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NEW EVIDENCE FOR THE BROAD VIEW: RECONSIDERING THE ABSOLUTE PRIORITY RULE IN INDIVIDUAL-DEBTOR CHAPTER 11 CASES POST-SBRA

Justin J. Maroni*

INTRODUCTION

Honest but unfortunate debtors who find themselves in financial distress may seek relief under the United States Bankruptcy Code (“the Code”).1 Chapter 11 of the Code is specifically designed to promote the successful reorganization of distressed business entities (though not limited exclusively to business entities) by affording debtors “a ‘financial breathing spell’ from most creditor collection efforts.”2 Under the protections of Chapter 11, such as the automatic stay, debtors can continue business operations while formulating a plan of reorganization to repay creditors.3 Confirming a plan of reorganization is typically the primary goal in a Chapter 11 case.4 Once a plan is proposed, “the plan is voted upon by the debtor’s creditors, and the bankruptcy court must make certain findings (e.g., the plan was proposed in good faith and it complies with specified payment priorities).”5 “If the court is satisfied, then the plan is confirmed and the debtor is no longer in Chapter 11.”6 If the case is unsuccessful however—i.e., the debtor is unable to confirm a plan—then the case will either be converted to a Chapter 7 bankruptcy or dismissed, whichever is in the best interests of the creditors and the bankruptcy estate.7 Ultimately, the provisions of Chapter 11 are designed to foster, not frustrate, the reorganization and economic well-being of the debtor. This fundamental principle should apply equally whether the debtor is a corporation or an individual.

Although Chapter 11 was unquestionably designed with large businesses in mind, individual debtors are also eligible to file for Chapter 11 relief.8 In fact, the ABI Commission to Study the Reform of Chapter 11 (‘‘ABI Commission’’) found that the number of Chapter 11 cases filed by individuals has increased dramatically since 2006,

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3 Id.
4 Id.
5 Id.
6 Id.
7 Id.
a trend the Commission attributed to “[an] increase in the number of individuals needing the bankruptcy remedy but precluded from filing under Chapter 13 because of statutory debt limits.” This increase “[has] led many to question the adequacy and suitability of Chapter 11 for individual debtors.” A paramount concern is the applicability of the “absolute priority rule” in individual-debtor Chapter 11 cases. If applicable, the rule effectively precludes confirmation of an individual debtor’s plan of reorganization if an unsecured creditor will not be paid in full. Yet, the ABI Commission underscored that, “currently, there is no judicial consensus on whether (and to what extent) the Bankruptcy Abuse Prevention and Consumer Protection Act (“BAPCPA”) amendments abrogated the absolute priority rule by excepting post-petition property and earnings from amended Section 1129(b)(2)(B)(ii).” A majority of courts have adopted the so-called “narrow view” that the BAPCPA amendments abrogated the absolute priority rule only as to post-petition assets incorporated into the estate by Section 1115. Some courts, however, adhere to a different view—the so-called “broad view”—holding that the absolute priority rule no longer applies in individual Chapter 11 cases.

While the narrow view has taken hold as the clear majority position on this issue, this Note reevaluates the broad view in light of Congress’s recent enactment of the Small Business Reorganization Act (“SBRA”) in August 2019. The SBRA adds a new Subchapter to Chapter 11 of the Code, intended to improve the reorganization process for debtors qualifying as small business debtors (which, as will be discussed, includes qualified individual debtors). Among the changes implemented by the SBRA is the unambiguous elimination of the absolute priority rule. If the absolute priority rule does not apply to individuals under the new SBRA provisions, why should it apply to individuals in a traditional individual-debtor Chapter 11 case? This Note contends that it should not.

This Note looks first at how an individual debtor finds him or herself proceeding under Chapter 11. As such, this Note briefly discusses the conventional forms of relief for individual debtors, namely Chapters 7 and 13, before turning to the Chapter 11 alternative. The focus of this Note then shifts to the requirements for confirmation of a debtor’s plan of reorganization in what is known as a cram-down process, and, more specifically, the fair and equitable requirement for a cram-down. To that end, this Note provides background on the fair and equitable requirement, the development of the

10 Id. at 318. See discussion infra pp. 7–17.
11 See In re O’Neal, 490 B.R. 837, n. 9 (Bankr. W.D. Ark 2013) (listing courts adhering to the narrow view).
12 Id. at n. 8 (listing courts adhering to the broad view).
13 See discussion infra pp. 18–20.
absolute priority rule, and the challenges that the rule created for individual debtors following the Bankruptcy Reform Act of 1978. Next, this Note addresses the 2005 BAPCPA amendments. As mentioned, following the BAPCPA amendments, a split in authority emerged regarding the meaning of amended Section 1129(b)(2)(B)(ii)’s individual-debtor exception. This Note carefully considers the arguments for both the narrow and broad view of the exception and the impact the exception has in individual-debtor cases. Lastly, this Note examines the expected impact of the SBRA. In light of the SBRA’s elimination of the absolute priority rule, this Note argues that bankruptcy courts should reconsider the broad view in traditional individual-debtor Chapter 11 cases.

I. CONVENTIONAL RELIEF FOR INDIVIDUAL DEBTORS: CHAPTERS 7 & 13

Individuals who find themselves insolvent or in financial distress, and considering filing for bankruptcy, primarily have three options: Chapter 7, Chapter 13, and Chapter 11.\(^\text{19}\) Chapter 7 is best considered a last resort. This is because Chapter 7 does not involve the filing of a plan of repayment as in Chapter 13, or a plan of reorganization as in Chapter 11.\(^\text{20}\) Instead, Chapter 7 involves a complete liquidation: “[t]he bankruptcy trustee [appointed by the bankruptcy court] gathers and sells the debtor's nonexempt assets and uses the proceeds of such assets to pay holders of claims (i.e., creditors) in accordance with the provisions of [the Code].”\(^\text{21}\) Thus, besides the exempt property specified by the Code or the laws of the debtor’s home state, a debtor will usually lose property.\(^\text{22}\) In order to avoid this result, qualified individual debtors may find Chapter 13 to be a useful alternative.

Chapter 13—commonly referred to as a wage earner’s plan—“enables individuals with regular income to develop a plan to repay all or part of their debts.”\(^\text{23}\) This repayment plan provides debtors the ability to make regular payments of fixed amounts to the trustee appointed by the court over the course of three to five years.\(^\text{24}\) Thus,

\(^\text{19}\) It is also worth noting that some individual debtors may be eligible for Chapter 12 relief. Chapter 12 - Bankr. Basics, U.S. Cts., https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/Chapter-12-bankruptcy-basics (last visited Nov. 24, 2019). Congress designed Chapter 12 for “family farmers” or “family fishermen” with “regular annual income” by combining aspects of Chapter 11 and Chapter 13. Id. Chapter 12 is substantially similar to Chapter 13, in that it “enables financially distressed family farmers and fishermen to propose and carry out a plan to repay all or part of their debts” over a three to five-year commitment period. Id. Moreover, like Chapter 13, Chapter 12 eliminates the absolute priority rule, imposing a “best interest of creditors” test instead. Id. However, Chapter 12 is better tailored to the needs of family farmers and fisherman, because Chapter 13 was “designed for wage earners who have smaller debts than those facing family farmers.” Id.


\(^\text{21}\) Id.

\(^\text{22}\) The Bankruptcy Code and the laws of most states allow debtors to keep a certain amount of equity in the debtor’s home, personal property, such as a car, if the exemption covers the remaining equity in the property, retirement accounts, and some wages, as well as most household goods and clothing. See Cara O’Neill, Exemptions in Chapter 7 Bankruptcy, NOLO, https://www.nolo.com/legal-encyclopedia/property-exemptions-Chapter-7-bankruptcy.html (last visited Nov. 24, 2019).


\(^\text{24}\) Id.
much like Chapter 11, “[t]he focus of Chapter 13 is [the] confirmation of a plan.”

After the debtor proposes a plan, “creditors and the Chapter 13 trustee have the opportunity to object to it.” The court then considers whether the plan complies with the requirements for the contents of a Chapter 13 plan (found primarily in Section 1322) and the requirements for confirmation of the plan (found in Section 1325). As this Note will discuss below, the template for the individual-debtor Chapter 11 provisions implemented by the BAPCPA amendments in 2005, “was to adopt and adapt as much of Chapter 13 as possible with respect to individual debtors in Chapter 11.” Therefore, it will be helpful to briefly describe Chapter 13’s confirmation requirements with respect to unsecured claims.

A Chapter 13 plan may modify unsecured claims. “Modification occurs if the plan provides for anything other than immediate payment in full.” Indeed, “Chapter 13 plans frequently modify unsecured claims by providing for payment of only a portion of the total debt.” In order to confirm a plan where a modification is proposed, however, the amount the debtor proposes to pay must meet the “best interest of creditors” test of Section 1325(a)(4) and, potentially, the projected disposable income test of Section 1325(b). “The best interest of creditors test . . . requires that each unsecured creditor receive distributions with a value as of the effective date of the plan equal at least to the amount that the creditor would receive if the debtor’s assets were liquidated in a Chapter 7 case.” If all of the requirements of Section 1325(a), including the best interest of creditors test, are satisfied, “the court must confirm the plan unless there is an objection that invokes the ‘projected disposable income test’ of Section 1325(b).” If so, then the plan must also satisfy that test. Specifically, Section 1325(b)(1) provides:

If the trustee or the holder of any unsecured claim objects to the confirmation of the plan, then the court may not approve the plan.

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26 Id.
27 Id.
29 11 U.S.C. § 1322(a)(4) (2018). “Unsecured claims are generally those for which the creditor has no special rights to collect against particular property owned by the debtor.” Drake, et al., supra note 25, § 7:1. Unsecured claims are junior to priority claims and secured claims. Chapter 13 – Bankr. Basics, supra note 23. “Priority claims are those granted special status by the bankruptcy law, such as most taxes and the costs of bankruptcy proceeding.” Drake, et al., supra note 25, § 7:1. Generally, priority claims must be repaid in full. Chapter 13 – Bankr. Basics, supra note 23. “Secured claims are those for which the creditor has the right to take back certain property (i.e., the collateral) if the debtor does not pay the underlying debt.” Drake, et al., supra note 25, § 7:1. Generally, secured claims “must provide that the holder of the secured claim receive at least the value of the collateral.” Id. The treatment of priority claims and secured claims under Chapter 13 is similar to the treatment of such claims under Chapter 11.
30 Drake et al., supra note 25, § 7:2.
31 Id.
32 Id.
33 Id. “The best interest test thus requires calculation of what an unsecured creditor would receive in a hypothetical Chapter 7 case from the liquidation of the debtor’s assets after payment of secured and priority claims.” Id.
34 Id.
35 Id.
unless . . . (A) the value of the property to be distributed under the
plan on account of such claim is not less than the amount of the claim;
or (B) the plan provides that all of the debtor’s projected disposable
income to be received in the applicable commitment period . . . will
be applied to make payments to unsecured creditors of the plan.36

Yet, so long as these requirements—the best interest of creditors test and, if
applicable, the projected disposable income test—are met (and the plan is proposed in
good faith) “[t]he plan is confirmable even if it provides for nominal, or even no,
payments to unsecured creditors.”37 Critically, this means that the debtor may also
retain property, even if a class of unsecured creditors is impaired by the plan. In other
words, Chapter 13 contains no absolute priority rule.38

In re Ruggles is illustrative.39 In that case the debtor, Darlene Ruggles
(“Ruggles”), owned a duplex worth approximately $125,000 that was encumbered by
a secured claim of $75,000.40 Ruggles filed a Chapter 13 petition and then “proceeded
to claim a $50,000 homestead exemption in the entire equity of the duplex.”41
Although unsecured creditors held claims in the amount of $59,115, Ruggles’s
repayment plan provided that all of her projected disposable income received during
the three year commitment period—just $6,327 (only slightly more than ten percent of
the total unsecured claims)—would be applied to make payments to the unsecured
creditors.42 However, because the duplex would have been exempt under a Chapter 7
liquidation, the unsecured creditors would purportedly receive $500 more under the
repayment plan than they would have received in a hypothetical liquidation.43 The
bankruptcy court noted that “the sole purpose of the plan [was] to retain exempt and
non-exempt assets while paying a minimal return to unsecured creditors,” but
nevertheless confirmed Ruggles’s plan, finding that it was filed in good faith, was in
the best interest of her creditors, and satisfied the projected disposable income test.44

Under Chapter 11, on the other hand, Ruggles’s plan would have inevitably
violated the absolute priority rule—Ruggles retained her interest in the duplex even
though the unsecured creditors neither accepted the plan nor were they to be repaid in
full under the plan.45 Consequently, individual debtors typically prefer Chapter 13 to
Chapter 11. But not all individual debtors are eligible for Chapter 13 relief; some may
be forced to contend with the absolute priority rule under Chapter 11.

difference between ‘current monthly income,’ calculated in accordance with its statutory definition, less
permitted expenditures. The ‘applicable commitment period’ is three years for a debtor with current monthly
income below the applicable median income in the debtor’s state for a family of the same size as the debtor’s
household and five years if it is above the applicable median income, unless the plan provides for payment of
unsecured claims in full within a shorter time.” DRAKE, et al., supra note 25, § 7:2.
37 DRAKE, et al., supra note 25 at § 7:2.
38 Id.
40 Id. at 59.
41 Id.
42 Id.
43 Id.
44 Id. at 59, 61.
45 See discussion infra at p. 11–17.
II. THE CHAPTER 11 ALTERNATIVE

A. INDIVIDUAL-DEBTOR CHAPTER 11 CASES

Individual-debtor Chapter 11 cases usually involve debtors with complex financial affairs or a home mortgage balance exceeding Chapter 13’s limit on secured debt. In fact, Professor Richard Hynes, et al., made the following findings about the typical profile of an individual Chapter 11 debtor:

Chapter 11 debtors are much more likely to operate a business, and they have dramatically higher debt-to-income ratios than other consumer debtors . . . . As expected, Chapter 11 debtors have much higher household incomes than individuals in Chapters 7 or 13, but their expenses also are quite large. Real estate debt plays a particularly prominent role, which, unsurprisingly is especially true of the filings made in 2010.

At the same time, however, Professor Hynes, et al., found that “the vast majority of [these] debtors have a small number of creditors. Half have liabilities that fall below the liability threshold for small business debtors and assets and liabilities that fall far below the $10 million cutoff that the American Bankruptcy Commission recently recommended for small and medium sized enterprises.” Thus, despite having more complex financial affairs or slightly larger debts, Professor Hynes, et al., writes, “it makes little sense to apply very different rules” to individuals with otherwise similar characteristics depending on whether they file under Chapter 11 or Chapter 13.

Yet, in a majority of jurisdictions, a different rule—the absolute priority rule—is applied depending on whether an individual debtor files under Chapter 11 or Chapter 13. In Chapter 13, the absolute priority rule simply does not exist. In Chapter 11, however, application of the rule sometimes proves fatal to individual debtors’ chances of confirming a plan of reorganization. In fact, in those jurisdictions adhering to a narrow view of Section 1129(b)(2)(B)(ii)’s individual-debtor exception, individual debtors are less likely to succeed at confirming a plan of reorganization than individual debtors in jurisdictions adhering to the broad view. This, in turn, contributes to disparity between the success rates for individual debtors in Chapter 11 and Chapter

46 PRACTICAL LAW BANKRUPTCY AND RESTRUCTURING, INDIVIDUAL CHAPTER 11 BANKRUPTCY: OVERVIEW (n.d.), Westlaw W-008-8977. “Only an individual with regular income that owes, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts of less than $250,000 and noncontingent, liquidated, secured debts of less than $750,000 . . . may be a debtor under Chapter 13 of this title.” 11 U.S.C. § 109(e) (2018).
47 Hynes et al., supra note 8, at 66.
48 Id. at 67.
49 Id. at 66.
50 Id. at 132–35.
In order to understand why and how the rule applies to individual debtors in Chapter 11, it is first critical to understand Chapter 11’s cram-down confirmation requirements.

**B. SECTION 1129 AND THE CONFIRMATION CONUNDRUM**

A debtor’s plan of reorganization can generally be confirmed in two ways. Most plans are confirmed consensually under Section 1129(a),” in which case “every impaired class has voted to accept the plan of reorganization.” However, when a debtor cannot confirm a plan consensually under Section 1129(a) because one or more impaired classes have not accepted the plan proposed by the debtor, one potential alternative is nonconsensual confirmation through the “cram-down” provisions set forth in Section 1129(b). In order for the court to confirm a plan of reorganization in a cram-down, the debtor must request that the court confirm the plan in a cram-down procedure and satisfy three substantive requirements. “The first substantive requirement is that all the requirements of [Section] 1129(a) must be satisfied, except for [Section] 1129(a)(8).” Second, the plan must not discriminate unfairly against dissenting classes. Third, “the plan must be fair and equitable with respect to dissenting classes.” The “fair and equitable” requirement is the primary focus of this Note. In order for a plan to be fair and equitable with respect to a dissenting class of unsecured creditors, the plan must not violate the absolute priority rule: “a dissenting class of unsecured creditors must be provided for in full before any junior class of unsecured creditors can receive or retain property under a reorganization plan.”

**i. The Fair and Equitable Requirement: Origins of The Absolute Priority Rule and The New Value Exception**

“The absolute priority rule initially was a judicially created concept, arising from a series of early twentieth-century railroad cases, including *Northern Pacific Railway Co. v. Boyd.*” In *Northern Pacific Railway Co. v. Boyd,* the Northern Pacific Railroad (the “Railroad”) purchased the stake of the majority shareholder of the Coeur d’Alene Railway (“Coeur”). After the purchase, the Railroad apparently began to struggle...
financially, and, in 1893, creditors brought a bill of insolvency against the Railroad and the Coeur line. In 1895, however, as the result of an agreement between the Railroad’s shareholders and mortgage bondholders, the mortgage holders began foreclosure proceedings against the Railroad’s assets. In 1899, the line's property was sold at foreclosure for $220,000 to the newly organized Northern Pacific Railway Company. Under the agreement, the new railway company was to purchase the property of the old railroad, issue more bonds, use part of the money from these bonds to pay the receiver's certificates from the insolvency proceeding, purchase new equipment, and make some improvements to the lines. The balance of the bond money was used to purchase the bonds of the old company. In addition, the new railroad issued preferred and common stocks to pay the debts of some of the subsidiaries for which the railroad was liable, the expenses of the reorganization, and to redeem the stock of the older railroad. No provisions, however, were made for any payment to creditors other than the bondholders. Consequently, unsecured creditors brought a suit asking that the court enjoin the foreclosure sale as a conspiracy between the bondholders and the stockholders to exclude the general creditors.

On appeal to the Supreme Court, the Court was persuaded that the undertaking was a conspiracy between the secured creditors of the railroad and the company's stockholders to benefit their individual interests at the expense of the general creditors. The Court found that the shareholders had joined forces with the bondholders to “reorganize” in a way that left the unsecured creditors without payment or remedy. The Court therefore “adopted the absolute priority rule to prevent deals between senior creditors and equity holders that would impose unfair terms on unsecured creditors.” In the decades since the Boyd decision “the . . . concern . . . that the equity owners or senior debt holders might act separately or in combination to extinguish the rights of junior creditors, has been the driving force behind judicial scrutiny of plans of reorganization under federal law where the absolute priority rule has arisen.”

In 1978, Congress passed the Bankruptcy Reform Act of 1978, which, among comprehensive reforms, codified the absolute priority rule in Chapter 11 of the Code under Section 1129(b)(2)(B). As it existed then, Section 1129(b)(2)(B) read:

> With respect to a class of unsecured claims, (i) the plan provides that each holder of a claim of such class receive or retain on account of

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62 Id. at 487.
63 Id. at 488.
64 Id.
65 Id.
66 Id. at 488.
67 Id.
68 Id. at 488–89.
69 Id. at 489.
70 Id. at 490.
72 Id.
73 Id.
such claim property of a value, as of the effective date of the plan, equal to the allowed amount of such claim; or (ii) the holder of any claim or interest that is junior to the claims of such class will not receive or retain on account of such junior claim or interest any property.75

In the wake of the Bankruptcy Reform Act, the question arose whether a Chapter 11 debtor could ever confirm a plan while retaining an interest in property.

In 1988, the United States Supreme Court took up this question in the case of *Northwest Bank Worthington v. Ahlers.*76 Fittingly enough, respondents—the Ahlers—were individual debtors operating a failing family farm in Minnesota.77 Between 1965 and 1984, the Ahlers had obtained several secured loans from petitioners, Northwest Bank Worthington (“Northwest Bank”).78 Then, “in November 1984, respondents defaulted on their loan payments to . . . [Northwest Bank] . . . .”79 In order to avoid repossession of the collateral securing the loans, the Ahlers sought the protection of Chapter 11.80 In response, Northwest Bank sought relief from the automatic stay, arguing that the absolute priority rule would have prevented confirmation of any plan under which the Ahlers retained their farm because without the farm to generate cash flows no plan of reorganization would be successful.81

The Eighth Circuit Court of Appeals rejected Northwest Bank’s argument.82 Notwithstanding the absolute priority rule, the circuit court held that the absolute priority rule did not bar respondents from retaining their equity interest in the farm if they contributed “money or money’s worth” to the reorganized enterprise.83 The circuit court further concluded that Ahlers’ “yearly contributions of labor, experience, and expertise” would constitute a contribution of “money or money's worth,” and would permit confirmation of a reorganization plan over petitioners' objections.84 In reaching this conclusion, the circuit court relied on dicta in the Supreme Court’s decision in *Case v. Los Angeles Lumber Products Co.*85 There, the Court posited the existence of a so-called “new value exception” to the absolute priority rule:

It is, of course, clear that there are circumstances under which stockholders may participate in a plan of reorganization of an insolvent debtor . . . . [W]e believe that to accord ‘the creditor of his full right of priority against the corporate assets' where the debtor is insolvent, the stockholder's participation must be based on a

75 *Id.*
77 *Id.* at 199.
78 *Id.*
79 *Id.* “[T]he aggregate loan balance owed the petitioners exceeded $1 million.” *Id.* at 200.
80 *Id.* at 200.
81 *Id.*
82 *Id.* at 200.
83 *Id.*
84 *Id.* at 201.
contribution in money or money's worth, reasonably equivalent in view of all the circumstances to the participation of the stockholder.\textsuperscript{86}

Although the circuit court had found that such an exception was applicable to the Ahlers’ situation, the Supreme Court disagreed.\textsuperscript{87} In an opinion in which all of the justices joined (except Justice Kennedy, who took no part in the consideration or decision of the case), the Court held that the absolute priority rule applied, and that “respondents' promise of future labor warranted no exception to its operation.”\textsuperscript{88} Turning first to the statutory language and legislative history of Section 1129(b)(2)(B)(ii), the Court concluded that Congress did not intend to liberalize the absolute priority rule when it was codified.\textsuperscript{89} The Court reasoned that Congress had explicitly rejected a proposal by the Bankruptcy Commission to “modify the absolute priority rule to permit equity holders to participate in a reorganized enterprise based on their contribution of ‘continued management . . . essential to the business’ or other participation beyond ‘money or money's worth.'”\textsuperscript{90} Further, according to the Court, even assuming that an equity holder might be able to retain property under the plan in the event that he or she makes a contribution in money or money's worth, respondents’ promise of future services was not such a contribution.\textsuperscript{91}

Having decided that the Ahlers’ promise of future services was not a contribution of money or money’s worth, the Court then addressed an argument advanced by the Ahlers that “the absolute priority rule has no application . . . where the property which the junior interest holders wish to retain has no value to the senior unsecured creditors.”\textsuperscript{92} The Court rejected this so-called “no value” theory, finding that:

Even where debts far exceed the current value of assets, a debtor who retains his equity interest in [an] enterprise retains “property.” Whether the value is present or prospective, for dividends or only for purposes of control, a retained equity interest is a property interest to which the creditors [are] entitled . . . before the stockholders [can] retain it for any purpose whatever.\textsuperscript{93}

Perhaps the most important passage of the Ahlers opinion for purposes of this Note though, is that in which the Court acknowledges the then recently enacted Family

\textsuperscript{87} Id. at 202 (1988).
\textsuperscript{88} Id. at 206.
\textsuperscript{89} Id. at 205.
\textsuperscript{90} Id.
\textsuperscript{91} Id. at 204 (“A promise of future services is intangible, inalienable, and, in all likelihood, unenforceable. It 'has no place in the asset column of the balance sheet of the new [entity]' . . . Unlike 'money or money's worth,' a promise of future services cannot be exchanged in any market for something of value to the creditors today.'”) (quoting L.A. Lumber Prod. Co., 308 U.S. at 122–23).
\textsuperscript{92} Id. at 207. The Ahlers specifically contended that, because the farm has no "going concern" value (apart from their own labor on it), any equity interest they retain in a reorganization of the farm is worthless, and therefore is not "property" under 11 U.S.C. § 1129(b)(2)(B)(ii).
\textsuperscript{93} Id. at 207–08.
Farmers Bankruptcy Act of 1986. That Act created the Chapter 12 bankruptcy proceeding. Notably, the Court pointed out that “one of Congress' principal concerns in adopting Chapter 12 was the difficulties farmers encountered in seeking to reorganize under Chapter 11.” Yet, the Court continued: “as respondents concede, the Court of Appeals' decision here creates a method of proceeding under Chapter 11 which is far more advantageous to farmers than is Chapter 12.” Finding such a state of affairs unlikely, the Court refused to believe “that Congress created, in Chapter 12, an option for farm reorganizations less accessible to most farmers than current Chapter 11 proceedings.” On the contrary, the Court held: “where Congress adopts a new law . . . [it] normally can be presumed to have had knowledge of the interpretation given to the [old] law.”

The Supreme Court later returned to the issue of the new value exception in Bank of America National Trust and Savings Association v. 203 North LaSalle Street Partnership. In that case, the impaired creditor-bank took the position that the plan could not be confirmed as a cram-down because old equity holders would receive property despite the fact that the bank’s unsecured deficiency claim would not be paid in full—i.e., the absolute priority rule would be violated. The debtor-partnership responded that the plan satisfied the new value exception because “in exchange for the partnership’s entire ownership of the reorganized debtor . . . certain former partners of the Debtor would contribute $6.125 million in new capital.” The Court, however, declined to decide whether the absolute priority included a new value exception, and, instead, held on narrower grounds that the proposed plan failed to satisfy Section 1129(b)(2)(B).

Explaining why the debtor’s plan failed to satisfy the statute, the Court focused on the fact that “[b]efore the debtor’s plan was accepted no one else could propose an alternative one, and after its acceptance no one else could obtain equity in the reorganized entity.” Consequently, the result of such a plan would be that “at the moment of the plan’s approval the debtor’s partners necessarily enjoyed an exclusive opportunity . . . .” Thus, the Court believed that this opportunity should be treated as the retention of a property right, in violation of the absolute priority rule. The Court reasoned:

If the price to be paid for the equity interest is the best obtainable, old equity does not need the protection of exclusiveness (unless to trump

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94 Id. at 210–11; See Pub. L. 99-544, § 255, 100 Stat. 3105-14
95 Ahlers, 485 U.S. at 210.
96 Id.
97 Id.
98 Id. at 211.
101 Id. at 442.
102 Id. at 440.
103 Id at 443.
104 Id. at 455.
105 Id.
106 Id.
an equal offer from someone else); if it is not the best, there is no apparent reason for giving old equity a bargain. There is no reason, that is, unless the very purpose of the whole transaction is, at least in part, to do old equity a favor. And that, of course, is to say that old equity would obtain its opportunity, and the resulting benefit, because of old equity’s prior interest within the meaning of [the absolute priority rule]. Hence it is that the exclusiveness of the opportunity, with its protection against the market’s scrutiny of the purchase price by means of competing bids or even competing plan proposals, renders the partners’ right a property interest extended “on account of” the old equity position and therefore subject to an unpaid senior creditor class’s objection.107

The primary takeaway from 203 North LaSalle Street Partnership, therefore, is that a “new value plan cannot be confirmed if the old equity holders are the only ones given an opportunity to bid on the debtor’s ownership interests.”108 Thus, even if it is possible to take advantage a new value exception, such exception is narrowly construed. Consequently, after the enactment of the Bankruptcy Act of 1978, the absolute priority rule, in combination with the narrowness of the new value exception, quickly made apparent that individual Chapter 11 debtors were extraordinarily unlikely to be able to confirm a plan of reorganization if a dissenting class of unsecured creditors was impaired.

ii. Pre-BAPCPA Plans of Reorganization for Individuals—Practically Unconfirmable!

In the years following the 1978 reforms, it became clear that the application of Section 1129(b)(2)(B) imposed a serious impediment to reorganization. In fact, application of the absolute priority rule effectively meant that no individual debtor could ever confirm a Chapter 11 plan if an unsecured creditor would not be paid in full.109 Consequently, individual debtors filing under Chapter 11 were left searching for arguments that would allow them to circumvent the rule and retain property.

In In re Davis, for instance, the debtors argued,

It makes no sense to apply the rule in individual cases for two fundamental reasons: first, that the rule was developed in the context of corporate or partnership cases where equity “interests” are held by third parties, not by the debtors themselves; and, second, that it is

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107 Id. at 456.
impossible to apply without, in effect, denying meaningful Chapter 11 relief to individual debtors.\textsuperscript{110}

In that case, the debtor’s plan of reorganization proposed that the debtors would retain rent-producing properties, distributions from which would be used to fund the repayment of unsecured creditors.\textsuperscript{111} Moreover, the plan provided that if the Court determined that “a contribution of new value was necessary for confirmation,” then the debtors would “agree to contribute $100,000 of non-estate funds as their new-value contribution,” provided, however, that they would “reserve the right to liquidate the properties.”\textsuperscript{112} The plan also stated that the purpose of the new value would be to ensure timely performance of their obligations under the plan and “to avoid adverse tax consequences which might arise from the sale or disposition of the properties.”\textsuperscript{113}

The plan was rejected by one class of creditors, but otherwise satisfied the requirements for a cram-down under Section 1129(a)(10).\textsuperscript{114} The objecting class argued that the debtors’ plan could not be confirmed because it violated \textit{203 North LaSalle Street Partnership}.\textsuperscript{115}

In support of the plan, the debtors argued that under \textit{Toibb v. Radloff},\textsuperscript{116} the absolute priority rule should not apply to individual, nonbusiness debtors.\textsuperscript{117} Specifically, the Debtors argued that “applying the rule to individual debtors would result in undesirable forced asset sales not otherwise contemplated by the structure of Chapter 11.”\textsuperscript{118} Because this result is irrational in individual-debtor cases, they argued, the court should ignore the rule.\textsuperscript{119} The bankruptcy court disagreed.\textsuperscript{120} The court did not dispute that \textit{Toibb} stands primarily for the proposition that certain provisions in Chapter 11 have little application to nonbusiness debtors, but concluded that the absolute priority rule is not among those provisions.\textsuperscript{121} Instead, relying primarily on \textit{Ahlers}, the court held that the absolute priority rule applied even in the case of an individual debtor.\textsuperscript{122} The court explained: “[t]he fact that the application of the law to a certain situation may be inconvenient or painful does not justify ignoring a clearly relevant statute and those cases at all levels that have interpreted it.”\textsuperscript{123}

Moreover, the court addressed the debtors’ argument that the plan fell within the new-value exception.\textsuperscript{124} The court found that even though the plan provided that the debtors could contribute $100,000 of non-estate funds as their new-value contribution, the plan did not provide for competing plans or any other mechanism for entities to

\textsuperscript{111} \textit{Id.} at 793.
\textsuperscript{112} \textit{Id.}
\textsuperscript{113} \textit{Id.}
\textsuperscript{114} \textit{Id.} at 794.
\textsuperscript{115} \textit{Id.}
\textsuperscript{117} \textit{Davis}, 262 B.R. at 794.
\textsuperscript{118} \textit{Id.} at 797.
\textsuperscript{119} \textit{Id.}
\textsuperscript{120} \textit{Id.}
\textsuperscript{121} \textit{Id.} at 795, 797.
\textsuperscript{122} \textit{Id.} at 797.
\textsuperscript{123} \textit{Id.}
\textsuperscript{124} \textit{Id.} at 797–98.
compete with the new value proposed by the debtors. Consequently, the proposed plan would necessarily fail the so-called “market” or “nonexclusive” test established in 203 North LaSalle Street Partnership. Consequently, the debtors’ plan of reorganization could not be confirmed.

_in re Davis_ is just one among many individual-debtor cases in which the debtors failed to confirm a plan or reorganization because of the barrier imposed by the absolute priority rule and the narrowly construed new-value exception. Simply stated, prior to enactment of BAPCPA in 2005, it was incredibly difficult to perceive how an individual Chapter 11 debtor could meet the requirements of the new-value exception, and thereby maintain an interest in the estate despite the absolute priority rule. The 2005 BAPCPA amendments, however, provided new hope for individual debtors proceeding under Chapter 11.

### iii. Individual Debtors After BAPCPA—Still Unconfirmable?

In 2005, Congress completed a comprehensive overhaul of the Code by enacting the Bankruptcy Abuse and Consumer Protection Act (“BAPCPA”). As part of BAPCPA, Congress enacted a host of changes applicable in individual-debtor Chapter 11 cases. “Most of the changes . . . were part of an overall design of adapting various Chapter 13 provisions to fit in Chapter 11.” In fact, courts and commentators have pointed out that the individual-debtor provisions the BAPCPA implemented “operate in ways very similar to Chapter 13 [provisions].” One such change was an amendment to Section 1129(b)(2)(B)(ii). The statute now reads:

(ii) the holder of any claim or interest that is junior to the claims of such class will not receive or retain under the plan on account of such junior claim or interest any property, except that in a case in which the debtor is an individual, the debtor may retain property included in the estate under [Section] 1115, subject to the requirements of Subsection (a)(14) of this Section.

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125 Id. at 798.
126 Id. at 799; See Bank of Am. Nat. Tr. & Sav. Ass'n v. 203 N. LaSalle St. P'ship, 526 U.S. 434, 458 (1999) (“Plans providing junior interest holders with exclusive opportunities free from competition and without benefit of market valuation fall within the prohibition of § 1129(b)(2)(B)(i).”).
129 Robert J. Landry III, Individual Chapter 11 Reorganizations: Big Problems with the New Big Chapter 13, 29 U. ARK. LITTLE ROCK L. REV. 251, 251–52 (2007). “The principal purpose of the [BAPCPA amendments] was to change the rules related to an individual’s eligibility for bankruptcy, particularly in Chapter 7, by linking the availability of bankruptcy relief to a debtor’s income and other means.” Shat, 424 B.R. at 60 (citing H.R. 2500, 105th Cong. § 101 (1997); S. 1301, 105th Cong. § 102 (1997)). While “the initial ‘means-testing’ provisions did not purport to make any changes to Chapter 11,” the version eventually passing both the House and the Senate contained “a short, but significant list” of amendments which applied only to individuals in Chapter 11. Shat, 424 B.R. at 859–60.
130 Shat, 424 B.R. at 868.
131 Id. at 862 (comparing post-BAPCPA individual-debtor provisions with analogous Chapter 13 provisions).
After the BAPCPA amendments, the additional clause creating an exception for individual debtors has been a source of controversy. “[T]he clause obviously modifies the absolute priority rule . . . . The question is, how extensive is the modification?”

One interpretation of the additional clause is that it effectively abrogates the absolute priority rule. This would, of course, accord with the idea that Congress sought to mirror Chapter 13 because, as previously discussed, there is no absolute priority rule under Chapter 13. Professor Robert Landry and others have argued that Congress recognized the barrier the absolute priority rule previously imposed for individual Chapter 11 debtors, and amended Section 1129(b)(2)(B)(ii) with the intention of making confirmation of a plan in an individual-debtor Chapter 11 case easier. According to adherents of this interpretation, the conclusion that the BAPCPA amendments abrogated the absolute priority rule is supported both by a plain-language reading of Section 1129(b)(2)(B)(ii) and the thrust of the overall statutory scheme.

Recall first that in order to confirm a plan in a cram-down procedure, the debtor must initially meet all of the applicable requirements of Section 1129(a), except for Subsection (a)(8). Notably, as part of the BAPCPA Congress amended Section 1129(a) by adding paragraph (15), which provides:

(15) In a case in which the debtor is an individual and in which the holder of an allowed unsecured claim objects to the confirmation of the plan—

(A) the value, as of the effective date of the plan, of the property to be distributed under the plan on account of such claim is not less than the amount of such claim; or

(B) the value of the property to be distributed under the plan is not less than the projected disposable income of the debtor (as defined in Section 1325(b)(2)) to be received during the 5-year period beginning on the date that the first payment is due under the plan, or during the period for which the plan provides payments, whichever is longer.

The new paragraph imports the disposable-income test available under Chapter 13 into Chapter 11 for individual debtors. Thus, under the amended individual-debtor confirmation requirements, a plan need not provide for full payment, or otherwise attempt to avoid operation of the absolute priority rule by satisfying the new-value exception, in order to be confirmed. An individual debtor may, instead, “commit

134 Shat, 424 B.R. at 859.
136 Landry, supra note 129, at 270.
140 Shat, 424 B.R. at 862.
141 Landry, supra note 129, at 271.
value equal to five years’ worth of earnings to the plan . . . .” 142 It follows, however, that the debtor must have some income or earnings to commit. “Debtors in many individual Chapter 11 cases have a prepetition ownership interest in a business that is their primary source of income.” 143 Some such debtors will necessarily continue to depend on their prepetition business assets to generate income. 144 Indeed, “[i]t would be ‘illogical’ to require individual debtors to devote five years of disposable income to their plans, but remove the debtors' [primary] means of providing that income.” 145 Therefore, it makes sense to read Section 1129(b)(2)(B)(ii) as eliminating the absolute priority rule and enabling individual debtors to retain their prepetition assets.

Courts that read Section 1129(b)(2)(B)(ii) as eliminating the absolute priority rule do so by relying on a broad reading (thus, the broad view) of the phrase, “included in the estate under Section 1115.” 146 Section 1115—also added by the BAPCPA amendments—provides, in part:

In a case in which the debtor is an individual, property of the estate includes, in addition to the property specified in Section 541—

(1) all property of the kind specified in Section 541 that the debtor acquires after commencement of the case . . . ; and

(2) earnings from services performed by the debtor after the commencement of the case . . . . 147

In In re Shat, the bankruptcy court persuasively explained:

Section 1115 thus defines property of the estate for an individual Chapter 11 debtor via a two-step process. Initially, Section 1115 creates a baseline estate of all the property covered by Section 541. It then adds to that one class of property excluded for other Chapter 11’s by Section 541(a)(6): postpetition income from services. 148

The phrase, “included in the estate under Section 1115,” can therefore be read broadly to “refer to all property Section 1115 itself references, and this would then be a reference to the superset of Section 541(a) property and the debtor’s postpetition service income.” 149 As a result, under the broad view an individual debtor can retain

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142 Shat, 424 B.R. at 864.
143 In re Lucarelli, 517 B.R. 42, 52 (Bankr. D. Conn. 2014).
144 Id.
146 Id. at 847.
149 Id. (emphasis omitted). The bankruptcy court further reasoned that the broad view “saves § 1129(b)(2)(B)(ii) from an almost trivial reading; if the narrow view is taken, the Section protects only the value of aggregate postpetition earnings payable after the fifth anniversary of plan confirmation.” Id. at 868.
the entirety of the bankruptcy estate as property, thus effectively abrogating the absolute priority rule in individual-debtor Chapter 11 cases.¹⁵⁰

Nevertheless, a majority of courts have rejected the notion that Congress intended to abrogate the absolute priority rule altogether, and have instead interpreted the phrase “included in the estate under Section 1115” much more narrowly (thus, the narrow view).¹⁵¹ In Zachary v. California Bank & Trust, the Ninth Circuit Court of Appeals explained:

Courts applying the narrow view . . . hold that the BAPCPA amendments merely have the effect of allowing individual Chapter 11 debtors to retain property and earnings acquired after the commencement of the case that would otherwise be excluded under Section 541(a)(6) & (7). Under this view, an individual debtor may not cram down a plan that would permit the debtor to retain prepetition property that is not excluded from the estate by Section 541, but may cram down a plan that permits the debtor to retain only postpetition property.¹⁵²

The Ninth Circuit’s reasoning in Zachary is representative of the arguments generally made in support of the narrow view.¹⁵³ The Zachary Court first held that the term “include” was best defined as “to take in.”¹⁵⁴ Thus, according to the court, Section 1129(b)(2)(b)(ii) naturally reads: the debtor may retain “property that Section 1115 takes into the estate.”¹⁵⁵ “Under this reading,” the court stated, “what Section 1115 takes into the estate is property that the debtor acquires after the commencement of the case;” property included in the estate by Section 541 is not “taken in” by Section 1115.¹⁵⁶ The court reasoned that this reading created harmony between the new individual-debtor exception and Section 1115.¹⁵⁷ Moreover, the court found that the narrow reading was supported by the history of the absolute priority rule and the Supreme Court’s express warning against finding an implied repeal of provisions of the Code—“such a major change in the existing rules would not likely have been made without specific provision in the test of the statute; it is improbable that it would have been made without even any mention in the legislative history.”¹⁵⁸ Although the court

¹⁵⁰ Id. at 865 (“Given the relatively straightforward reading of the statute supporting the broad reading, and the general rehabilitative aim of Chapter 11 . . . [the construction of § 1115] leads to the position that § 1129(B)(2)(B)(ii) extends to all property of the estate . . . . This conclusion is supported by the revisions in 2005 to bring individual Chapter 11’s more in line with Chapter 13.”).


¹⁵² Zachary v. Cal. Bank & Tr., 811 F.3d 1191, 1196 (9th Cir. 2016) (quoting In re Maharaj, 681 F.3d 558, 563 (4th Cir. 2012)) (internal quotations omitted).

¹⁵³ Salzberg & Thomas, supra note 151, at 41.

¹⁵⁴ Zachary, 811 F.3d at 1197 (citing Ice House Am., LLC v. Cardin, 751 F.3d 734, 738–39 (6th Cir. 2014)).

¹⁵⁵ Id.

¹⁵⁶ Id.

¹⁵⁷ Id. at 1198 (quoting United Sav. Ass’n of Tex. v. Timbers of Inwood Forest Assocs., Ltd., 484 U.S. 365, 380 (1988)).

¹⁵⁸ Id. at 1199.
recognized that “retaining the absolute priority rule . . . works a double whammy on [individual debtors],” the circuit court resolved that Congress could have abrogated the absolute priority rule in a far more straightforward manner if that was what Congress intended.

For example, the court reasoned, “[i]nstead of adding language to Section 1129(b)(2)(B)(ii), Congress simply could have made that provision inapplicable to individual Chapter 11 reorganizations . . . [or] raised the debt limits for Chapter 13 cases, ushering more individuals into that regime.”

Although a majority of courts have adopted the narrow view, the broad view should not be abandoned. At least one commentator has advanced salient arguments for courts to adopt the broad view, and, further, for Congress to amend the Code to abrogate the absolute priority rule for individual-debtor Chapter 11 cases in spite of the prominence of the narrow view. Lee argues that “the congruence BAPCPA created between individual debtors under Chapters 11 and 13” supports the assertion that “Congress, at least in part, desired to treat individual Chapter 11 debtors like Chapter 13 debtors.” Further, Lee concludes that “the broad view addresses individual Chapter 11 cases through the lens of common sense . . . acknowledge[ing] the symmetry Congress created between individual Chapter 11 and Chapter 13 cases . . . [and] facilitate[ing] the goals of BAPCPA by protecting consumers’ ability to retain valuable assets and therefore successfully reorganize.” Likewise, in In re O’Neal, an Arkansas bankruptcy court concluded that “since there does not appear to be any other logical reason for all of the changes made exclusively to Chapter 11 for individuals except to make it work like Chapter 13,” the broad view—abrogating the absolute priority rule in individual-debtor cases—should be adopted. Following the enactment of the Small Business Reorganization Act in August 2019, it appears even more illogical for courts to require compliance with the absolute priority rule in individual-debtor Chapter 11 cases.

III. THE SMALL BUSINESS REORGANIZATION ACT OF 2019

On August 23, 2019, President Donald Trump signed the Small Business Reorganization Act (the “SBRA”) into law, adding a new Subchapter—Subchapter V—to Chapter 11. Touted as a bipartisan measure with support from various nonpartisan organizations, the SBRA is intended to “streamline the bankruptcy process by which small businesses (sic) reorganize and rehabilitate their financial

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159 Id. (quoting Ice House Am., LLC v. Cardin, 751 F.3d 734, 740 (6th Cir. 2014)) (“[U]nder the BAPCPA amendments to § 1129(a)(15), [the debtor] ‘must dedicate at least five years’ disposable income to the payment of unsecured creditors, and—unlike a debtor in Chapter 13—is also subject to the absolute-priority rule (and thus cannot retain any pre-petition property) if he does not pay those creditors in full.’”)
160 Id.
161 Id.
163 Id. at 14.
164 Id.
affairs.”\textsuperscript{167} The push for this legislation emerged from a “consensus view among insolvency professionals . . . that the 2005 BAPCPA amendments did not ‘fix’ Chapter 11 for small businesses.”\textsuperscript{168} Indeed, both the National Bankruptcy Conference (the “NBC”) and the American Bankruptcy Institute (the “ABI”) developed recommendations to improve the reorganization process for small business debtors under Chapter 11.\textsuperscript{169} The bill ultimately enacted into law (H.R. 3311) represents a slightly revised version of a draft statute introduced by the NBC in 2010, and “the House Report on H.R. 3311 credits both the NBC and ABI recommendations as the inspiration for [the bill].”\textsuperscript{170} In order to accomplish its objective, the SBRA consists of three principal features:

(1) [R]equiring the appointment of an individual to serve as the trustee in a Chapter 11 case filed by a small business debtor . . . ; (2) requiring such private trustee to monitor the debtor’s progress toward confirmation of a reorganization plan; and (3) authorizing the court to confirm a plan over the objection of a debtor’s creditors, providing (sic) such plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan.\textsuperscript{171}

The third feature is of particular importance for the purpose of this Note. Like a general Chapter 11 case, the SBRA authorizes the bankruptcy court to confirm a plan over the objection of a debtor’s creditors, provided that,\textit{ inter alia}, the plan is fair and equitable with respect to each impaired class.\textsuperscript{172} The requirements for a cram-down confirmation under the SBRA, however, differ from Chapter 11’s general cram-down requirements. Critically, the absolute priority rule codified in Section 1129(b)(2)(B)(ii) is not replicated.\textsuperscript{173}

A. NEW ALTERNATIVE FOR INDIVIDUAL DEBTORS

“Under the SBRA, a Section 101(51D) ‘small business debtor’ that files for Chapter 11 relief has two options: (1) proceed as a Subchapter V case by affirmatively electing Subchapter V, or (2) proceed as a BAPCPA ‘small business case’ by not

\textsuperscript{169} \textit{Id.}; See, generally, ABI COMMISSION TO STUDY THE REFORM OF CHAPTER 11, \textit{FINAL REPORT AND RECOMMENDATIONS: SMALL AND MEDIUM-SIZED ENTERPRISES} (2014); NATIONAL BANKRUPTCY CONFERENCE, \textit{A PROPOSAL FOR AMENDING CHAPTER 12 TO ACCOMMODATE SMALL BUSINESS ENTERPRISES SEEKING TO REORGANIZE} (2010).
\textsuperscript{170} \textit{Id.}
\textsuperscript{171} \textit{Id.} at 4 (emphasis added).
\textsuperscript{173} Brubaker, \textit{supra} note 168, at 13–14.
electing Subchapter V.”

As Ralph Brubaker has noted, however, “given the relatively disadvantageous BAPCPA ‘small business case’ provisions, as compared to the much more advantageous provisions of Subchapter V, it can be expected that virtually all ‘small business debtors’ filing under Chapter 11 will elect to proceed under Subchapter V, rather than as a Section 101(51C) ‘small business case.’” In addition to being more advantageous for small businesses, the plan confirmation requirements under Subchapter V are also more advantageous for qualified individual debtors.

The requirements for confirmation of a plan of reorganization under Subchapter V are set out in Section 1191. Similar to Section 1129 in a general Chapter 11 case, Section 1191 provides for both consensual confirmation and non-consensual confirmation, i.e. a cram-down. “Confirmation of a consensual Subchapter V under newly enacted 1191(a) is achieved according to the same standards for and with the same effect as a confirmation [under Section 1129(a)].”

In the case of a cram-down, however, newly enacted Section 1191(b) departs substantially from Section 1129(b). Specifically, Section 1191(b) provides:

[I]f all of the applicable requirements of Section 1129(a) of this title, other than paragraphs (8), (10), and (15) of that Section, are met with respect to a plan, the court, on request of the debtor, shall confirm the plan notwithstanding the requirements of such paragraphs if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted the plan.

Section 1191(c), in turn, sets forth a rule of construction defining the requirements for a plan to be fair and equitable. Importantly, with respect to a rejecting, impaired class of unsecured creditors, a Subchapter V debtor may still confirm the plan by meeting the “best efforts requirement” set forth in Section 1191(c)(2).

(2) As of the effective date of the plan—

(A) the plan provides that all of the projected disposable income of the debtor to be received in the 3-year period, or such longer

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174 Section 101(51C) operates as a switching mechanism. If a debtor qualifies as a small business debtor under § 101(51D), then § 101(51C) triggers the mandatory application of the BAPCA small business reorganization provisions, but only if a small business debtor has not elected to proceed under Subchapter V of Chapter 11. If the Subchapter V election has been made, then the small business debtor will proceed under Subchapter V. Id. at 4.
175 Id.
177 Brubaker, supra note 168, at 12.
178 Id.
179 Id. at 14.
180 Id. at 14.
182 Brubaker, supra note 168, at 14.
period not to exceed 5 years as the court may fix, beginning on the date that the first payment is due under the plan will be applied to make payments under the plan; or 
(B) the value of the property to be distributed under the plan in the 3-year period, or such longer period not to exceed 5 years as the court may fix, beginning on the date on which the first distribution is due under the plan is not less than the projected disposable income of the debtor.\textsuperscript{183}

Brubaker has pointed out that Subchapter V’s best efforts requirement is modeled on the disposable income tests applicable in Chapters 12 and 13 and in post-BAPCPA individual-debtor Chapter 11 cases.\textsuperscript{184} However, Congress has made some important modifications pertinent to individual debtors. Recall that in an individual-debtor Chapter 11 case, the disposable income test may be impracticable in jurisdictions adhering to the narrow view where application of the absolute priority rule prevents the debtor from retaining an interest in prepetition assets. In enacting Subchapter V, Congress clearly recognized the difficulty that the absolute priority rule caused small businesses (and, by extension, individuals) attempting to reorganize under Chapter 11. Indeed, Congress eliminated the rule entirely—it is simply not replicated in Section 1191(c)(2).\textsuperscript{185} As a result, “Subchapter V’s replacement of the . . . absolute priority rule with a best-efforts requirement will enable small business debtors [and individuals] to more easily reorganize under Chapter 11 without losing ownership and control of their businesses.”\textsuperscript{186}

While it is a step in the right direction that the SBRA will enable some individual debtors to avoid the absolute priority rule by electing to proceed under Subchapter V, the SBRA is only available to individual debtors that qualify for small business debtor

\textsuperscript{183} Pub. L. No. 116-54, 133 Stat. 1079, 1082 (2019) (enacting 11 U.S.C. § 1191). Section 1191(c) also defines disposable income:

(d) Disposable income.--For purposes of this Section, the term “disposable income” means the income that is received by the debtor and that is not reasonably necessary to be expended—

(1) for--

(A) the maintenance or support of the debtor or a dependent of the debtor; or

(B) a domestic support obligation that first becomes payable after the date of the filing of the petition; or

(2) for the payment of expenditures necessary for the continuation, preservation, or operation of the business of the debtor. \textit{Id.}

\textsuperscript{184} Brubaker, \textit{supra} note 168, at 14.


\textsuperscript{186} Brubaker, \textit{supra} note 168, at 17; \textit{See also} Brian Gifford, \textit{Chapter 11’s Double Whammy on Individual Debtors}, AM. BANKR. INST., J., Oct. 2019, at 16, 75 (“This change harkens back to the days when Congress declined to adopt the absolute priority rule in Chapter XI of the Bankruptcy Act, which was a remedy for small, privately held businesses. According to the legislative history of the1952 amendments to the Act, ‘the fair and equitable requirement . . . cannot realistically be applied,’ because if it were, ‘no individual debtor and . . . no corporate debtor where the stock ownership is substantially identical with management could effectuate an arrangement except by payment of the claims of all creditors in full.’”).
status. The Code, as amended by the SBRA, defines “small business debtor” as “a person engaged in commercial or business activities . . . that has aggregate noncontingent liquidated and unsecured debts . . . in an amount not more than $2,725,625 . . . not less than fifty percent of which arose from the commercial or business activities of the debtor . . . .” Consequently, not all individual debtors will qualify as a small business debtor. In fact, according to one calculation, between 2008 and 2018, only about twenty-five percent of individual cases would have qualified for the small-business-debtor election. Consequently, in the majority of jurisdictions that adhere to the narrow view of Section 1129(b)(2)(B)(ii)’s individual-debtor exception, the resulting statutory scheme for reorganizing individual debtors will become even more absurd. Individual debtors who qualify for Chapter 13, as well as individual debtors who exceed the Chapter 13 debt limitation but otherwise qualify as small business debtors under Subchapter V, can retain prepetition business assets to fund a plan of reorganization. Individual debtors who exceed the debt limitations of both Chapter 13 and Subchapter V, on the other hand, are left to suffer the implications of the absolute priority rule.

IV. RECONSIDERING THE “BROAD VIEW” APPROACH

In In re Summers, the debtor, James Summers (“Summers”) reported unsecured debt totaling $450,479.00—exceeding Chapter 13’s unsecured debt limitation. Instead of choosing to liquidate his assets under Chapter 7, Summers filed a voluntary individual-debtor Chapter 11 petition, and, subsequently, a plan of reorganization. The plan impaired both of the two classes of unsecured claims, yet provided that Class 9—Summers’s own interest in his property—would be unimpaired. Consequently, one of the classes of unsecured creditors voted to reject the plan based on the fact that the plan violated the absolute priority rule. The bankruptcy court denied confirmation of Summers’s plan, holding that under the narrow view of Section 1129(b)(2)(B)(ii)’s individual-debtor exception, the absolute priority rule continues to apply to the pre-petition property defined by Section 541. Curiously, however, had the SBRA been effective at the time Summers filed his petition, he likely would have been eligible as a small business debtor to take advantage of Subchapter V (assuming Summers otherwise met all of the other requirements, his debts did not exceed Subchapter V’s limitation). Had Summers been able to elect to proceed under

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190 In re Summers, 594 B.R. 707, 708 (Bankr. D. Colo. 2018) (“An individual debtor is ineligible for relief under Chapter 13 if such debtor’s secured debts exceed $1,184,200.00 or unsecured debts exceed $394,725.00.”).
191 Id.
192 Id.
193 Id.
194 Id. at 711.
Subchapter V rather than the traditional individual-debtor provisions he likely would have found it to be an advantageous alternative: the absolute priority rule would be inapplicable and the best-efforts requirement would be much less rigorous.\textsuperscript{195} It is unclear why an individual debtor who is eligible for Chapter 13 or Subchapter V should have the advantage of being able to retain pre-petition property, but an individual debtor with debts slightly exceeding the debt limitation of Subchapter V should still have to contend with the absolute priority rule.

Of course, as one commentator has explained, the debt limit for SBRA eligibility will very likely increase sometime in the future.\textsuperscript{196} “The reality is that, as with Chapter 12, Congress is establishing a baseline from which to measure the SBRA’s impact . . . . It is hoped that the recommendations of ABI ($10 million) or the National Bankruptcy Conference ($7.5 million) will be considered in the near future,”\textsuperscript{197} But in the meantime the absolute priority rule will continue to serve as an impediment to the overwhelming majority of individual-debtors that will not be eligible to proceed under Subchapter V when it becomes effective in February 2020. Courts should, therefore, reconsider the broad view of Section 1129(b)(2)(B)(ii)’s individual-debtor exception.

Not only is the broad view supported by a logical, plain meaning interpretation of the statute, but it is more sensible and responsive toward achieving a successful reorganization in individual-debtor Chapter 11 cases. Indeed, Congress evidently understands that abrogating the absolute priority rule is a key component of enabling small business and individual debtors to more easily reorganize under Chapter 11 without losing ownership and control of their businesses. This is quite clear under the SBRA, and, at least in the view of some courts, was apparent when Congress enacted the BAPCPA amendments. As the courts have said repeatedly, “statutory language cannot be construed in a vacuum. It is a fundamental canon of statutory construction that the words of a statute be read in their context and with a view to their place in the overall statutory scheme.”\textsuperscript{198} Subchapter V, as added by the SBRA, is largely modeled after Chapter 12 and 13. Likewise, most of the changes effected by BAPCPA in individual-debtor Chapter 11 cases were part of an overall design of adapting various Chapter 13 provisions to fit Chapter 11. The common thread in these changes is the goal of making it easier for small businesses and individuals to reorganize under Chapter 11. The narrow view ignores this goal and renders Section 1129(b)(2)(B)(ii) wholly inconsistent with the overall statutory scheme merely because courts adhering to this view refuse to believe that Congress would eliminate the absolute priority rule in such a convoluted way. Yet, Congress’s intent to eliminate the absolute priority rule is unambiguous under Subchapter V. Given the similarity of objectives between the BAPCPA amendments and the SBRA, eliminating the absolute priority rule in traditional individual-debtor Chapter 11 cases through adoption of the broad view is certainly deserving of reconsideration by the courts.

\textsuperscript{195} Brubaker, supra note 168, at 18.
\textsuperscript{196} Donald L. Swanson, SBRA: Frequently Asked Questions and Some Answers, AM. BANKR. INST. J., Nov. 2019, at 8, 77.
\textsuperscript{197} Id.
\textsuperscript{198} Id.
CONCLUSION

In light of the recent enactment of the Small Business Reorganization Act, which eliminates the absolute priority rule, courts should reconsider the broad view of Section 1129(b)(2)(B)(ii)’s individual-debtor exception. The enactment of the SBRA, which seeks to facilitate more successful reorganizations, reinforces the importance of eliminating the absolute priority rule in traditional individual-debtor Chapter 11 cases if such debtors are to successfully reorganize. Therefore, courts should consider the SBRA when interpreting Section 1129(b)(2)(B)(ii) and adopt the more sensible broad view, thereby abrogating the absolute priority rule.