfairly discriminating in favor of such debt. Careful analysis of the underlying obligation, and its term, may help the practitioner on this point.

[72] *Benner*, 156 B.R. 631. In *Benner*, the Bankruptcy Court applied the *Leser* test to determine whether the proposed separate classification of the student loan debt was appropriate. *Id*. at 634. Typically, section 1322(b)(5) is used by chapter 13 debtors to maintain mortgage payments or other long-term secured debt while curing the arrearages under the plan. However, by its express terms section 1322(b)(5) also applies to long-term unsecured debt. Pursuant to 11 U.S.C. § 1322(b)(5), a plan may provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due.

[73] *Id*. at 633.

## IV. EFFECT OF CONFIRMATION OF CHAPTER 13 PLANS THAT PROVIDE FOR DISCHARGE OF STUDENT LOAN OBLIGATIONS OR LIMIT THE ACCRUAL OF POST-PETITION INTEREST ON NONDISCHARGEABLE DEBTS

### (A) DISCHARGE OF STUDENT LOAN OBLIGATIONS

Recently, there have been a number of chapter 13 plans filed that provide either for a discharge of student loan debt or limit the accrual of post-petition interest on such debt.[74] Depending on where the plan is filed, such provisions may be enforceable or sanctionable, an important distinction.

In the 9th and 10th circuits, such provisions are valid and enforceable, as long as the right language is used. For example, in *Anderson*[75], the Court of Appeals for the 10th Circuit held that an order confirming a chapter 13 plan providing that the debtor's student loan debt would be discharged was *res judicata*, when the plan contained language declaring that if the debtor were forced to pay such debt, it would impose an undue hardship on the debtor.[76] In *Anderson*, the student loan creditor file an untimely objection to the plan, which was denied, and after the plan was confirmed, such creditor failed to appeal the confirmation order.[77] In addition, despite adequate notice, the student loan creditor failed to challenge such provision until after the debtor

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[74] Such a provision is typically called a "discharge by declaration" provision. *In re Ruehle*, 307 B.R. 28, 31 (6th Cir. BAP 2004).

[75] 179 F.3d 1253 (10th Cir. 1999).

[76] *Id*. at 1259-60. The debtor's plan provided "[p]ursuant to 11 U.S.C. §523(a)(8), excepting the aforementioned education loans from discharge will impose an undue hardship on the debtor and the debtor's dependents. Confirmation of debtor's plan shall constitute a finding to that effect and that said debt is dischargeable." *Id*. at 1254.

[77] *Id*.

completed the chapter 13 plan payments and received her discharge.[78] Following the debtor's discharge, the student loan creditor initiated collection proceedings on the debt and informed the debtor of the same.[79] The debtor reopened her case for the purpose of filing a complaint to determine dischargeability of the student loan debt.[80]

The Court of Appeals for the Tenth Circuit began its analysis of whether the confirmation order constituted a binding judicial determination of undue hardship, by noting that there is a general exception to discharge of student loan debt pursuant to 11 U.S.C. §523(a)(8) which is applicable in chapter 13 cases through 11 U.S.C. §1328(a)(2).[81] However, if the debtor is able to establish that excepting such debt from discharge would impose an undue hardship on the debtor and the debtor's dependents, then the debt may be discharged. Typically, a debtor establishes undue hardship by bringing an adversary proceeding on that issue, presenting evidence and creating a record.[82] However, in *Anderson*, rather than bringing an adversary proceeding, the debtor simply put language in her plan that stated that the debt, if excepted from discharge, would create an undue burden on her and her dependents. The Bankruptcy Court confirmed the plan and the Court of Appeals concluded that the confirmation order constituted a binding adjudication regarding hardship. In the Court's opinion, the creditor bore some burden to take an active role in protecting its interest, which it failed to do here.[83] The Court explained, "[w]hile Anderson did not properly prove undue hardship pursuant to the requirements of the Code, we

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[78] *Anderson*, 179 F.3d at 1254.

[79] *Id*. at 1255.

[80] *Id*.

[81] *Id*. at 1256.

[82] *Id*. (citing *Buford v. Higher Education Assistance Foundation*, 85 B.R. 579, 581-82 (D. Kan. 1988).

[83] *Anderson*, 179 F.3d at 1256.

agree with the Third Circuit that, "*after* the plan is confirmed the policy favoring the finality of confirmation is stronger than the bankruptcy court's and the trustee's obligations to verify a plan's compliance with the Code."[84] The Court reasoned "although the provision at issue did not comply with the Code, it is now too late for [the creditor] to make the argument that [the creditor] failed to timely raise."[85] It was a little too little and a little too late for the creditor.

Other courts have approached the issue in a different fashion. For example, the Bankruptcy Court for the Western District of Oklahoma, when faced with a debtors' attorney who repeatedly put such provisions in chapter 13 plans, considered whether such an attorney should be sanctioned for such action.[86] The Bankruptcy Court held that if attorneys intentionally include such discharge language in proposed chapter 13 plans in the hope that creditors will fail to object and be bound by confirmation, those attorneys violate their ethical duties as officers to the court and should be subject to Rule 9011 sanctions.[87] In *Hensley*, the Court noted that *Anderson* was not persuasive because it could be distinguished on the facts. In *Hensley*, the debtors had not completed their plan payments or received a discharge; and the confirmation orders in question had only recently been entered.[88] Because the confirmation orders were final and non-appealable, the student loan creditors brought motions to dismiss each of the chapter 13 cases of the debtors in question. The *Hensley* Court read "*Anderson* as applying to a different factual

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[84] *Id*. at 1258 (citing *In re Szostek*, 886 F.2d 1405, 1406 (3d Cir. 1989) (emphasis added). The Court reasoned that the majority view was that upon confirmation of a plan, courts will enforce "'offending plan provisions even though acknowledging that a provision may be contrary to the Code.'" *Anderson*, 179 F.3d at 1258 (quoting *In re Mammel*, 221 B.R. 238, 240 (Bankr. N.D. Iowa 1998).

[85] *Anderson*, 179 F.3d at 1259.

[86] *In re Hensley*, 249 B.R. 318 (Bankr. W.D. Ok. 2000). *See, e.g., In re Evans*, 242 B.R. 407, 411-13 (Bankr. S.D. Ohio 1999).

[87] *Hensley*, 249 B.R. at 323-24.

[88] *Id*. at 323.

situation in which the creditor simply waited too long to attempt to correct the obvious error committed by the bankruptcy court in confirming the plan containing the offending language."[89] In the *Hensley* Court's opinion, a discharge of a student loan debt in a chapter 13 could only be obtained by bringing an adversary proceeding to determine dischargeability.[90] Finally, the Court held that if debtors' attorneys continued to place such provisions in proposed chapter 13 plans, the attorneys faced having sanctions issued against them.

In September 2004, the Court of Appeals for the Tenth Circuit again revisited the issue of whether a student loan debt could be discharged in a chapter 13 plan in *In re Poland*.[91] In *Poland*, the Court of Appeals explained its determination in *Anderson* and reaffirmed its holding, ruling that where a confirmed chapter 13 plan contains a provision discharging a student loan debt, and contains language that discloses that excepting the debt from discharge would impose an undue hardship on the debtor and the debtor's dependents, such confirmation would be upheld.[92] In *Poland*, the debtor's plan contained language attempting to discharge student loan debt, but failed to contain any language discussing undue hardship.[93] In addition, the confirmation order made no mention of a finding of undue hardship should the student loan debt be excepted from discharge.[94] Because neither the plan nor the order contained any language

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[89] *Id*. at 322.

[90] *Id*.

[91] 382 F.3d 1185 (10th Cir. 2004).

[92] *Id*. at 1188. "*Anderson* rests on the fact that the confirmation of the plan, to which there was no objection, amounted to a binding adjudication of undue hardship thereby turning a nondischargeable debt into a dischargeable debt." *Id*. (citing *Anderson*, 179 F.3d at 1260).

[93] 382 F.3d at 1188.

[94] *Id*. at 1189.

referring to undue hardship, the student loan debt could not be discharged.[95] Note the important factual distinction.

In *Ruehle*, the Bankruptcy Appellate Panel for the 6th Circuit considered whether a discharge by declaration provision in a chapter 13 plan was enforceable.[96] The plan had been confirmed. The Court started its analysis by setting out the general rule, that normally, upon confirmation, the terms of the plan are binding on both the debtor and the creditor(s).[97] Fed. R. Civ. P. 60(b), however, provides courts with the power to relieve a party from an order under certain circumstances, including when a judgment is void.[98] A "judgment is void if the court lacked jurisdiction over the affected party because of a lack of notice resulting in violation of due process and it would be 'per se abuse of discretion to deny the movant's motion to vacate.'"[99] The Court reasoned that although the debtor's plan contained a provision discharging the student loan debt, such provision could not be considered appropriate notice to the student loan creditor that its rights were being affected.[100] Therefore, the creditor did not have proper notice, there was a denial of the creditor's due process rights, and as such the confirmation order entered was void. Because it was void, the confirmation order was unenforceable and the debt in question was not discharged.[101] The confirmation order was not considered *res judicata* and the student loan creditor was not barred from collecting on the debt.[102]

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[95] 307 B.R. at 33.

[96] *Id*. at 33.

[97] 11 U.S.C. §1327(a).

[98] *Ruehle*, 307 B.R. at 33. Motions under Fed. R. Civ. P. may be made within a reasonable time.

[99] *Id*. (citing *Eglinton v. Loyer (In re G.A.D., Inc.)*, 340 F.3d 331, 335-36 (6th Cir. 2003)).

[100] *Ruehle*, 307 B.R. at 34.

[101] *Id*.

[102] *Id*.

### (B) LIMITING THE ACCRUAL OF POST-PETITION INTEREST ON NONDISCHARGEABLE DEBTS

In addition to containing "discharge by declaration" provisions regarding student loan debts, chapter 13 plans may also contain provisions attempting to limit the amount of postpetition interest that has accrued on student loans during the pendency of the chapter 13 bankruptcy proceedings. Courts are split as to whether such provisions are enforceable and binding.

In *In re Pardee*[103], the chapter 13 debtors filed a plan that provided for a discharge of post-petition interest on a student loan debt.[104] The student loan creditor, Great Lakes Higher Education Corporation ("Great Lakes") failed to object, the plan was confirmed, and Great Lakes did not appeal the confirmation order.[105] After the debtors received their discharge, Great Lakes attempted to collect the postpetition interest on the student loan in the amount of $6,095.92. The debtors filed a motion in the Bankruptcy Court to enforce the discharge of interest and enjoin Great Lakes from attempting to collect the postpetition interest.[106] The Bankruptcy Court granted the motion, and the Bankruptcy Appellate Panel ("BAP") for the Ninth Circuit affirmed.[107] The Court of Appeals for the Ninth Circuit affirmed the lower court opinions, holding that although the chapter 13 plan contained an otherwise inappropriate provision cutting

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[103] 193 F.3d 1083 (9th Cir. 1999).

[104] *Id*. at 1084.

[105] *Id*.

[106] *Id*. Note that injunctive relief is typically obtained by adversary proceeding, governed by Bankruptcy Rule 7001.

[107] *Id*. The BAP held that the confirmed chapter 13 plan was *res judicata* as to the discharge provision and the failure of Great Lakes to either object to the plan or appeal the order "constituted a waiver of its ability to challenge the provision or collect the interest." *Id*. (citing *Great Lakes Higher Educ. Corp. v. Pardee (In re Pardee)*, 218 B.R. 916, 925 (9th Cir. BAP 1998).

off post-petition interest on a nondischargeable student loan debt, the plan had been confirmed, the creditor failed to object timely to the plan and failed to appeal the order confirming the plan, and therefore lost its right to collaterally attack the plan on the basis that the plan unfairly discriminated.[108] The Court of Appeals in *Pardee* noted that normally such provisions would not be appropriate, but implied that upon confirmation of a plan containing such a provision, the provision is no longer challengeable.[109] The Court of Appeals explained, "[i]f a creditor fails to protect its interests by timely objecting to a plan or appealing the confirmation order, 'it cannot later complain about a provision contained in a confirmed plan, even if such a provision is inconsistent with the Code.'"[110] Cases such as *Pardee* enforce the policy that confirmation orders are given preclusive effect and this policy overrides the concern that a plan may unfairly discriminate or contain other objectively inappropriate provisions. But, remember the Rule 60 discussion above.

## V. CHAPTER 13 PROVISIONS DETERMINING SECURITY INTERESTS TO BE UNPERFECTED AND AVOIDABLE

Upon entry of an order confirming a chapter 13 plan, the order is considered a binding determination of the rights and liabilities of the parties, including the debtor and the debtor's creditors. If no party appeals such an order, the confirmed plan is *res judicata* and the terms of the plan may not be collaterally attacked.[111] The binding effect of the plan extends to all of the issues that are determined by the order confirming said plan.

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[108] *Pardee*, 193 F.3d at 1085.

[109] *Id*.

[110] *Id*. at 1086 (citing *Andersen*, 179 F.3d at 1258).

[111] *See, e.g., In re Harvey*, 213 F.3d 318 (7th Cir. 2000); *Anderson*, 179 F.3d 1253. *But see In re Escobedo*, 28 F.3d 34 (7th Cir. 1994) (trustee may obtain dismissal of a chapter 13 plan that failed to comply with 11 U.S.C. §1322(a), even though the confirmation order was not appealed).

However, if a chapter 13 plan attempts to alter the characterization of a claim (that has been filed), the plan may not be binding on that creditor, even if confirmed. The Court of Appeals for the Fifth Circuit held that when a creditor files a proof of secured claim and no objection is made prior to confirmation, the claim is deemed allowed as a secured claim, even though a debtor's chapter 13 plan calls for the claim to be treated as an unsecured claim and is confirmed.[112] In *Simmons*, the debtor stated in his plan that the claim in question was unsecured and that the lien in question was to be avoided. The plan was confirmed with the above provision, but according to the Court of Appeals, the lien passed through, remaining unimpaired by the confirmation order.[113] The Court of Appeals rejected the debtor's argument that "confirmation of [the] repayment plan had the effect of dissolving [the creditor's] statutory lien because the validity of his secured claim could have been decided at the confirmation hearing, had a party in interest requested the court to do so . . . ."[114]

In a similar vein, the Court of Appeals for the Fourth Circuit has held that even if a plan that states that a secured claim is unperfected and avoidable is confirmed, the creditor's security interest survives confirmation because debtors must take certain steps to avoid a creditor's lien.[115] As the Court explained, "to extinguish or modify a lien during the bankruptcy process, some affirmative step must be taken toward that end."[116] Normally, "liens pass through bankruptcy unaffected" and '[u]nless the debtor takes appropriate affirmative action to avoid a security interest in property of the estate, that property will remain subject to the security interest

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[112] *In re Simmons*, 765 F.2d 547, 558-59 (5th Cir. 1985).

[113] *Id*. at 559.

[114] *Id*.

[115] *Cen-Pen Corp. v. Hanson*, 58 F.3d 89, 91 (4th Cir. 1995).

[116] *Id*. at 92.

following confirmation."[117] The Court in *Cen-Pen* held that "confirmation generally cannot have preclusive effect as to the validity of a lien, which must be resolved in an adversary proceeding . . ." pursuant to Rule 7001(2) of the Federal Rules of Bankruptcy Procedure.[118]

Besides bringing an adversary proceeding in order to challenge the validity of the liens, debtors may also object to the secured proof of claim filed by the creditor. If the debtor fails to do so, but instead places a provision in his plan stating that the claim is unsecured, the debtor has not taken the appropriate path to reclassify the claim, and therefore even if the plan is confirmed, such provision generally will be unenforceable.

Although a debtor may attempt to reclassify a secured claim as unperfected, and thus unsecured, in addition to avoiding the lien in a chapter 13 plan, such a provision is inappropriate and invalid, even if the plan is confirmed. A debtor must address such issues in the above manner or the claims at issue will be treated as secured regardless of what the plan provides for. If this is not done, the debtor, and perhaps counsel, will have problems down the line.

## VI. POST-CONFIRMATION MODIFICATION OF CHAPTER 13 PLANS BASED ON INCREASED DISPOSABLE INCOME

A modification of a confirmed plan is governed by section 1329 of the Bankruptcy Code. An order confirming a chapter 13 plan is a final order. Once confirmed, the plan is binding on the debtor as well as on the creditors. However, the binding effect of the confirmation order of a chapter 13 plan is not absolute. If it were, no modifications would be allowed, regardless of the circumstances.

Pursuant to section 1329, a chapter 13 debtor may request permission to modify his plan after confirmation but before completion of the plan. In addition, the trustee or an unsecured

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[117] *Id*. (citing *In re Honaker*, 4 B.R. 415, 417 (Bankr. E.D. Mich. 1980).

creditor may also request modification of a chapter 13 plan. The modified plan must meet the same standards as those provided in 11 U.S.C. §§1322(a) and (b), 1323(c) and 1325(a). In addition, the time limits on the original chapter 13 plan also apply to any modified plan. However, "principles of *res judicata* bar modification based upon issues that were known and could have been raised prior to confirmation of the debtor's plan."[119]

Pursuant to section 1329(a), a chapter 13 trustee and unsecured creditors may seek modifications of a debtor's plan. Prior to the 1984 amendments to the Bankruptcy Code, a chapter 13 trustee did not have standing to propose modifications to a confirmed chapter 13 plan.[120] The party proposing the modification bears the burden of establishing that the modification is appropriate. "A trustee or unsecured claim holder may not raise as grounds for modification under this section facts that were known and could have been raised in the original confirmation proceedings, because the order of confirmation must be considered *res judicata* as to that set circumstances."[121]

The question is: what standard must the chapter 13 trustee or unsecured creditor meet in order for the proposed modification to be approved? Not surprisingly, there is a split of authority as to the appropriate standard regarding when to allow modifications.

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[118] *Id*. at 93.

[119] *In re Miller*, 2002 WL 31115656, *2 (Bankr. M.D.N.C. 2002) (citing *Arnold v. Weast (In re Arnold)*, 869 F.2d 240 (4th Cir. 1989)).

[120] *In re Boone*, 53 B.R. 78, 80 (Bankr. E.D. Va. 1985); *but see, In re Koonce*, 54 B.R. 643, 644 (Bankr. D.S.C. 1985).

[121] *See* **5 COLLIER ON BANKRUPTCY**, ¶ 1325.03[1] (Alan N. Resnick & Henry J. Sommer, eds., 15th ed. rev. 2004).

Some courts hold that a modification proposed by the chapter 13 trustee will be allowed as long as the modified plan comports with other mandated conditions.[122] For example, in *In re Barbosa*, the First Circuit held that there is no requirement for a change of circumstances in order for a party to propose a modification to a debtor's chapter 13 plan.[123] The Bankruptcy Court for the Middle District of Florida agreed, concluding a chapter 13 trustee did not have to establish a substantial change in circumstances as a basis for a proposed modification.[124]

Other courts have held that the trustee or unsecured creditor proposing a modification to a chapter 13 plan must establish a substantial change in circumstances in order for the modification to be allowed.[125] Otherwise, the principles of *res judicata* prevent any modification to chapter 13 plans. In *Arnold v. Weast (In re Arnold)*[126], the Fourth Circuit held that a proposed modification calling for an increase in payment amounts would be barred by *res judicata* if there was no evidence presented of a substantial and unanticipated change in circumstances.[127] This standard has been reiterated in numerous bankruptcy cases.[128] The Ninth Circuit has also held that before a modification of a chapter 13 plan is permitted, a substantial change in circumstances must be

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[122] *See, e.g., Barbosa v. Soloman* (*In re Barbosa*), 235 F.3d 31, 38-41 (1st Cir. 2000); *In re Thomas*, 291 B.R. 189 (Bankr. M.D. Ala. 2003); *In re Witkowski*, 16 F.3d 739 (7th Cir. 1994) (holding that section 1329 gives debtors, creditors and trustee the absolute right to seek a modification of a chapter 13 plan).

[123] *Barbosa*, 235 F.3d at 38-41.

[124] *In re Studer*, 237 B.R. 189, 193 (Bankr. M.D. Fla. 1998).

[125] *See, e.g., In re Euler,* 251 B.R. 740 (Bankr. M.D. Fla. 2000); *In re Ferguson*, 263 B.R. 28 (Bankr. N.D.N.Y. 2001); *In re James*, 260 B.R. 368, 374 (Bankr. E.D.N.C. 2001). The moving party must also show that the modified plan satisfies 11 U.S.C. §§ 1322(a), 1322(b), 1322(c), and 1325(a). *In re Wilson*, 1997 WL 33343974, *2 (Bankr. D.S.C. 1997).

[126] 869 F.2d 240 (4th Cir. 1989); *cf. In re Solis*, 172 B.R. 530 (Bankr. S.D.N.Y. 1994).

[127] *Id*. at 243 (citations omitted).

[128] *See, e.g., In re Joseph*, 1998 WL 939694 (Bankr. E.D. Va. 1998); *In re Fowler*, 1998 WL 748643 (Bankr. E.D. Va. 1998); *In re Euler*, 251 B.R. 740 (Bankr. M.D. Fla. 2000); *In re Solis*, 172 B.R. 530 (Bankr. S.D.N.Y. 1994).

demonstrated by the trustee.[129] Recently, the Bankruptcy Court for the District of Maryland held that when considering a modification where assets have not re-vested pursuant to the confirmation order, and thus are estate assets at the time of a proposed sale, the court is required to perform a liquidation analysis under § 1325(a)(4) as of the time of the requested modification.[130]

This view is also supported by one of the leading commentators on bankruptcy, who explains, "in view of [the] congressional purpose [of section 1329(a)], the right of the trustee or the holder of an unsecured claim should be limited to situations in which there has been an unanticipated substantial change in the debtor's income or expenses that was not anticipated at the time of the confirmation hearing. As to other matters, the confirmation order should be considered *res judicata* insofar as the matters do not relate to a change in the debtor's ability to pay, subject only to the limited right to revocation of the order of confirmation and, of course, the debtor's right to voluntarily request modification."[131]

The test in determining whether there has been an unanticipated change in circumstances that warrants a modification is an objective test and it is: "'[w]hether a debtor's altered financial circumstances could have been reasonably anticipated at the time of confirmation by the parties seeking modification."[132]

Certain circumstances warrant modifications of confirmed chapter 13 plans, including an increase in disposable income. Upon an increase in disposable income, certain interested parties, including the chapter 13 trustee and unsecured creditors, may move for a modification of a

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[129] *In re Anderson*, 21 F.3d 355 (9th Cir. 1994).

[130] *In re Morgan* 299 B.R. 118, 124-25 (Bankr. D. Md. 2003).

[131] *See* **5 COLLIER ON BANKRUPTCY**, *supra* note 120, ¶ 1329.03.

[132] *Arnold*, 869 F.2d at 243 (citing *In re Fitak*, 92 B.R. 243, 249-50 (Bankr. S.D. Ohio 1988)).

chapter 13 plan. For instance, in *In re Koonce*[133], the chapter 13 debtor won approximately $1.3 million in the Massachusetts state lottery, to be paid out over twenty years.[134] Based on his winnings, the debtor experienced a significant increase in his income and therefore the chapter 13 trustee moved for a modification of the debtor's chapter 13 plan to increase payments.[135] Based on the substantial increase in income, the Bankruptcy Court for the District of South Carolina approved the modification and increased the debtor's chapter 13 payments.[136]

A modification may be warranted where a debtor experiences an increase in salary. In *Arnold*, the debtor's yearly income increased from $80,000 to $200,000.[137] Based on the substantial increase, one of the debtor's unsecured creditors moved for the Bankruptcy Court to increase the amount the debtor was paying into his chapter 13 plan, and the Bankruptcy Court granted the motion and modified the debtor's plan.[138] The Court of Appeals for the Fourth Circuit affirmed the lower court's decision, concluding that because the chapter 13 debtor's gross monthly income had increased $10,000 from the time of confirmation, modification was warranted.[139]

## V. CONCLUSION

When individuals file for chapter 13 relief, they are required to present to the Bankruptcy court, all creditors, and all parties in interest, a chapter 13 plan. The plan must satisfy certain

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[133] 54 B.R. 643 (Bankr. D.S.C. 1985).

[134] *Id*. at 644.

[135] *Id*.

[136] *Id*. at 645.

[137] *Arnold*, 869 F.2d at 241.

[138] *Id*.

[139] *Id*. at 243.

requirements, such as being proposed in good faith, paying the unsecured creditors at least as much as they would receive in a chapter 7 liquidation and proposing to put all of the individual's disposable income into the plan over the duration of the plan.

While chapter 13 plans may propose separate classification of unsecured claims, the plan must not unfairly discriminate against any class, so bankruptcy courts must determine whether the proposed treatment unfairly discriminates. Plans may propose separate classification for either co-signed debts or student loan obligations. The bankruptcy courts must determine whether such proposed treatment should be allowed. If a bankruptcy court determines that the proposed separate classification of certain debt unfairly discriminates against other general unsecured creditors, the chapter 13 plan will not be confirmed.

Upon confirmation of a plan, the confirmation order entered by the Bankruptcy Court is a binding determination of the rights and liabilities of the various interested parties and typically has a *res judicata* effect. Therefore, if a chapter 13 plan provides that a security interest is unperfected and avoidable, and the Court confirms the plan, that provision may or may not be binding on the creditor holding the claim. Creditors should review plans before the deadline to object to confirmation, in order to determine if they are being treated unfairly under the proposed plan. If so, they should object. If no objection is filed, and a plan is confirmed, the plan may be binding, even if it unfairly discriminates.