

BANKRUPTCY:
TRENDS AND CHARACTERISTICS WITH SPECIAL
EMPHASIS ON THE WAGE EARNER'S PLAN

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I. Introduction.

A. Comments on Bankruptcy Statistics for 1972.

Much of the growing interest in bankruptcy, no doubt, reflects the long-term trend toward increased bankruptcy filings, as revealed in current bankruptcy statistics. But in the last five years there has been a decrease in the total number of bankruptcy cases filed in three of those years. A total of 182,869 bankruptcy cases were filed in the fiscal year 1972. This is a decline of 18,483 cases, or 9%, below the total of 201,352 cases filed in 1971.¹ In the 1970's, there were only two other declines in the total number of cases filed, and they were in 1968 and 1969. A decline of 10,518 cases, or 5%, were recorded in 1968 below the all-time high of 208,329 cases filed in 1967. A decline of 12,881 cases, or 6%, were recorded in 1969 below the total of 197,811 cases filed in 1968. In only one other year since World War II has there been a decline below the preceding year. The prior occasion was in 1952 during the Korean conflict.² The following table on page 1a shows the total number of bankruptcy cases filed for each year beginning with 1900. Page 1b contains a graphic view of the total cases filed.

II. Some General Information Concerning Bankruptcy.

B. Bankruptcy Laws in the United States.

¹"Bankruptcies Drop in Number," Credit and Financial Management, September, 1971, p. 32.

²"Bankruptcies Show a Decline," Credit and Financial Management, July, 1969, p. 14.

**TOTAL FILINGS OF ALL TYPES OF BANKRUPTCY
CASES BY FISCAL YEARS ENDING JUNE 30. OF
EACH YEAR FROM 1900 THRU JUNE 30, 1972**

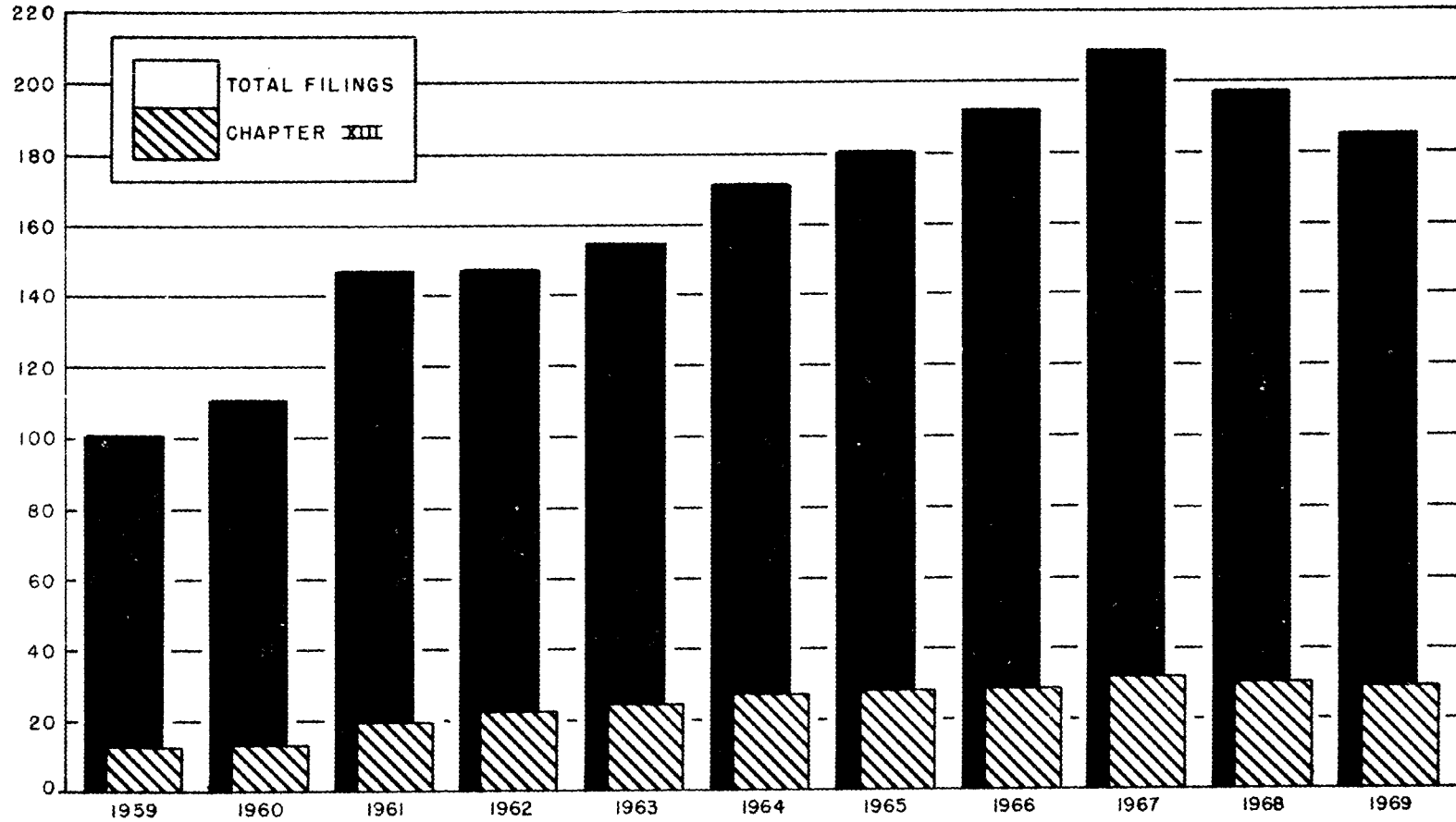
<u>Fiscal Year</u>		<u>Fiscal Year</u>	
1900	21,938	1936	60,624
1901	19,007	1937	57,485
1902	18,482	1938	57,306
1903	16,875	1939	50,997
1904	17,082	1940	52,577
1905	16,946	1941	56,332
1906	12,972	1942	52,109
1907	14,160	1943	34,711
1908	17,818	1944	19,533
1909	18,018	1945	12,862
1910	18,053	1946	10,196
1911	19,338	1947	13,170
1912	19,745	1948	18,510
1913	20,930	1949	26,021
1914	22,959	1950	33,392
1915	27,632	1951	35,193
1916	27,368	1952	34,873
1917	24,838	1953	40,087
1918	20,385	1954	53,136
1919	14,048	1955	59,404
1920	13,558	1956	62,086
1921	22,812	1957	73,761
1922	38,165	1958	91,668
1923	41,304	1959	100,672
1924	43,519	1960	110,034
1925	45,641	1961	146,643
1926	46,374	1962	147,780
1927	48,758	1963	155,493
1928	53,064	1964	171,719
1929	57,280	1965	180,323
1930	62,845	1966	192,354
1931	65,335	1967	208,329
1932	70,049	1968	197,811
1933	62,256	1969	184,930
1934	58,888	1970	194,399
1935	69,153	1971	201,352
		1972	182,869

DISTRICT COURTS

BANKRUPTCY CASES COMMENCED

FISCAL YEARS 1959 - 1969

THOUSANDS



Source: Administrative Office of the United States Courts

The framers of the Constitution of the United States gave the federal government the right to regulate and control bankruptcies. This power was first exercised in 1800, when Congress passed a bankruptcy act.³ Under the constitutional provision that Congress shall have the power to establish "uniform laws on the subject of bankruptcies throughout the United States" (Article 1, Section 8), four national bankruptcy laws have been enacted. The fourth, and present, bankruptcy law was passed July 1, 1898. The Bankruptcy Act has been amended a number of times since it was first enacted, but its general plan has not been changed by the amendments. In 1938, the Chandler Act was enacted providing several relief measures to debtors as alternatives to straight bankruptcy.⁴ This paper, however, will deal primarily with straight bankruptcy (with the exception of Chapters XI and XIII of the Bankruptcy Act).

C. Purpose and Scope of the Bankruptcy Act.

The purpose of the Bankruptcy Act is (1) to protect creditors from one another, (2) to protect creditors from their debtors, and (3) to protect the honest debtor from his creditors. To accomplish these objectives, the main concern of bankruptcy is to grant to the honest debtor who is overwhelmed by his debts a chance to make a fresh start in life and remain a useful member of society by relieving him of the oppressive burden of his debts.

³Harold F. Lusk, Charles Hewitt, John D. Donnell, and A. James Barnes, Business Law Principles and Cases, (Richard D. Irwin, Inc., Homewood, Illinois), 1970, p. 992.

⁴Ibid., p. 992.

As a condition for receiving a discharge in bankruptcy, however, the debtor must turn over to the bankruptcy court all property which he owns which is not exempt by federal or state law. This property is converted into money and is used to pay costs of administration and creditors to the extent possible. Usually there is so little money realized, that creditors receive only a small fraction or none of the money owed to them.⁵

D. An Attorney in a Bankruptcy Case.

An individual contemplating bankruptcy normally will require the services of an attorney. He needs an attorney to: (1) advise him whether bankruptcy or some alternative form of relief is the best solution to his financial problems and, if so; (2) prepare the necessary legal papers incident to filing bankruptcy; and (3) represent him during the course of the bankruptcy proceedings.⁶ The legal fees charged by an attorney to represent his client in the average individual (as distinguished from business) bankruptcy proceeding ordinarily will run between \$200 and \$250. In some urban localities, the charges may be somewhat higher. If a person encounters difficulty in securing the services of an attorney, he may be able to obtain a list of names of attorneys who accept bankruptcy cases from the Bar Association or Legal Aid Society serving the area in which he lives.

⁵George Allen Brunner, Personal Bankruptcies: Trends and Characteristics, (Columbus Bureau of Business Research, Columbus, Ohio), 1969, p. 80.

⁶David T. Stanley, Bankruptcy: Problem, Process, Reform, (Brookings Institute, Washington), 1971, p. 200.

E. Voluntary and Involuntary Bankruptcy Proceedings.

An individual may be adjudicated a bankrupt either voluntarily or involuntarily. Since most bankruptcies are voluntary, the information contained herein is primarily applicable to the individual who voluntarily is seeking a discharge in bankruptcy from the bankruptcy court.⁷

An individual voluntarily seeking to be adjudicated a bankrupt must meet certain conditions. He must owe one or more debts, although there is no minimum or maximum as to the amount of debts which he must owe. There is no requirement that the individual be insolvent. Normally, however, the individual seeking a discharge in bankruptcy is either insolvent, that is his liabilities exceed his assets, or unable to pay his debts as they accrue.⁸ He cannot file a petition to be adjudicated a bankrupt for the purpose of perpetuating a fraud. In addition, he may not file for bankruptcy if he previously has been adjudicated a bankrupt within six years.

In involuntary bankruptcy cases a debtor may, if he has committed an act of bankruptcy, be adjudged an involuntary bankrupt on the petition of his creditors. Under the provisions of the Bankruptcy Act an involuntary petition may be filed against any natural person, except a wage earner or farmer, and any moneyed, business, or commercial corporation, except a building and loan

⁷Lusk, p. 993.

⁸H. Lee Mathews, Causes of Personal Bankruptcies, (Bureau of Business Research, Ohio State University, Columbus, Ohio), 1969, p. 80.

association, a municipal, railroad, insurance, or banking corporation, owing debts amounting to \$1,000 or more and having committed an act of bankruptcy within four months before the filing of the petition.⁹ The following table on page 5a shows the total number of bankruptcy cases filed by class, including both business and non-business. Page 5b contains a graphic view of business and non-business bankruptcy cases filed.

F. Filing a Petition For Bankruptcy.

Bankruptcy begins with the filing of a petition to be adjudged a bankrupt with the Clerk of the United States District Court serving the area in which the individual has lived for the past six months prior to filing or for a longer portion of the preceding six months than in any other jurisdiction. A \$50 filing fee must be paid to the Clerk at the time the petition is filed. This fee is in addition to the fees charged by the attorney for his services. The Bankruptcy Act permits filing fees to be paid in short installments during the progress of the case but, in the event of default, the case will be dismissed or the bankrupt denied a discharge.¹⁰ The following table on page 5c shows all the bankruptcy cases commenced and terminated by districts from July, 1970, to June, 1971.

In addition to the petition, the bankrupt must also file with the Clerk of Court a schedule of all his debts and a list

⁹Lusk, p. 993.

¹⁰Samuel Whitney Dunscomb, Bankruptcy: A Study in Comparative Legislation, (Ams Press, New York), 1969, p. 123.

BANKRUPTCY FILINGS BY CLASS

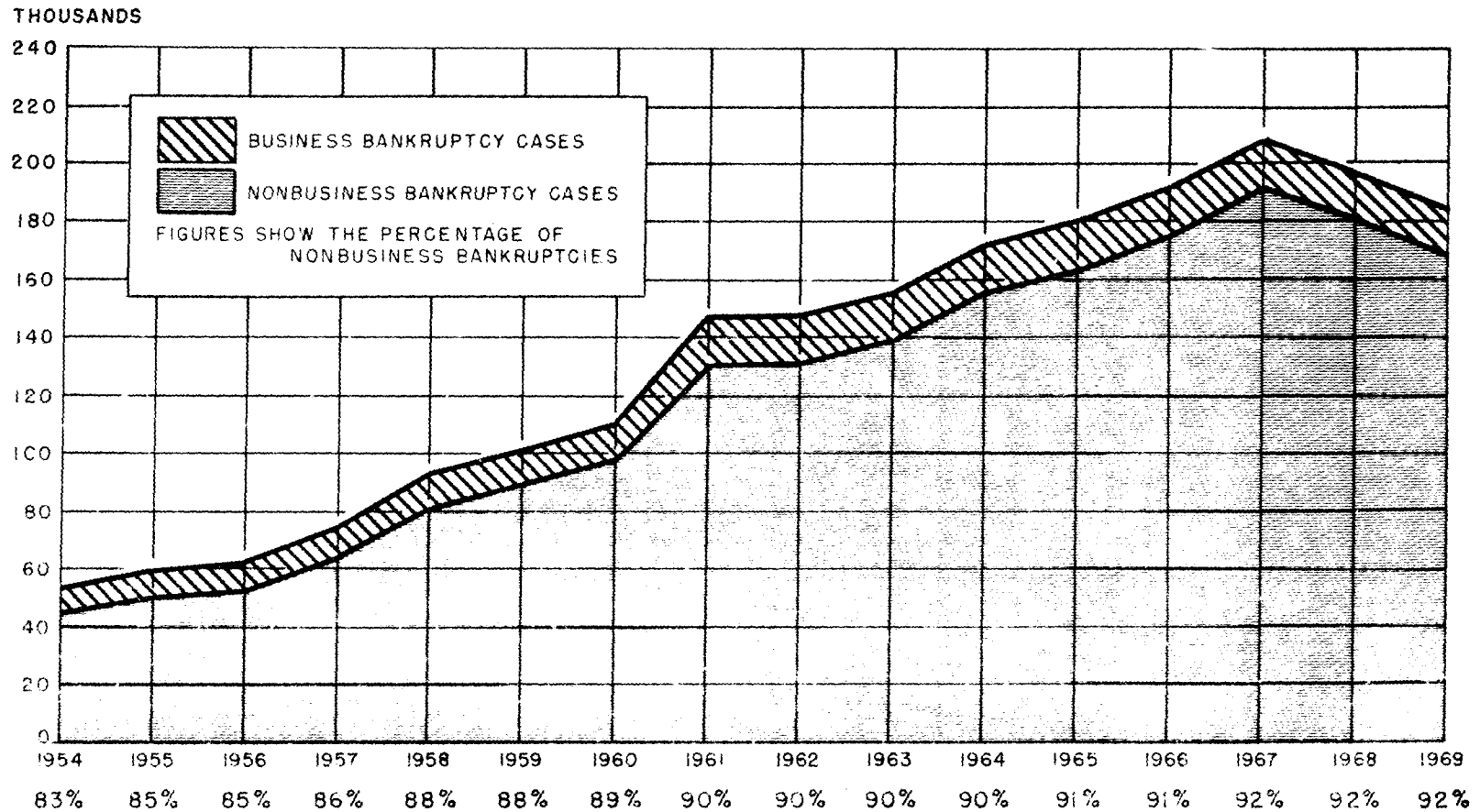
<u>Fiscal Year</u>	<u>Chapter XIII</u>	<u>Employee</u>	<u>Non-Business</u>	<u>Business</u>	<u>Total Bkcy Case Filings</u>
1939	1,639*				50,997*
1940	3,260	36,843	39,073	13,248	52,577
1941	4,433	42,348	44,713	11,619	56,335
1942	4,100	40,180	42,251	9,858	52,109
1943	2,007	27,020	28,782	5,929	34,711
1944	1,249	15,460	16,752	2,781	19,533
1945	1,248	10,010	11,051	1,811	12,862
1946	1,371	7,618	8,566	1,630	10,196
1947	2,354	9,396	10,234	2,936	13,170
1948	3,351	12,546	13,537	4,973	18,510
1949	5,111	17,772	19,144	6,877	26,021
1950	6,007	22,933	25,040	8,352	33,392
1951	6,924	25,984	27,806	7,387	35,193
1952	7,397	26,527	28,331	6,542	34,873
1953	8,670	31,253	33,315	6,772	40,087
1954	9,634	40,889	44,248	8,888	53,136
1955	9,864	46,163	50,219	9,185	59,404
1956	9,535	48,784	52,608	9,478	62,086
1957	11,549	59,053	63,617	10,144	73,761
1958	13,391	73,379	80,265	11,403	91,668
1959	12,993	81,516	88,943	11,729	100,672
1960	13,599	89,639	97,750	12,284	110,034
1961	19,723	119,117	131,402	15,241	146,643
1962	22,880	120,742	132,125	15,655	147,780
1963	24,329	127,156	139,190	16,303	155,493
1964	27,292	141,550	155,209	16,510	171,719
1965	28,027	148,965	163,413	16,910	180,323
1966	28,261	160,299	175,924	16,430	192,354
1967	31,963	174,205	191,729	16,600	208,329
1968	31,065	162,879	181,266	16,545	197,811
1969	28,910	150,235	169,500	15,430	184,930
1970	30,510	156,397	178,202	16,197	194,399
1971	30,904	156,143	182,249	19,103	201,352
1972	27,373	139,466	164,737	18,132	182,869

* From Attorney General's Report

DISTRICT COURTS

BUSINESS AND NONBUSINESS BANKRUPTCY CASES COMMENCED

FISCAL YEARS 1954-1969



Source: Administrative Office of the United States Courts

Table F 1. United States District Courts
 Bankruptcy Cases Commenced and Terminated During the Fiscal Year
 Ended June 30, 1971, by District

Circuit and District	Pending July 1, 1970	Commenced	Terminated	Pending June 30, 1971
TOTAL ALL DISTRICTS.....	190,627	201,352	190,609	201,370
District of Columbia.....	208	140	168	180
First Circuit.....	7,048	4,685	4,422	7,311
Maine.....	4,188	1,540	1,995	3,733
Massachusetts.....	1,897	1,951	1,349	2,499
New Hampshire.....	312	550	570	292
Rhode Island.....	434	527	498	463
Puerto Rico.....	217	117	10	324
Second Circuit.....	7,854	9,489	6,821	10,522
Connecticut.....	1,032	1,641	1,194	1,479
New York:				
Northern.....	1,776	2,336	1,829	2,283
Eastern.....	1,525	1,306	1,160	1,671
Southern.....	1,428	1,208	879	1,757
Western.....	1,995	2,656	1,415	3,236
Vermont.....	96	342	344	96
Third Circuit.....	3,758	3,798	3,161	4,395
Delaware.....	68	105	92	81
New Jersey.....	2,026	1,596	1,515	2,107
Pennsylvania:				
Eastern.....	824	934	564	1,194
Middle.....	250	374	314	310
Western.....	579	783	676	686
Virgin Islands.....	11	6	-	17
Fourth Circuit.....	7,719	9,636	7,773	9,582
Maryland.....	564	575	345	794
North Carolina:				
Eastern.....	179	274	185	268
Middle.....	861	962	128	1,695
Western.....	111	105	85	131
South Carolina.....	206	267	251	222
Virginia:				
Eastern.....	1,450	3,490	3,344	1,596
Western.....	3,276	2,280	1,878	3,678
West Virginia:				
Northern.....	546	603	560	589
Southern.....	526	1,080	997	609
Fifth Circuit.....	28,267	28,327	25,661	30,933
Alabama:				
Northern.....	9,258	5,930	6,244	8,944
Middle.....	2,671	1,742	1,755	2,658
Southern.....	2,576	1,660	1,782	2,454
Florida:				
Northern.....	107	151	117	141
Middle.....	635	1,449	1,106	978
Southern.....	672	669	225	1,116
Georgia:				
Northern.....	2,500	4,384	3,889	2,995
Middle.....	2,436	2,114	1,926	2,624
Southern.....	1,874	1,180	1,245	1,809
Louisiana:				
Eastern.....	1,179	2,792	2,296	1,675
Western.....	1,715	2,383	2,130	1,968
Mississippi:				
Northern.....	229	380	371	238
Southern.....	420	1,046	836	630
Texas:				
Northern.....	923	1,217	769	1,371
Eastern.....	128	116	108	136
Southern.....	452	487	339	600
Western.....	492	627	523	596

Table F 1. United States District Courts

Bankruptcy Cases Commenced and Terminated During the Fiscal Year
 Ended June 30, 1971, by District - Concluded

Circuit and District	Pending July 1, 1970	Commenced	Terminated	Pending June 30, 1971
Sixth Circuit.....	37,455	37,462	37,784	37,133
Kentucky:				
Eastern.....	1,880	1,647	1,579	1,948
Western.....	3,618	3,770	3,665	3,723
Michigan:				
Eastern.....	5,782	4,950	4,553	6,179
Western.....	1,993	1,792	1,672	2,113
Ohio:				
Northern.....	7,612	8,351	7,971	7,992
Southern.....	7,440	9,005	9,338	7,107
Tennessee:				
Eastern.....	3,117	2,974	3,297	2,794
Middle.....	1,782	2,423	2,537	1,668
Western.....	4,231	2,550	3,172	3,609
Seventh Circuit.....	14,001	25,525	23,766	15,760
Illinois:				
Northern.....	3,932	8,984	8,060	4,856
Eastern.....	1,205	1,290	1,249	1,246
Southern.....	2,715	3,121	2,857	2,979
Indiana:				
Northern.....	1,108	2,718	2,873	953
Southern.....	1,500	5,390	4,977	1,913
Wisconsin:				
Eastern.....	2,410	2,671	2,501	2,580
Western.....	1,131	1,351	1,249	1,233
Eighth Circuit.....	15,093	15,541	14,726	15,908
Arkansas:				
Eastern.....	1,926	933	1,113	1,746
Western.....	274	236	240	270
Iowa:				
Northern.....	1,017	1,501	1,261	1,257
Southern.....	1,359	1,639	1,497	1,501
Minnesota.....	5,202	3,240	3,148	5,294
Missouri:				
Eastern.....	2,911	2,581	2,765	2,727
Western.....	1,382	3,154	2,698	1,838
Nebraska.....	671	1,675	1,483	863
North Dakota.....	247	282	262	267
South Dakota.....	104	300	259	145
Ninth Circuit.....	53,411	51,150	50,936	53,625
Alaska.....	127	204	166	165
Arizona.....	3,126	3,057	2,825	3,358
California:				
Northern.....	12,306	8,330	8,329	12,307
Eastern.....	9,610	5,455	7,357	7,708
Central.....	14,737	18,660	17,063	16,334
Southern.....	2,943	2,609	2,529	3,023
Hawaii.....	385	384	402	367
Idaho.....	1,155	989	1,030	1,114
Montana.....	722	962	881	803
Nevada.....	1,164	1,448	1,242	1,370
Oregon.....	2,965	4,208	4,496	2,677
Washington:				
Eastern.....	708	1,077	776	1,009
Western.....	3,458	3,759	3,839	3,378
Guam.....	5	8	1	12
Tenth Circuit.....	15,813	15,599	15,391	16,021
Colorado.....	4,999	3,999	3,504	5,494
Kansas.....	6,553	4,597	5,294	5,856
New Mexico.....	675	1,628	1,441	862
Oklahoma:				
Northern.....	1,011	1,362	1,357	1,016
Eastern.....	126	251	227	150
Western.....	615	1,861	1,828	648
Utah.....	1,245	1,354	1,397	1,202
Wyoming.....	589	547	343	793

of all his creditors, (Schedule A), including their addresses if known. He must also file a Schedule B, which is a detailed list of all property he owns, including monies owed to him, property which he may inherit within six months, and insurance policies which he holds. He also must list on Schedule B all property owned by him which he claims as being exempt under state law.¹¹ At least five days prior to the first meeting of creditors, the bankrupt must also prepare and file with the court a detailed statement of his financial affairs. There are prescribed legal forms for all of these requirements. The bankrupt's attorney will normally provide for and prepare these forms based on information furnished by the bankrupt. These forms may be obtained by anyone, however, at nominal cost from a stationery store which stocks legal forms.

The simple act of filing a petition in bankruptcy has far-reaching significance. On the date that the petition is filed, the debtor is automatically adjudicated a bankrupt.¹² The petition itself serves as the application for discharge without further action on the part of the bankrupt. On this date title to all property owned by the bankrupt which is not exempt by federal or state law automatically passes under the Bankruptcy Act to the trustee who subsequently will be elected or appointed to liquidate the bankrupt's estate for the benefit of creditors. Although the

¹¹The New York Times, January 31, 1972, p. 6.

¹²J. Stutman, "What's New in Bankruptcy and What's Not so New," Journal of Commercial Bank Lending, February, 1972, p. 19.

Bankruptcy Act is a federal law, the exemptions of the bankrupt and the rights of creditors to repossess mortgaged property are determined by state law. Consequently, the property which a bankrupt may claim as exempt and the rights of creditors to recover mortgaged property possessed by the bankrupt vary from state to state.¹³

G. Administration of the Bankrupt's Estate - The Referee and Trustee.

When a petition is filed in bankruptcy, it is normally automatically referred to a referee in bankruptcy. The referee in bankruptcy is a federal judicial officer who is a specialist in bankruptcy matters. He acts as a judge in presiding over the bankruptcy proceeding and determines whether the petitioner is entitled to a discharge in bankruptcy.¹⁴

The usual chronology of events in a bankruptcy proceeding is discussed in the following paragraphs. As previously noted, a voluntary bankruptcy proceeding begins with the filing of a petition to be adjudged a bankrupt. When the petition together with supporting schedules previously mentioned are referred to the referee, the referee calls a first meeting of all creditors listed on the schedule and notifies them by mail that they may attend this meeting, file their claims, elect a trustee, and examine (question) the bankrupt who must take the witness stand.¹⁵

¹³Brunner, p. 21.

¹⁴"Referee in Bankruptcy - Mr, Master or Judge?" Credit and Financial Management, August, 1970, p. 13.

¹⁵Stanley, p. 190.

The referee also notifies creditors that if they have a valid objection to the bankrupt receiving a discharge, they must file a formal written objection within thirty days. The first meeting of creditors is usually held from two to four weeks after the date the petition is filed.

At the first meeting of creditors, the bankrupt is questioned under oath by the referee and by any interested creditors who so desire. The bankrupt must be completely truthful and cooperative in answering questions concerning his financial status. Normally, at the first meeting of creditors, a trustee is either elected by creditors or, if no election is made, appointed by the referee.¹⁶ The trustee is a bonded officer of the court and is given title to all property owned by the bankrupt which is not exempt by law. The trustee, under the supervision of the referee, takes possession of all property owned by the bankrupt which is not exempt; converts such property into money by selling it; and, on order of the referee, after costs of administration have been paid (which average 25% of the value of the estate), distributes dividends to creditors to the extent money is available.

To protect the interests of the creditors, the trustee in bankruptcy is given the right to bring suit in any court in which the bankrupt could have brought suit to enforce claims of the bankrupt's estate. Such suits are brought in the name of the trustee.¹⁷ All such suits are brought under the supervision of

¹⁶"Referee in Bankruptcy - Mr, Master or Judge?" p. 14.

¹⁷Mathews, p. 81.

the court in which the bankruptcy proceedings are pending. Also, the trustee owes a duty to defend all suits brought against the bankrupt's estate.

Creditors must file their claims with the referee within six months of the first date set for the first meeting of creditors or be barred from participating in any dividend which might be declared.¹⁸ There is a prescribed form for submitting proofs of claim which may be obtained from any stationery store which stocks legal forms.

H. Basis For Granting a Discharge.

If there are no objections to the discharge filed, the referee will grant the bankrupt a discharge. A bankrupt is granted a discharge unless he has been guilty of a serious infraction of the code of business ethics or has failed to fulfill his duties as a bankrupt. The time for filing the objections to a bankrupt's discharge is fixed at the first meeting of creditors or at a special meeting called for that purpose.¹⁹

The discharge in bankruptcy relieves the bankrupt from legal liability for the payment of all provable debts owed at the time of bankruptcy with certain exceptions which are discussed below. If a creditor has a mortgage or lien on the bankrupt's property, such as a house, car, or furniture, the trustee will determine whether the bankrupt has any interest or equity in the property

¹⁸E. T. Sivertsen, "How To Prevent Credit Frauds," Credit and Financial Management, October, 1967, p. 30.

¹⁹Lusk, p. 1003.

over and above the amount of the mortgage or lien. If the trustee believes that the bankrupt has some equity in the property, he will sell it and pay off the mortgage or lien. If the trustee feels that the bankrupt has no equity in the property, the secured creditor will be permitted to foreclose his security, that is repossess the property, by separate action in a state or county court.²⁰ In the latter event, any deficiency which the secured creditor suffers as the result of the foreclosures can be claimed as an unsecured debt. The following Pie Chart on page 10a shows the distribution of assets to creditors with special emphasis on secured and unsecured creditors.

I. Priority of Claims of Certain Creditors.

After all assets have been sold, a final meeting of creditors is held in which the trustee reports to the court what he has done. The referee then orders the costs of the proceeding to be paid and declares a dividend of the balance, if any, to creditors who have filed claims. The Bankruptcy Act gives claims of certain creditors priority in payment over the claims of other creditors. These priority debts must be paid in full before any dividends may be declared and paid to the general creditors.²¹ The following debts are given priority by the Bankruptcy Act and

²⁰P. B. Chabrow, "Estates in Bankruptcy; Return Requirements, Rules Concerning Income and Deductions," Journal of Taxation, December, 1969, p. 365.

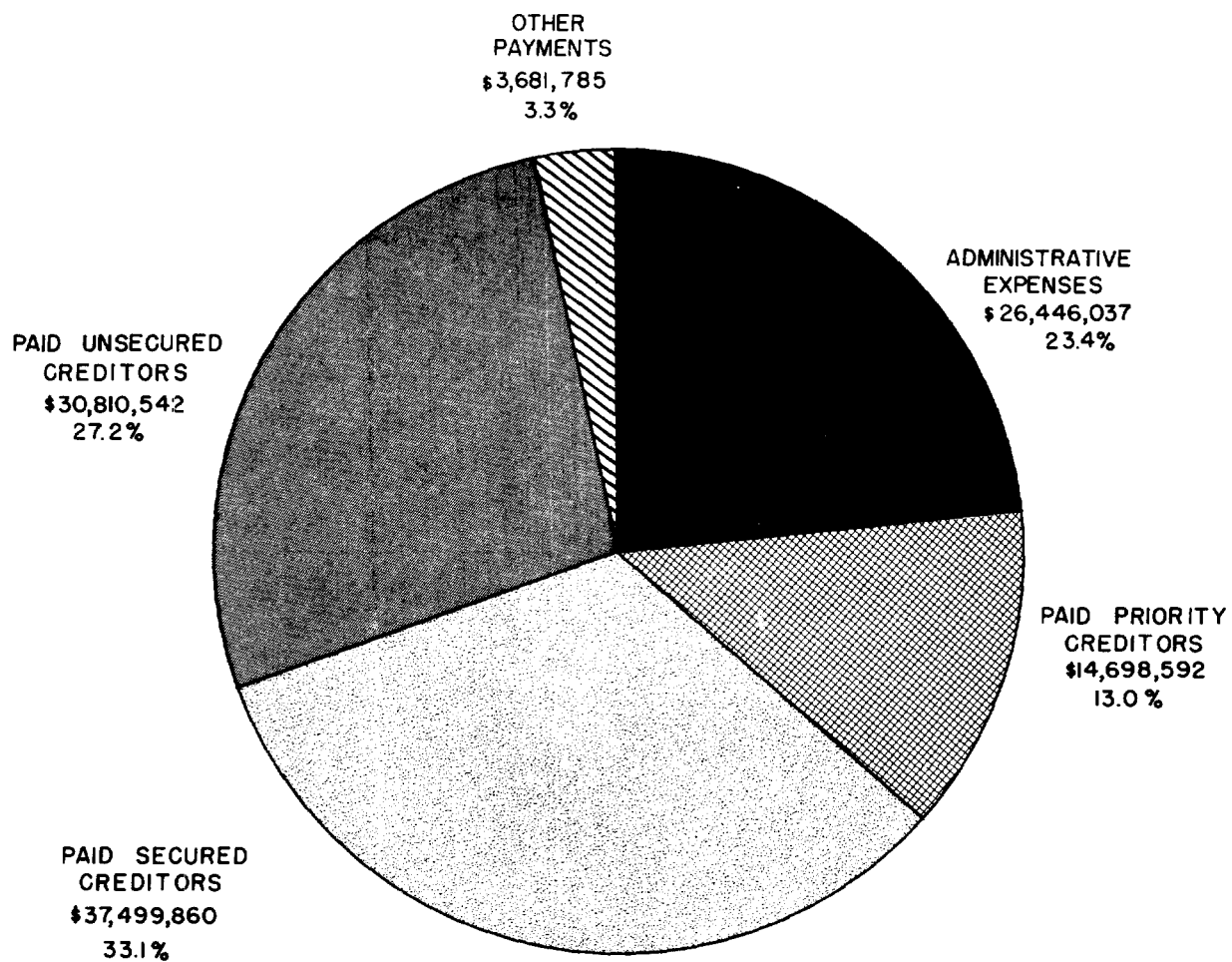
²¹W. T. Plumb, "Relative Priority of Claims of Workingmen and of the Federal Government in Insolvency," Labor Law Journal, May, 1972, p. 260.

DISTRICT COURTS

DISTRIBUTION OF TOTAL REALIZATION
IN ASSET CASES

FISCAL YEAR 1969

TOTAL REALIZATION \$113,136,826



Source: Administrative Office of the United States Courts

are paid in the order listed:

- (1) The actual and necessary cost of preserving the estate subsequent to filing the petition.
- (2) The filing fees paid by creditors in involuntary proceedings, and the reasonable expenses of recovering transferred and concealed property.
- (3) The cost of administration, including fees and mileage payable to witnesses, and reasonable fees to one attorney for services actually rendered to the petitioning creditors in involuntary cases, and to the bankrupt in voluntary cases, as the court may allow.
- (4) Wages due to workmen or other employees which have been earned within 3 months prior to the date of the commencement of proceedings, not exceeding \$600 to each claimant.
- (5) Reasonable expenses incurred by creditors in opposing the confirmation of an arrangement or wage earners plan.
- (6) All taxes due to the United States, the state, county, district, or municipality.
- (7) Debts owing to any person who by the laws of the states or the United States is entitled to priority.²²

If no assets have been recovered, there will be no final meeting of creditors. Normally, it is not necessary that the bankrupt attend this meeting. By this time, he has probably received his discharge in bankruptcy. The court may, however, revoke

²²Brunner, p. 58.

a discharge if information is brought to its attention within one year after the discharge was granted showing that the bankrupt was guilty of fraud or the actual facts did not warrant the discharge.²³

J. Dischargeable Debts.

Certain debts are not affected by the bankrupt's discharge. Section 17 of the Bankruptcy Act provides that a discharge in bankruptcy shall release a bankrupt from all his provable debts, whether allowable in full or in part, except those that are:

- (1) due as a tax levied by the United States, or any state, county, district, or municipality.
- (2) liabilities for obtaining money or property by false pretense or false representations.
- (3) having not been duly scheduled in time for proof and an allowance, with the name of the creditor, if known to the bankrupt, unless such creditor had notice or actual knowledge of the proceedings in bankruptcy.
- (4) were created by his fraud, embezzlement, misappropriation, or defalcation while acting as an officer or in any fiduciary capacity.
- (5) are for wages which have been earned within three months before the date of commencement of the proceedings in bankruptcy due to workmen, servants, clerks or city salesmen.
- (6) are due for monies of an employee received or retained

²³Ibid., p. 59.

by his employer to secure the faithful performance by such employee of the terms of a contract of employment.²⁴

The debts just listed are provable debts, and the owner of such a debt has the right to participate in the distribution of the bankrupt's estate; but his right to recover the unpaid balance of the debt is not cut off by the bankrupt's discharge.²⁵ All provable debts except those listed above are dischargeable debts, that is, the right to recover the unpaid balance is cut off by the bankrupt's discharge.

If a creditor believes that the debt owed him is not discharged in bankruptcy, he may petition the bankruptcy court to find that particular debt non-dischargeable. If the bankruptcy court finds that this particular debt is one of the debts not affected by a discharge under Section 17 of the Bankruptcy Act, it may, under authority granted it by Public Law 91-467, effective December 13, 1970 and applicable to all cases filed after that date, render a judgement in favor of the creditor which is legally enforceable against the bankrupt.²⁶

K. Secured and Unsecured Debt.

Secured debt is where a creditor holds an interest in collateral as security for the payment of its debt. Secured claims

²⁴Lusk, p. 999.

²⁵"Lending to a Recent Bankrupt - A Case Study," Journal of Commercial Bank Lending, August, 1969, p. 38.

²⁶The New York Times, February 23, 1972, p. 2.

also do not necessarily represent creditor losses. A bankruptcy court may not destroy the value of any valid security which a creditor has on property possessed by a bankrupt.²⁷ Thus, if the bulk of a bankrupt's debts are secured debts, e.g., a mortgage on his house and a chattel mortgage or lien on his automobile, furniture, etc., he will not be able through bankruptcy to receive a discharge of these debts and at the same time keep the property without further liability. In other words, while the bankrupt may receive a discharge of the debt upon which the lien is based, the bankruptcy court may not destroy the lien itself. The trustee will elect whether to take possession of the mortgaged property and sell it for the benefit of creditors or abandon it. If the trustee sells the property, he must pay the secured creditor the value of the security. If the trustee abandons the property because he believes the bankrupt has equity in it above the amount of the mortgage or lien, then the secured creditor may repossess his property in the state court in accordance with state law.²⁸

Unsecured debt is where a creditor has a claim which is neither secured by collateral nor given priority under the Bankruptcy Act. Unsecured claims are the lowest in priority of types of debt that the bankrupt schedules.²⁹ In bankruptcies

²⁷Brunner, p. 64.

²⁸Ibid., p. 65.

²⁹Stanley, p. 112.

that are found to be no-asset or nominal-asset cases, this class of creditor will receive no dividend and the indebtedness does, then, represent full creditor loss through bankruptcy. Unsecured debts would include such things as open charge accounts, medical and dental services, rents, and utilities.

L. Money Earned By the Bankrupt After Bankruptcy Proceedings.

Normally, any money earned by the bankrupt after adjudication (date he filed his petition) is his to keep; however, title to any property inherited by or bequeathed to the bankrupt within six months after filing the petition is vested in the trustee.³⁰ Creditors who received little or nothing on their claims sometimes are dismayed to see the bankrupt driving a new car or living in an expensive house after he has received a discharge in bankruptcy. The explanation for this, however, is that if the bankrupt owned or possessed this property at the time of bankruptcy (filing of the petition) it was either exempt property under state law or the trustee decided the bankrupt had no equity in the property and abandoned it to the secured creditor.³¹ If the latter alternative is the case, the secured creditor probably elected not to foreclose his mortgage or lien upon the property on condition that the bankrupt reaffirm his debt. The

³⁰"Bankruptcy - A Study in Functional Obsolescence," Credit and Financial Management, April, 1970, p. 15.

³¹J. W. Day, "Investor Insights: Getting Back Your Money in a Liquidation is Getting Tougher," Business Management, November, 1970, p. 11.

reaffirmed debt, being made after filing of the petition, was not discharged in bankruptcy. To some creditors, a bankrupt is a better credit risk after bankruptcy than before because he cannot go into bankruptcy again until after six years have passed.

M. Credit Counseling.

To help reduce the growth of bankruptcy, some significant steps have been taken by the business community. Credit counseling services on a free or nominal-fee basis have been established in many cities; among them are Columbus and Cleveland, Ohio; Indianapolis, Indiana; and Phoenix, Arizona. The counseling services offer individuals financial aid ranging from advice to actual arrangements with creditors for reduced payments over a set period of time.³²

Since most bankrupts appear to be willing to accept the responsibility for their financial trouble, it seems reasonable to assume that they would accept budgeting help if available. This type of service with the cooperation of creditors could be very significant in limiting the number of bankruptcies.³³

III. Rehabilitating Rather Than Liquidating the Bankrupt - Two Methods. N. Arrangements - Chapter XI of the Bankruptcy Act.

Often a debtor can overcome many of the difficulties encountered in voluntary bankruptcy settlements by utilizing the

³²"Bank-Supported Credit Counseling," Burroughs, Clearing House, November, 1971, p. 26.

³³"Do Creditors Committees Work?" Credit and Financial Management, June, 1967, p. 35.

arrangements proceedings set forth in Chapter XI of the Bankruptcy Act. An arrangement is defined as any plan of a debtor for the settlement, satisfaction, or extension of the time of payment of his unsecured debts, upon any terms.³⁴ Arrangements proceedings usually are started under one of three sets of circumstances, all involving a debtor who is hopeful of being rehabilitated rather than liquidated but who is financially distressed:

- (1) If negotiations for an out-of-court settlement break down because of inability to secure the consent of important creditors, perhaps the next best step is for the debtor to file a petition under Chapter XI.
- (2) The debtor may decide not to undertake an out-of-court settlement, and may proceed at once to file under Chapter XI.
- (3) If an involuntary petition in bankruptcy has been filed against a debtor, he can avoid this by filing a petition under Chapter XI.³⁵

Proceedings under Chapter XI are voluntary only. No creditor may force a debtor into Chapter XI; the proceedings may be instituted by the debtor alone. An individual, partnership, or corporation may file a petition. The arrangement will modify the rights of unsecured creditors only, although others may be

³⁴Robert H. Cole, Consumer and Commercial Credit Management, (Richard D. Irwin, Inc., Homewood, Illinois), 1968, p. 576.

³⁵Ibid., p. 577.

indirectly affected.³⁶

In looking at Chapter XI proceedings, it is important to remember that they apply only to unsecured obligations of the debtor. When secured claims are outstanding, such as mortgages, conditional sales, or assigned accounts receivables, they may be unaffected by the proceedings under Chapter XI. On the other hand, the debtor is free to arrange privately with the secured creditors for the settlement of their claims. The court, however, usually will require that priority claims, such as taxes, rent, wages, and administrative costs, are covered before approving any arrangement plan for the unsecured creditors.³⁷

C. The Wage Earner's Plan - Chapter XIII of the Bankruptcy Act.

In 1938, the Congress of the United States passed some major legislation amending the Bankruptcy Act. One portion of this legislation was Chapter XIII of the Bankruptcy Act, entitled "Wage Earner Plans." Chapter XIII provides the wage earner a means of paying off his debts from future earnings, under the protection of the bankruptcy court and free from harrassment by creditors.³⁸ In this way the debtor avoids the stigma of being adjudicated a bankrupt. Chapter XIII was enacted several years after a comprehensive study of the field of bankruptcy was made by the Attorney General of the United States.

³⁶"Alive and Kicking; Chapters X and XI Sometimes Have a Happy Ending," Barrons, May 26, 1969, p. 3.

³⁷"What it Takes to Come Out of Chapter XI," (Federal Bankruptcy Act), Credit and Financial Management, February, 1972, p. 11.

³⁸Brunner, p. 10.

a. Who is Eligible For Chapter XIII.

Under existing law, not everyone is eligible to file a wage earner's plan under Chapter XIII of the Bankruptcy Act. To be eligible, the debtor must be a wage earner. A wage earner, as defined by section 606(8) of the Bankruptcy Act, is "an individual whose principal income is derived from wages, salary, or commissions." (Thus, an individual who operates a business is not eligible to file a wage earner's plan. Such individual, however, who wishes to avoid being adjudicated a bankrupt, may be able to obtain relief under Chapter XI of the Bankruptcy Act). There is, however, no minimum or maximum income required to be eligible for a wage earner's plan.³⁹

b. How The Wage Earner's Plan Works.

As the name implies, it is a plan for paying off all debts from future earnings over an extended period of time (normally not more than three years). During this period of time, the wage earner is under the supervision and protection of the bankruptcy court, a United States District Court presided over by a referee (judge). The bankruptcy court will not permit creditors of the wage earner to obtain garnishments or otherwise to "hound" the wage earner while he is paying off his debts under court supervision.⁴⁰ An indication of how often the Wage Earner's Plan is used can be seen in the table on page 19a.

³⁹I. L. Berg, "Wage Earner Plan as an Alternative to Bankruptcy," Personnel Journal, March, 1971, p. 234.

⁴⁰Stanley, p. 105.

FILINGS BY CHAPTER OF THE BANKRUPTCY ACT

Fiscal Year	Total	Volun-	Invol-	Ch		Ch	Ch	Ch	Ch	Sec. 77
		tary straight bank- ruptcy	untary straight bank- ruptcy	IX	X	XI	XII	XIII	XV	
1940	52,577	43,902	1,752	117	320	990	149	3,247	6	0
1941	56,332	47,578	1,491	19	269	769	71	4,433	0	0
1942	52,109	44,366	1,295	43	183	520	52	4,100	0	0
1943	34,711	30,913	649	13	114	205	22	2,007	5	0
1944	19,533	17,629	277	5	68	58	10	1,249	0	0
1945	12,862	11,101	264	8	72	41	5	1,248	0	0
1946	10,196	8,293	268	7	54	79	1	1,371	1	0
1947	13,170	9,657	697	7	96	291	7	2,354	0	0
1948	18,510	13,546	1,029	7	137	442	20	3,315	0	0
1949	26,021	18,882	1,240	2	149	531	17	5,111	4	0
1950	33,392	25,263	1,369	4	134	583	31	6,007	0	0
1951	35,193	26,594	1,099	3	88	459	22	6,924	2	0
1952	34,873	25,890	1,059	15	74	413	21	7,397	1	0
1953	40,087	29,815	1,064	0	86	437	15	8,670	0	0
1954	53,136	41,335	1,398	2	104	649	12	9,634	1	0
1955	59,404	47,650	1,249	1	73	547	19	9,864	1	0
1956	62,086	50,655	1,240	1	40	597	15	9,535	2	0
1957	73,761	60,335	1,189	0	65	599	24	11,549	0	0
1958	91,668	76,048	1,417	2	67	720	23	13,391	0	0
1959	100,672	85,502	1,288	3	78	787	21	12,993	0	0
1960	110,034	94,414	1,296	0	90	622	12	13,599	1	0
1961	146,643	124,386	1,444	0	112	947	31	19,723	0	0
1962	147,780	122,499	1,382	1	77	903	37	22,880	1	0
1963	155,493	128,405	1,409	0	128	1,188	33	24,329	0	0
1964	171,719	141,828	1,339	0	125	1,088	47	27,292	0	0
1965	180,323	149,820	1,317	0	88	1,022	49	28,027	0	0
1966	192,354	161,840	1,173	2	93	909	75	28,261	0	1
1967	208,329	173,884	1,241	1	138	1,033	68	31,963	0	1
1968	197,811	164,592	1,001	3	128	953	69	31,065	0	0
1969	184,930	154,054	946	0	87	867	66	28,910	0	0
1970	194,399	161,366	1,085	0	115	1,262	58	30,510	0	3
1971	201,352	167,149	1,215	2	179	1,782	120	30,904	0	1
1972	182,869	152,839	1,094	1	105	1,361	92	27,374	0	3

This table contains the filings for bankruptcy by chapter of the Bankruptcy Act.

The debtor's plan in essence consists of paying to a trustee, who is appointed by the bankruptcy court, a fixed amount of money each payday. The trustee, who is a bonded officer of the court, uses this money to pay off the creditors of the debtor and costs of administration. To arrive at the amount of money to be paid to the trustee each payday (the Wage Earner's Plan) requires some careful budgeting.⁴¹ The debtor needs to know the total amount of debts which he owes. This amount should be increased by about 20% to take care of all costs, including court costs, attorney's fees, and trustee's commissions and fees.⁴²

The debtor must also list his essential expenses per month for such items as food, clothing, shelter, utilities, taxes, transportation, medicine, etc., allowing some small latitude for unexpected emergency expenses. If the total of these essential living expenses does not exceed approximately 80% of the debtor's take-home pay for the month, then the debtor can turn 20% (or more) of his paycheck over to the trustee each payday to pay off his debts. If by doing this the debtor can pay off his debts within three years, the debtor's or wage earner's plan will be considered feasible by the referee and normally will be approved by him provided a majority of creditors

⁴¹"Bankruptcies - Are We on the Right Road?" Credit and Financial Management, July 12, 1971, p. 14.

⁴²Mathews, p. 86.

will accept the plan. The 80% of his paycheck which the debtor is to keep to pay his current living expenses and the 20% of the paycheck which the debtor is to turn over to the trustee to pay off his debts are merely examples which have been found to be workable. These percentages will vary from plan to plan. Each wage earner's plan must be tailored to the debtor's individual circumstances.⁴³

c. Costs of Wage Earner Plans.

As previously stated, the costs of a wage earner's plan may be as high as 20% of the debtor's total debts. If the debtor owes less than \$1,000, he probably would be well advised to try to settle with his creditors outside the bankruptcy court and thus avoid the attorney's fee and court costs. The protection which the bankruptcy court offers the debtor, however, usually is well worth the extra cost. For example, when the debtor's petition for a wage earner's plan is filed, creditors are stopped at that point from adding delinquency charges and interest on to the debts owed them. The specific costs of this plan are as follows:

- (1) Court Costs. A \$15 filing fee must be paid to the Clerk of the United States District Court at the time the petition for a wage earner's plan is filed. At the first meeting of creditors another \$15 must be paid. Also, the court receives 1% of all monies paid the trustee during the course of the plan.

⁴³Brunner, p. 11.

(2) Attorney's Fees. This is usually the largest cost item and will normally range from \$150 to \$200. In some areas the charge might be slightly higher or slightly lower. Usually, however, this fee is not paid in advance but in installments to the attorney for the debtor along with other creditors.

(3) Trustee's Fees and Costs. The trustee's fee is established by the referee. It may not exceed 5% of all monies paid to him by the debtor. The trustee is also granted an allowance for his costs which normally will run about 5% of all monies paid to him by the debtor.⁴⁴

d. Procedure for a Wage Earner's Plan.

For a wage earner's plan to be initiated, the debtor must consult his attorney. The attorney will need to get a lot of financial information from the debtor; (1) the amount of debt owed to each creditor and his name; (2) the debtor's income; and (3) the debtor's monthly living expenses.⁴⁵ The attorney needs this information in order to determine whether the debtor can come up with a wage earner's plan which is feasible, which will be accepted by creditors, and which the referee can approve. If the attorney believes that the debtor can qualify for a wage earner's plan, he will prepare a petition in effect requesting approval of the court for a wage earner's plan for the debtor.

⁴⁴Stanley, p. 104.

⁴⁵Ibid., p. 102.

The petition for approval of a wage earner's plan is filed with the Clerk of the United States District Court serving the area in which the debtor lives.⁴⁶ As previously mentioned, a \$15 filing fee must be paid at the time the petition is filed. As soon as the petition is filed, the debtor's attorney should be able to obtain, if necessary, a temporary restraining order against all creditors forbidding them to take any actions against the debtor without the bankruptcy courts consent. This will stop any wage attachments or garnishments.⁴⁷

e. The First Meeting of Creditors.

When the petition is filed with the Clerk of the United States District Court, it is normally referred to a referee in bankruptcy. Not less than ten days or more than 30 days after the petition is filed, the referee calls a first meeting of all creditors of the debtor to determine whether they will approve the debtor's plan. Creditors are invited to attend this meeting but are not required to do so. Usually, the creditors have received a copy of the proposed plan along with the notice of the first meeting of creditors. In areas where wage earner plans are well established, creditors often do not bother to attend the first meeting. The debtor's attorney usually will obtain the necessary acceptances from creditors of the debtor. The debtor and his attorney normally must attend the first meeting of creditors. Typically, the referee and/or the trustee will ask

⁴⁶Mathews, p. 88.

⁴⁷Berg, p. 235.

the debtor a few questions about his debts, income, and his financial situation. In the absence of objections from creditors, the referee will approve the plan if he feels it is feasible and makes sense.⁴⁸

IV. Conclusion.

This paper was broken down into two major sections in discussing bankruptcy: some general information concerning bankruptcy and The Wage Earner's Plan. The general information section consisted mainly of explaining what a bankrupt must do in going through a bankruptcy proceeding and the factors involved after he has filed a bankruptcy petition. This section was intended to be mainly informative in attempting to explain the complicated and lengthy process of a bankruptcy proceeding. The second section, concerning The Wage Earner's Plan, was also intended to be informative in discussing what is considered one of the most important chapters of the Bankruptcy Act. The Wage Earner's Plan deals with one section of the Bankruptcy Act that is concerned with rehabilitating rather than liquidating the debtor. This plan simply provides the wage earner a means of paying off his debts from future earnings, under the protection of the bankruptcy court and free from harrassment by creditors. The combination of these two sections just described represents only a small part of the total process of bankruptcy.

⁴⁸Brunner, p. 12.

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