MODULAR BANKRUPTCY: TOWARD A CONSUMER SCHEME OF ARRANGEMENT

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INTRODUCTION

In the world of cross-border corporate insolvency, those in the know are familiar with the increasingly popular scheme of arrangement, the British quasi-reorganization procedure that allows a company to restructure some, but not all, of its debt.[1] The typical scheme effects a corporate balance sheet reshuffling by supermajoritarian approval (and judicial "sanction") but often leaves other debt, such as the trade, untouched.[2] A key conceptual component of the scheme mechanism is its intentional modularity, called by some its "selectivity."[3] It does not require a comprehensive reckoning of all claims against a given debtor, only some. The scheme has proved popular—so popular, in fact, that corporate bankruptcy market share–grabber Singapore introduced scheme-like procedures in its most recent overhaul of its insolvency system.[4] Indeed, some wags have pronounced it the Decline and Fall of Chapter 11.[5]

Yet our European friends have struggled with how to assess the scheme legally. Formally, it originated outside insolvency law.[6] It does not appear in Annex A of the EU Insolvency Regulation (which houses the

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1 *See* Corporate Insolvency and Governance Act 2020, c. 12, sched. 9, pt. 1 (UK) (amending Companies Act 2006, c. 46, pt. 26A (UK)); *Corporations Act 2001* (Cth) pt 5.1 (Austl.).

2 *See*, *e.g.*, Re Hertz UK Receivables Ltd. (2020) EWHC (Ch) 3649 (Eng.).

3 Sarah Paterson & Adrian Walters, *Chapter 11's Inclusivity Problem*, 55 ARIZ. ST. L.J. (forthcoming 2024), https://dx.doi.org/10.2139/ssrn.4448945 [https://perma.cc/NYZ4-L3TR].

4 *See* Insolvency, Restructuring and Dissolution Act 2018 (Act No. 40/2018) (Sing.).

5 *See* Simon Thomas, Kizzy Jarashow & Oonagh Steel, *UK Restructuring Proceedings May Attract More Foreign Cos.*, GOODWIN PROCTOR LLP (Dec. 6, 2019), https://www.goodwinlaw.com//-//media//files//publications//uk-restructuring-proceedings-may-attract-more-fore.pdf [https://perma.cc/G53J-25WD].

6 *See* Regulation 2015/848, annex A, 2015 O.J. (L 141) 19, 60–63 (EU) [hereinafter Recast Insolvency Regulation] (listing applicable "insolvency proceedings" in Annex A).

"insolvency proceedings" entitled to automatic recognition), although it has been adjudicated by some courts to constitute an "insolvency proceeding" for purposes of, for example, the Lugano Convention and the United Nations Commission on International Trade Law (UNCITRAL) Model Law on Cross-Border Insolvency.[7] The reason for this tension arises from the deep-seated understanding in the restructuring world that one foundational pillar of what it means to be a "bankruptcy" law is that the legal intervention should be comprehensive and address all circumstances of general financial default, with its attendant collective action challenges.[8] Talk of a "partial" bankruptcy proceeding may strike many well-socialized insolvency professionals as simply nonsensical. And yet the scheme persists; if anything, its ascendancy reveals its Darwinian staying power from market demand.

Less attention—no attention, really—has been devoted to the potential applicability of the corporate scheme of arrangement to the consumer side of bankruptcy.[9] This Article seeks to fill that gap. Specifically, this Article suggests that the intentional modularity of the scheme procedure may well be transplantable to the world of consumer debt readjustment. Such a transplant would be far from effortless. Consumer bankruptcy raises different policy concerns, implemented through different doctrines, from those raised by corporate reorganization, including such issues as, inter alia, discharge, priority, and abuse-prevention. In addition to these consumer-specific policy concerns, implementation of a consumer scheme would raise questions flowing from the attempt to resolve only part of a consumer's financial distress. Unpacking a seeming premise of the primary extant consumer provisions of the U.S. Bankruptcy Code (Chapters 7 and 13)[10]—that all the individual debtors' debts will be settled and their creditors' rights functionally extinguished—would necessarily require difficult consideration of how to address the differential treatment of secured and unsecured debt in a modular proceeding. For example, in the realm of secured debt, assets in which the debtors had equity would have to be treated differently from assets in which the debtors had no equity (and,

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[7] Re Gategroup Guarantee Ltd. [2021] EWHC (Ch) 304 [109]–[131] (Eng.) (discussing Lugano); *In re* Oi S.A., 587 B.R. 253, 274 (Bankr. S.D.N.Y. 2018) (highlighting UNCITRAL).

[8] Riz Mokal, *What Is an Insolvency Proceeding?* Gategroup *Lands in a Gated Community*, 31 INT'L INSOLVENCY REV. 418 (2022); *see also* ELIZABETH WARREN, JAY LAWRENCE WESTBROOK, KATHERINE PORTER & JOHN A.E. POTTOW, THE LAW OF DEBTORS AND CREDITORS: TEXT, CASES, AND PROBLEMS 7 (8th ed. 2021).

[9] Tanzania has the closest to a consumer scheme. Ngwaru Maghembe & Melanie Roestuff, *Bankruptcy and Alternative Debt Relief for Consumers in Tanzania—a Comparative Investigation*, 43 COMPAR. & INT'L L.J. S. AFR. 292, 301–02, 308–09 (2010) (describing scheme-like procedures in prebankruptcy filing).

[10] 11 U.S.C. chs. 7, 13.

indeed, a sizable deficiency), depending on the scope of the "partial" bankruptcy estate. Each of these challenges could be overcome, albeit doubtless with differing degrees of satisfaction, in considering a modular system of consumer bankruptcy inspired by the modern usage of the British scheme.

This Article will proceed as follows. First, it will briefly canvass the major current theories of the consumer bankruptcy system to extract some conceptual foundations necessary to appraise critically the proposal for a consumer scheme. Second, it will describe the UK scheme of arrangement and its unique approach to debt adjustment, as well as examining the empirical and normative case for selective consumer relief. Third, it will outline what a consumer scheme would look like, with a focus on asset-based relief, using a proposed "car scheme" as an explanatory prototype. Fourth, it will consider in some detail the serious normative, constitutional, and doctrinal challenges to how a consumer scheme would address such issues as deficiency claims for undersecured debt and surplus equity for oversecured debt. Finally, this Article will conclude and discuss a current legislative proposal to overhaul the bankruptcy system to gauge compatibility with the scheme proposal. In doing so, this Article will argue that a consumer scheme is not just possible but desirable to accord consumers the same heterogeneity benefits of lower-cost debt relief enjoyed by their corporate insolvency peers.

I. NORMATIVE ATTRIBUTES OF DEBT RELIEF

A. *Theoretical Approaches*

To consider seriously a proposal for modular consumer bankruptcy, we must start with a normative discussion of just what bankruptcy law—at least consumer bankruptcy law—is trying to do. And indeed, bankruptcy legal scholarship has embraced various spirited debates about the normative foundation of consumer debt relief: the discharge.[11] Certainly, the historical pedigree of the discharge is lengthy; for example, the Biblical Jubilee concept worked into the Code's time bar on filing for relief.[12] But there is hardly normative consensus on just what bankruptcy

[11] *See, e.g.*, Charles G. Hallinan, *The "Fresh Start" Policy in Consumer Bankruptcy: A Historical Inventory and an Interpretative Theory*, 21 U. RICH. L. REV. 49 (1986).

[12] *See Deuteronomy* 15:1–3; 11 U.S.C. § 727(a)(8). The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) extended the Chapter 7 refiling restriction to eight years, surpassing the Biblical seven. Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, § 312, 119 Stat. 23, 86–87 (codified as amended at 11 U.S.C. § 727(a)(8)).

law is all about. To be sure, "forgiveness" grounds much modern virtue theory of the reason for the discharge, with motivations ranging from the deontic to the aretaic.[13] We discharge debts because it is the right thing to do when people become overwhelmed and suffer from debt overhang, and we also discharge them because it makes us better people to recognize this and show this forgiveness.[14] This moral basis for the discharge wanders into conceptions of desert, too, with only the "honest but unfortunate" debtors entitled to the beneficence of the state's discharge power.[15] Let us therefore consider the first cluster of normative justifications of a consumer bankruptcy system as "morality-based."

Of course, articulating a normative theory does not suffice to trace it into the compelled content of substantive discharge law. For example, one can agree that the purpose of the bankruptcy discharge is to forgive "worthy" debtors, but then have marked disagreement as to which debtors demonstrate such worth. For example, one may start from the orientation that *pacta sunt servanda* dictates that promises carry a moral and sometimes legal duty to be kept; discharge's mockery of that pledge should thus be constrained only to the most very wretched.[16] Conversely, one could start with the moral prior that rapacious corporations overlend to blindsided and unsophisticated consumers, and those debtors therefore deserve as much succor as the law can muster.[17] Accordingly, even a coherently articulated bankruptcy theory—for example, that bankruptcy discharge is morally compelled—can yield a substantial theory-doctrine gap.

Sitting alongside such virtue-based normative theories of consumer bankruptcy discharge are more economically inspired ones. Thus, while

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13 *See* WARREN, WESTBROOK, PORTER & POTTOW, *supra* note 8, at 294–304.

14 *See* KAREN GROSS, FAILURE AND FORGIVENESS: REBALANCING THE BANKRUPTCY SYSTEM 102–03 (paperback ed. 1999); Heidi M. Hurd & David C. Baum, *The Virtue of Consumer Bankruptcy*, *in* A DEBTOR WORLD: INTERDISCIPLINARY PERSPECTIVES ON DEBT 217, 221–22 (Ralph Brubaker, Robert M. Lawless & Charles J. Tabb eds., 2012). Discharge comes from relief from debtor's prison. *See, e.g.*, Emily Kadens, *The Last Bankrupt Hanged: Balancing Incentives in the Development of Bankruptcy Law*, 59 DUKE L.J. 1229, 1236 (2010); BRUCE H. MANN, REPUBLIC OF DEBTORS: BANKRUPTCY IN THE AGE OF AMERICAN INDEPENDENCE (2002).

15 Marrama v. Citizens Bank of Mass., 549 U.S. 365, 367 (2007) ("The principal purpose of the Bankruptcy Code is to grant a 'fresh start' to the 'honest but unfortunate debtor.'" (quoting Grogan v. Garner, 498 U.S. 279, 286 (1991) (quoting Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934)))); *see* CHARLES JORDAN TABB, LAW OF BANKRUPTCY 36 (5th ed. 2020) ("While the quasi-criminal nature of bankruptcy remained, the Statute of Anne established the roots of a more humanitarian legislative attitude toward honest but unfortunate debtors.").

16 *E.g.*, Edith H. Jones & Todd J. Zywicki, *It's Time for Means-Testing*, 1999 BYU L. REV. 177, 207–08.

17 *E.g.*, Oren Bar-Gill & Elizabeth Warren, *Making Credit Safer*, 157 U. PA. L. REV. 1 (2008); Susan Block-Lieb & Edward J. Janger, *The Myth of the Rational Borrower: Rationality, Behavioralism, and the Misguided "Reform" of Bankruptcy Law*, 84 TEX. L. REV. 1481 (2006).

for some the purpose of debt forgiveness is to protect the human dignity of the overindebted individual,[18] others see it from a more utilitarian focus, with the goal of rehabilitating the debtor to productive economic participation.[19] "[S]ociety as a whole also loses when moping bankrupt debtors are distracted from working at their highest and best-use level of productivity because they are instead coping with financial ruin."[20] Thus, the consumer bankruptcy discharge has nothing to do with such namby-pamby ideals as dignity but rather the "redeployment of the debtor's human capital."[21] Note that both approaches can (but need not) purport to be agnostic over the origin of the debtor's woes.

A somewhat different conceptualization from either the morality or the economic utility focus of the bankruptcy discharge considers its social insurance function. Here, like Medicaid or other government programs, the social function of the bankruptcy discharge is to provide state mitigation against financial dislocation caused by exogenous shock (which can be both morally compelled and economically efficient).[22] To be sure, risk-based premium pricing suggests that insured risk likely comprises both endogenous and exogenous vectors.[23] But the mandatory nature of the bankruptcy discharge is consistent with an understanding of consumer debt as an intrinsically dangerous activity that requires some protection, even at force of government intervention in the presence of risk-tolerant consumers. You don't get to opt out of car insurance in most states.[24] Indeed, Professor Robert Lawless's meticulous empirical work shows that, at least up through the first decade of this century when he published, bankruptcy filings tend to correlate (with some lag) with

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18 *E.g.*, Directive 2019/1023, recital 21, 2019 O.J. (L 172) 18, 21 (EU) [hereinafter Preventative Restructuring Directive]; Iain Ramsay, *The New Poor Person's Bankruptcy: Comparative Perspectives*, 29 INT'L INSOLVENCY REV. S4, S5 (2020).

19 *E.g.*, REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. DOC. NO. 93-137, pt. 1, at 71 (1973) (summarizing that bankruptcy should rehabilitate debtors to serve more productive economic purposes); *see* Katherine Porter & Deborah Thorne, *The Failure of Bankruptcy's Fresh Start*, 92 CORNELL L. REV. 67 (2006).

20 John A.E. Pottow, *Private Liability for Reckless Consumer Lending*, 2007 U. ILL. L. REV. 405, 412.

21 Ronald J. Mann, *Making Sense of Nation-Level Bankruptcy Filing Rates*, *in* CONSUMER CREDIT, DEBT AND BANKRUPTCY: COMPARATIVE AND INTERNATIONAL PERSPECTIVES 225, 242–43 (Johanna Niemi, Iain Ramsay & William Whitford eds., 2009).

22 *See* Katherine Porter, *The Damage of Debt*, 69 WASH. & LEE L. REV. 979, 996 (2012).

23 *See* Omri Ben-Shahar & Kyle D. Logue, *Outsourcing Regulation: How Insurance Reduces Moral Hazard*, 111 MICH. L. REV. 197 (2012).

24 TOM BAKER, KYLE D. LOGUE & CHAIM N. SAIMAN, INSURANCE LAW AND POLICY: CASES AND MATERIALS 471 (5th ed. 2021) ("Auto liability insurance is mandatory in all but a very few states.").

aggregate household debt.[25] Here, too, the desert/blame debate can be spun out as with other theories of consumer discharge. Mandatory insurance can be theoretically indifferent as to cause: one might have beliefs that much of that consumer debt is "bad" (the run-up of a decadent culture of mall-hungry overshoppers),[26] or that it is "good" (home mortgages that stabilize communities with the middle-class dream).[27] Bountiful empirical data suggest considerable exogenous forces at play, with most bankruptcies associated with a major life-event dislocation (job loss, family dissolution, medical crisis, etc.).[28] Behavioral learnings about consumer predictive capability also inform the desirability of a mandatory versus optional nature to the coverage.[29]

As the present discussion demonstrates, therefore, there really is no widespread consensus on a unitary theory of consumer bankruptcy. Some prefer economic conceptions, some prefer morality-based ones. Many find both attractive. Nor are these the exclusive approaches; some have even focused on the "public peace" aspect of a consumer debt relief system as an explanation of why we forgive consumer debt by force of law.[30] Note, too, that the aforementioned theories are *debtor focused*. Other prominent analysts of bankruptcy theory turn their attention to the collective action resolution justification of a bankruptcy discharge—guarded by an automatic stay of collection activity—and argue that it is in the *creditors'* collective best interest to stop in their tracks and accept an orderly pro rata distribution as opposed to the paltry spoils of piecemeal liquidation, although to be sure this thinking has more purchase in the corporate insolvency realm.[31]

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25 Robert M. Lawless, *The Paradox of Consumer Credit*, 2007 U. ILL. L. REV. 347; *see also* Robert M. Lawless et al., *Did Bankruptcy Reform Fail? An Empirical Study of Consumer Debtors*, 82 AM. BANKR. L.J. 349 (2008) [hereinafter Lawless et al., *Reform Fail?*].

26 *See* JOHN DE GRAAF, DAVID WANN & THOMAS H. NAYLOR, AFFLUENZA: THE ALL-CONSUMING EPIDEMIC (2001).

27 *See* 26 U.S.C. § 163(g) (providing a tax exemption for interest paid on a mortgage under 26 U.S.C. § 25).

28 *See, e.g.*, TERESA A. SULLIVAN, ELIZABETH WARREN & JAY LAWRENCE WESTBROOK, THE FRAGILE MIDDLE CLASS: AMERICAN IN DEBT (2000).

29 *See, e.g.*, Oren Bar-Gill, *Seduction by Plastic*, 98 NW. U. L. REV. 1373 (2004) (exploring consumer behavioral biases).

30 WARREN, WESTBROOK, PORTER & POTTOW, *supra* note 8, at 300–01 (arguing that insolvency proceedings maintain social peace by reducing "pitchfork costs").

31 Douglas G. Baird & Thomas H. Jackson, *Corporate Reorganizations and the Treatment of Diverse Ownership Interests: A Comment on Adequate Protection of Secured Creditors in Bankruptcy*, 51 U. CHI. L. REV. 97, 116–19 (1984); *see also* THOMAS H. JACKSON, THE LOGIC AND LIMITS OF BANKRUPTCY LAW 253, 259–63 (1986) [hereinafter JACKSON, LOGIC AND LIMITS] (canonical articulation of creditors' bargain theory).

B. *The Bankruptcy Discharge and the Risk of Abuse*

Whatever one's favorite anchoring normative theory of consumer bankruptcy law, at least one common theme emerges: the concept of a fresh start as the golden thread throughout the corpus of bankruptcy scholarship and jurisprudence. At a certain point, debtors need a fresh start from the overwhelming financial burdens of their past. "One of the primary purposes of the Bankruptcy Act is to 'relieve the honest debtor from the weight of oppressive indebtedness, and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortunes.'"[32] In more modern parlance, sometimes a financial reboot is in order. The doctrinal outlet for this central component of consumer bankruptcy is the *discharge* following a successful bankruptcy petition.[33] Under whatever normative theory one embraces, the purpose of consumer bankruptcy law is to provide the debtor with a discharge of debt.

1. The Risk of Abuse

For purposes of the instant discussion (not to pick theoretical favorites), consider especially the insurance conception of the consumer bankruptcy discharge. As alluded to above, understanding bankruptcy protection as "financial disaster insurance" recognizes the intrinsic risk of consumer credit and the pervasiveness and stochastically unpredictable nature of that risk. It also takes some of the moral heat off the assessment of whether debtors are good or bad people worthy of debt relief. Indeed, virtuous drivers and venal drivers alike procure car insurance. Insurance conceptualization thus takes the focus off the *person* (the debtor screwed up) and situates it more on the *event* (bad

32 Loc. Loan Co. v. Hunt, 292 U.S. 234, 244 (1934) (quoting Williams v. U.S. Fid. & Guar. Co., 236 U.S. 549, 554–55 (1915)) ("This purpose of the act has been again and again emphasized by the courts as being of public as well as private interest, in that it gives to the honest but unfortunate debtor who surrenders for distribution the property which he owns at the time of bankruptcy, a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt." (first citing Stellwagen v. Clum, 245 U.S. 605, 617 (1918); then citing Hanover Nat'l Bank of the City of N.Y. v. Moyses, 186 U.S. 181 (1902); then citing Swarts v. Fourth Nat'l Bank of St. Louis, 117 F. 1, 3 (8th Cir. 1902); then citing United States *ex rel.* Adler v. Hammond, 104 F. 862, 863 (6th Cir. 1900); then citing Barton Bros. v. Tex. Produce Co., 136 F. 355, 357 (8th Cir. 1905); then citing Hardie v. Swafford Bros. Dry Goods Co., 165 F. 588, 591 (5th Cir. 1908); and then citing Gilbert v. Shouse, 61 F.2d 398 (5th Cir. 1908))); *see also In re* Brown, 1 Mart (o.s.) 158, 159 (Orleans 1810) (earliest known reference to "honest but unfortunate debtor" phrase).

33 11 U.S.C. §§ 727, 1123, 1328.

financial things happened). Again, this is not a crisp dichotomy; bad things can happen more to bad people, and insurance can involve (and indeed is to a certain extent premised upon) risk-based pricing,[34] but the uncluttered orientation of bankruptcy discharge toward covering financial disaster is helpful for teasing out two other underlying insurance-cognate attributes of the consumer bankruptcy system: policing *fraud* and *moral hazard*.[35] That is, with any insurance product, one worries about the temptation on covered parties to cheat the system by fabricating claims. One also worries about insurance coverage distorting the levels of activity and risk of the insured.[36] The latter is surely known to anyone who has ever driven over speed bumps with me in a rental car.

Accordingly, if bankruptcy protection—that is, the capacity to receive a general discharge from consumer indebtedness—is a form of financial hazard insurance, then insurance theory teaches us to beware the dangers of people defrauding the system (for example, hiding assets that should be used to pay creditors as a precondition of receiving the discharge). And to reiterate, concern over fraud and the discharge does not require one to embrace an insurance function theory of bankruptcy relief. These policy worries have persisted for some time:

> Time and Experience has furnish'd the Debtors with Ways and Means to evade the Force of this Statute, and to secure their Estate against the reach of it; which renders it often insignificant, and consequently, the Knave, against whom the Law was particularly bent, gets off; while he only who fails of mere Necessity, and whose honest Principle will not permit him to practice those Methods, is expos'd to the Fury of this Act.[37]

The concomitant concerns of moral hazard are equally present but slightly more complex to disentangle. There are two decision points at which the presence of insurance might distort consumer financial behavior, and these relevant points are sometimes loosely referred to as *ex ante* and *ex post*. Take ex post first. One worry we might have with a bankruptcy discharge, unless it is punitively priced, is that consumers who have accrued substantial consumer debt and feel disinclined to pay

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[34] *See, e.g.*, Tom Baker, *Containing the Promise of Insurance: Adverse Selection and Risk Classification,* 9 CONN. INS. L.J. 371, 377 (2003).

[35] *See, e.g.*, Kent D. Syverud, *Insurance Law Out of the Shadows*, 89 MICH. L. REV. 1429, 1431 (1991); 1 JEFFREY E. THOMAS, LEO P. MARTINEZ, DOUGLAS R. RICHMOND & MARC S. MAYERSON, NEW APPLEMAN INSURANCE LAW PRACTICAL GUIDE § 3.11 (2023) (observing that insurance policies often include exclusions for fraud as to avoid coverage for moral hazard).

[36] *See* Steven Shavell, *Liability and the Incentive to Obtain Information About Risk*, 21 J. LEGAL STUD. 259, 259–61 (1992).

[37] DANIEL DEFOE, AN ESSAY UPON PROJECTS 197 (London, R.R. for Tho. Cockerill 1697).

the piper may simply "take bankruptcy" and file a petition instead of tightening their belts when financial winds blow in an unfriendly direction. Knowing they have an easy landing through the bankruptcy courts, they may "under try" at conducting the never-happy financial triage of adjusting their budgets to meet their obligations.[38]

The second decision point occurs further upstream, which is why some characterize it as ex ante. This risk is that exceptionally foresightful debtors might be incentivized to incur debt (in deciding, say, whether to fund a transaction through savings, consumer credit, or even to forgo the consumption entirely), secure in the knowledge that if and when financial hardship ever befalls them, the bankruptcy system provides a readily accessible discharge.[39] The difference between these two moral hazard risk points is that one pertains to the question of whether and how much debt to incur, whereas the other pertains to what to do about the debt once it has become unduly burdensome, irrespective of the decision-making that went into the debt's acquisition. Both have been argued to create risk points of moral hazard.[40]

The emerging data from the literature on consumer debtor behavior suggest that the ex ante risk is more hypothesized than real. Few consumers have the predictive capability to guide their day-to-day purchasing habits by a remote and abstracted risk of bankruptcy protection laws.[41] Indeed, most consumers who have never filed for bankruptcy would be hard-pressed even to articulate any substantive provisions of the Bankruptcy Code.[42] Much of the sociological data we have indicates that, if anything, consumers abhor bankruptcy, with many who have filed trying to hide this embarrassing development from their

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38 *See* Todd J. Zywicki, *Institutions, Incentives, and Consumer Bankruptcy Reform*, 62 WASH. & LEE L. REV. 1071, 1072 (2005) ("Individuals increasingly appear to be *choosing* to file bankruptcy as a response to financial distress, rather than reducing spending or tapping savings to avoid bankruptcy." (emphasis added)); *see National Bankruptcy Review Commission Report: Hearing Before the Subcomm. on Com. & Admin. L. of the H. Comm. on the Judiciary*, 105th Cong. 2–4 (1997) (statement of Rep. George W. Gekas, Chairman, Subcomm. on Commercial and Admin. Law, H. Comm. on the Judiciary); President George W. Bush, Remarks on Signing the Bankruptcy Abuse Prevention Consumer and Protection Act, 41 WEEKLY COMP. PRES. DOC. 641, 642 (Apr. 20, 2005) ("[T]oo many people have abused the bankruptcy laws. They've walked away from debts even when they had the ability to repay them. . . . Under the new law, Americans who have the ability to pay will be required to pay back at least a portion of their debts.").

39 *See, e.g.*, Jones & Zywicki, *supra* note 16, at 204–05; Michelle White, *Personal Bankruptcy Under the 1978 Bankruptcy Code: An Economic Analysis*, 63 IND. L.J. 1, 45 tbl.6 (1987) (showing positive correlation between generosity of exemptions and number of consumer bankruptcy filings).

40 *See* WARREN, WESTBROOK, PORTER & POTTOW, *supra* note 8, at 301–02.

41 *See* Block-Lieb & Janger, *supra* note 17, at 1490–91.

42 *See* Pamela Foohey, Robert M. Lawless, Katherine Porter & Deborah Thorne, *Life in the Sweatbox*, 94 NOTRE DAME L. REV. 219, 221 (2018).

friends and family,[43] although there are nuances within these data.[44] Thus, the supposition that consumption decisions are meaningfully influenced by substantive bankruptcy law is probably false.

By contrast, when a bankruptcy filing is more saliently on the horizon, then it is eminently plausible that consumer decision-makers consider the fate they would face in bankruptcy court in pondering the desirability of a possible filing (versus, say, just ducking their debt collectors' call, flying under the radar, tightening their belts, etc.).[45] Certainly, the 2005 amendments to the Bankruptcy Code[46]—which deliberately made bankruptcy relief more painful for debtors—demonstrated "success" along lawmakers' stated metrics by reducing the number of people filing for bankruptcy (albeit regressively).[47] This suggests that consumer behavior is not impervious to the content of bankruptcy law, only that its effect is likely to be concentrated on the short-term (ex post) horizon. By corollary, this means that even in a behaviorally constrained decision-making world, moral hazard concerns do resonate with regard to the discharge relief provided by the Code.

2. Policing Abuse

How, then, does the current Bankruptcy Code police fraud and moral hazard incentives, keeping with the insurance-function normative conception of the law? The former is addressed directly. Numerous provisions of the Code withhold the discharge for debtors who cheat the system.[48] Indeed, there is some nuance to what is called "nondischargeability." Some Code provisions target specific debts that are tarnished with a taint of fraud and simply say that they are categorically barred from the debtor's discharge.[49] And within those categories of specifically nondischargeable debt, there is even more

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43 TERESA A. SULLIVAN, ELIZABETH WARREN, JAY LAWRENCE WESTBROOK, THE FRAGILE MIDDLE CLASS: AMERICANS IN DEBT 32 (2020 ed.).

44 Sara Sternberg Greene, *The Broken Safety Net: A Study of Earned Income Tax Credit Recipients and a Proposal for Repair*, 88 N.Y.U. L. REV. 515, 555 (2013).

45 *See* Katherine Porter, *The Pretend Solution: An Empirical Study of Bankruptcy Outcomes*, 90 TEX. L. REV. 103, 132–35 (2011) (discussing goals of Chapter 13 bankruptcy filers).

46 Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 (codified as amended in scattered sections of 11 U.S.C.).

47 *See* Lawless et al., *Reform Fail?*, *supra* note 25, at 377.

48 *E.g.*, 11 U.S.C. §§ 523, 727.

49 *E.g.*, *id.* §§ 523(a)(2), 727(a)(2).

nuance.[50] Note that these provisions look at specific debts and remove bankruptcy relief for them and them only. Also note that fraud is not the exclusive ground for nondischargeable debts. Myriad policy reasons, not to mention rent-seeking lobbying spoils, ground additional categories of nondischargeable debt unrelated to fraud; some readers saddled with student loans may be familiar with at least one such other ground of nondischargeability. Suffice it to say that the Code frowns upon fraudulently incurred debt in policing the dispensation of the bankruptcy discharge.[51]

Beyond that, however, are provisions of the Code that not merely except specific debts due to fraud, but effectively kick debtors out of the bankruptcy system altogether through operation of a general denial of discharge.[52] One might think that this more draconian punishment is reserved for "bigger" frauds, perhaps when the harm caused by a fraudulently incurred debt is especially grave. In actuality, the general denial is focused more on systemic attacks to the bankruptcy process. For example, falsification of bankruptcy records in filing the petition,[53] or failure to identify or account for all one's assets,[54] may trigger a general denial of the discharge. In other words, when debtors are cheating. Thus, worries over filing false claims to get a state-provided "insurance benefit" are addressed principally, and rather forthrightly, through the nondischargeability provisions of the Bankruptcy Code. These provisions do not necessarily require an embrace of the insurance-function theory of consumer bankruptcy to explain themselves, of course; one could easily ascribe them to a desert-based morality theory and rationalize these rules as weeding out the undeserving who forfeit their moral claim to bankruptcy relief.

The Code's consideration of moral hazard—how to make sure the debtor's behavior comports with optimal financial risk-taking and bankruptcy-seeking—is more complicated for several reasons, not least of which is that debtors do not pay a direct premium for the government-provided insurance of the bankruptcy discharge, and so risk-based pricing, a cornerstone of the private market, seems unavailable.[55]

50 For example, some tax debts are forever barred from discharge (false returns, no returns) and some tax debts are stayed from discharge for a holding period (untimely returns). *Id.* §§ 508, 523(a)(8).

51 *Id.* § 523(a)(8).

52 *See, e.g.*, *id.* § 727(a).

53 *Id.* § 727(a)(3).

54 *Id.* § 727(a)(2)(A)–(B), (d)(2).

55 A now-discredited assertion abounded during the BAPCPA debates that bill-paying Americans were shouldering a $400 per family "bankruptcy tax" in higher credit costs to cross-subsidize their bankrupt peers. Elizabeth Warren, *The Phantom $400*, 13 J. BANKR. L. & PRAC., no. 2, 2004, at 77, 81 ("The industry, of course, never explicitly *said* that the $44 billion it planned to

Nonetheless, as the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) shows, the policing comes through the broader design of the Code itself and especially its admission screens (i.e., how and when it permits debt relief through discharge). For example, one might consider the provisions that bar refiling bankruptcy petitions within certain time periods as reflecting a gatekeeping role in making sure debtors do not file an initial petition too carefreely.[56]

The best way to think of the system's embrace of policing moral hazard is to think of the consumer bankruptcy system as requiring a grand bargain of sorts between debtors and their creditors as establishing the pain the debtors must endure to receive the psychic and financial pleasure of a discharge. That, in turn, requires a quick understanding of the multichapter approach to consumer bankruptcy in the United States. Very briefly, the typical debtor seeking relief has two choices of chapter: Chapter 7 or Chapter 13. Chapter 7 is a liquidation regime, in which debtors give up all their nonexempt assets, which are then liquidated and shared pro rata with creditors, in exchange for which they get an unconditional discharge as the celebrated fresh start.[57] Chapter 13, by contrast, is essentially a tithing program under which debtors contribute a share of their income for a fixed period (between three and five years), and only after which they receive the same discharge.[58] Nominally, a debtor proposes a Chapter 13 repayment plan for creditor consideration,[59] but there is no actual voting on the plan, as there is in the corporate world of Chapter 11, only a streamlined process of objection.[60] Upon satisfactory objection resolution, the court confirms the plan.[61]

The uninitiated may look at these two systems and be drawn to the intuition that receiving an immediate discharge and forfeiting no income is preferable to waiting several years while tithing a nontrivial part of one's income during the wait. But there is a method to the seeming madness: debtors who have accrued assets that would otherwise have to be handed over to the liquidating trustee in a Chapter 7 case get to retain that property in Chapter 13. Chapter 13 debtors, in other words, keep all

recover from the bankrupt families would be passed on to its customers. History suggests that it would not.").

56 11 U.S.C. §§ 727(a)(8)–(9), 1328(f).

57 *Id.* § 727.

58 *Id.* § 1328.

59 *Id.* § 1321 ("The debtor shall file a plan.").

60 *Id.* § 1325(b).

61 The most meaningful grounds of objection are that the debtor is not paying their full disposable income into the tithe, *id.* § 1325(a)(1), (b)(1)(B), or that the creditor is receiving less than they would in a Chapter 7 liquidation, *id.* § 1325(a)(4).

(not just the exempt) property—good news for yacht owners.[62] Indeed, one helpful way to think about Chapter 13 is that it allows debtors to redeem by installation payment all nonexempt property, with the price of the redemption being set, progressively, at the value of the payment stream of the tithable component of net income.

For not entirely coherent reasons, Congress has long favored Chapter 13 over Chapter 7,[63] even in the face of data starkly indicating that most Chapter 13 debtors never complete their multiyear repayment plans (and now, worse, increasing data showing the racially biased effects of Chapter 13).[64] Indeed, Chapter 13 favoritism was an anchoring premise of BAPCPA;[65] myriad statutory provisions try to steer debtors toward Chapter 13 over Chapter 7.[66] All that matters for the present discussion, however, is that both Chapters 7 and 13 have "buy-ins" that are designed to ensure that the debtor experiences some pain, and hence is not morally hazardous, in accessing the discharge. (Whether that pain level is properly calibrated under current law is an important debate left for another day.)

If the delicate policy balance of the consumer bankruptcy system mandates relinquishment of nonexempt assets or a commitment to tithe future income (and in many systems outside this country, both),[67] then it is fair to characterize this moral hazard pain as constitutive to the bankruptcy discharge. Indeed, backing up, it is not just the discharge itself and the fresh start that it accords that should be seen as the forming the conceptual core of what it means to provide bankruptcy relief. This discussion of moral hazard prevention has been to support the more

62 Congress does restrict Chapter 13 to the middle class, using debt as a proxy therefor by capping the maximum debt a Chapter 13 debtor can have and remain eligible for relief. 11 U.S.C. § 109(e). Good faith requirements also constrain yachts. *In re* Deutscher, 419 B.R. 42 (Bankr. N.D. Ill. 2009) (dismissing yacht owner's case).

63 *See* Susan Jensen, *A Legislative History of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 79 AM. BANKR. L.J. 485 (2005).

64 *See* Sara S. Greene, Parina Patel & Katherine Porter, *Cracking the Code: An Empirical Analysis of Consumer Bankruptcy Outcomes*, 101 MINN. L. REV. 1031, 1032, 1043, 1060 (2017) (confirming longstanding trend that two-thirds of consumers who begin Chapter 13 repayment plans do not complete them, and Black people are more likely not to complete those repayment plans); Jean Braucher, Dov Cohen & Robert M. Lawless, *Race, Attorney Influence, and Bankruptcy Chapter Choice*, 9 J. EMPIRICAL LEGAL STUD. 393, 420–21 (2012).

65 *See* H.R. REP NO. 105-794, at 121 (1998) (Conf. Rep.) (stating that House version steered debtors into Chapter 13 repayment, and aspects of that approach were retained); *see also* Jensen, *supra* note 63, at 501–11.

66 *See, e.g.*, 11 U.S.C. § 707(b)(2) (barring some debtors from Chapter 7 and hence forcing them into Chapter 13).

67 *E.g.*, U.N. COMM'N ON INT'L TRADE L., UNCITRAL LEGISLATIVE GUIDE ON INSOLVENCY LAW FOR MICRO- AND SMALL ENTERPRISES, at 28, U.N. Sales No. E.22.V.18 (2022), https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/msme_lg_insolvency_law_ebook.pdf [https://perma.cc/Y2AY-TGJE].

nuanced idea that it is not *discharge writ large* but *discharge tempered by abuse safeguards* that forms the theoretical core of a consumer bankruptcy system. This focus on an "abuse-policed discharge" will accordingly guide the subsequent consideration of a consumer bankruptcy scheme.

C. *Other Potentially Constitutive Attributes of Consumer Bankruptcy*

In addition to the abuse-policed discharge, other aspects of consumer bankruptcy law may be essential for a coherent system of financial relief.[68] In the interest of brevity, the reader is left to make the connection back from these proposed key attributes to the normative themes of consumer bankruptcy law canvassed above.

First, bankruptcy law plausibly requires, indeed as perhaps a necessary incidence to the concept of discharge and a fresh start, *collectivity*. The very conceptualization of the in rem nature of bankruptcy relief suggests an all-in approach to debt adjustment, and international instruments have explicitly emphasized this collectivity.[69] There are normative reasons why this is so. For example, the canonical creditors' bargain theory of bankruptcy mentioned above contends that for bankruptcy to work all creditors must be corralled into a group proceeding to blunt their destructive and ultimately self-defeating desires to grab assets and dismantle a debtor.[70] But there are also constitutional

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68 The deeply skeptical will get off the bus here:

> I should like to remark that any sort of 'ontological perspective' on the issue should be ruled out at the outset. There is no such thing as 'the nature' of an insolvency proceeding out of which certain characteristics of such a proceeding could be derived. Insolvency proceedings are jurisprudential and legal artefacts. Their normative features are based on a reasoned determination of the lawmaker in every individual case. Moreover, an abstract definition of 'insolvency proceeding' also is not helpful to adequately addressing the characterization problem.

Horst Eidenmüller, *What Is an Insolvency Proceeding?*, 92 AM. BANKR. L.J. 53, 65–66 (2018). The reader is nonetheless urged to press on.

69 In the development of the UNCITRAL Model Law on Cross-Border Insolvency (MLCBI), the Working Group on Insolvency Law's initial definition of an insolvency proceeding to mean "a judicial or administrative proceeding . . . for the purpose of liquidating the assets of a debtor for distribution to its creditors or adjusting the debts of a debtor to its creditors," was rejected for lack of a collectivity component, with its final definition including the modifier "collective" before "judicial or administrative." G. Ray Warner, *Comparative Collectivity: European Union and United States Approaches*, 32 INT'L INSOLVENCY REV. 156, 159 (2023) (quoting U.N. Comm'n on Int'l Trade L., Rep. of the Working Grp. on Insolvency L. on the Work of the Eighteenth Session, U.N. Doc. A/CN.9/419 (1995)). For thorough treatment of the UNCITRAL inclusion of collectivity, see *id.* at 158–59.

70 *See* JACKSON, LOGIC AND LIMITS, *supra* note 31.

reasons, at least in federal systems, such as the United States, where the central government houses "insolvency" power but not general residual common law legal authority.[71] Bankruptcy is but one member of the debtor-creditor law family (albeit the swaggering juggernaut); the primary content of collection law is at the state level. One creditor suing a debtor for judgment and initiating various collection writs all occurs under state law.[72] Bankruptcy, it is traditionally thought, is something different, which requires more than just a one-off creditor dispute; it's a group affair.[73] So rooted is this understanding of collectivity to the conceptual core of bankruptcy that U.S. bankruptcy courts will often dismiss a petition for failure to be filed in good faith if debtors really only have one creditor in conflict and are accessing bankruptcy relief to frustrate state law collection.[74] To be sure, the era of collectivity may be coming to a close if we look at the modern world of cross-border corporate insolvency (which we will below), but for now it suffices to observe that collectivity seems baked into the fabric of traditional conceptions of consumer bankruptcy and the fresh start.

Related to—and again, perhaps immanent in—this concept of collectivity is a *stay* or *moratorium*. A bankruptcy petition's invocation of an automatic stay to halt all collection activity makes clear not only that piecemeal dismemberment of debtors will not be tolerated, but that any ongoing disputes percolating in state court collection proceedings grind to a standstill and get effectively transferred (sublimated?) to the federal bankruptcy court housing the debtors' cases.[75] This centralization and control underscores that it is the bankruptcy proceeding that is paramount and will resolve, definitively, the debtor's various financial skirmishes. Hence, atomistic legal activity gives way to a collective affair. Readers can decide whether they code collectivity and moratorium as two or one constitutive elements to a bankruptcy proceeding in service of the ultimate goal of conferral of discharge. Many other bankruptcy law

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71 U.S. CONST. art. I, § 8, cl. 4; *cf.* Jacob Ziegel, *What Can the United States Learn from the Canadian Means Testing System?*, 2007 U. ILL. L. REV 195, 196–98 (discussing Canadian constitutional allocation).

72 *See, e.g.*, Duke v. Garcia, No. 11-CV-784, 2014 WL 1318646 (D.N.M. Feb. 28, 2014).

73 WARREN, WESTBROOK, PORTER & POTTOW, *supra* note 8, at 219–20.

74 *See, e.g.*, Indus. Ins. Servs., Inc. v. Zick (*In re* Zick), 931 F.2d 1124 (6th Cir. 1991) (dismissing the petition for bad faith after the debtor filed for bankruptcy solely in response to an adverse mediation award); *see also infra* notes 335–39 and accompanying text.

75 11 U.S.C. § 362; *see* Frank R. Kennedy, *The Automatic Stay in Bankruptcy*, 11 U. MICH. J. L. REFORM 175, 177–79 (1978); UNITED NATIONS COMM'N ON INT'L TRADE L., LEGISLATIVE GUIDE ON INSOLVENCY LAW, at 83–94, U.N. Sales No. E.05.V.10 (2005), https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/05-80722_ebook.pdf [https://web.archive.org/web/20231221195951/https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/05-80722_ebook.pdf].

provisions, such as the voidability of preferences,[76] can be explained with reference to the collectivity requirement.

Next, and this may be nonobvious to some, the ranking of *priority* of distribution of claims to a debtor's limited assets is essential to bankruptcy law.[77] The possibly counterintuitive nature of this assertion stems from those who subscribe to what has been called, infelicitously, a "proceduralist" view of bankruptcy law.[78] They follow and double down on the creditors' bargain theory, arguing that because bankruptcy law's sole telos is to solve collective action problems, it must strictly track legal entitlements at state law (among other reasons, to prevent whether-to-file incentive distortions).[79] Any dalliance into the love that dare not speak its name—redistribution—is an abomination.[80] Hence, specifying an order of payout under federal law, unmoored from the rights bargained for ex ante by contract, violates this parsimonious view of the proper scope of bankruptcy law. But, yet again, this proposition, like all normative theories of bankruptcy, is contested. Nor is it intrinsically economic. For even respected economists such as Professor Barry Adler have pushed back and suggested that the actual ranking of claims—with all the necessary redistribution that might carry—is an essential feature of bankruptcy law, a "primitive."[81] This characterization is apt, he argues, because these rules effect the state's distribution of negotiating endowments that facilitate the jockeying procedures of a corporate reorganization that allow self-resolution outside court.[82] This is so even if the substantive decisions of that regime often defer to the outcome at state law.[83] Priority of distribution, then, does fall within the necessary core of constitutive bankruptcy rules. And indeed, this element likewise relates to collectivity: if you are going to insist that everyone be corralled into the

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[76] 11 U.S.C. § 547. Voidable preference law requires a creditor who is paid on the eve of bankruptcy, and hence receives a better distribution than the paltry spoils of the bankruptcy estate, to return the money for pro rata distribution to the collective. Collectivity is taken seriously; the early bird has to give back the worm. *See* Vern Countryman, *The Concept of a Voidable Preference in Bankruptcy*, 38 VAND. L. REV. 713, 715 (1985); Robert Weisberg, *Commercial Morality, the Merchant Character, and the History of the Voidable Preference*, 39 STAN. L. REV. 3, 33 (1986).

[77] *See* 11 U.S.C. § 507.

[78] *See, e.g.*, Charles W. Mooney, Jr., *A Normative Theory of Bankruptcy Law: Bankruptcy as (Is) Civil Procedure*, 61 WASH. & LEE L. REV. 931, 946–51 (2004).

[79] *See, e.g.*, Douglas G. Baird & Robert K. Rasmussen, *The End of Bankruptcy*, 55 STAN. L. REV. 751, 753, 777 (2002).

[80] *See, e.g.*, Douglas G. Baird, *Bankruptcy's Uncontested Axioms*, 108 YALE L.J. 573 (1998).

[81] Barry E. Adler, *Bankruptcy Primitives*, 12 AM. BANKR. INST. L. REV. 219, 234–36 (2004).

[82] *Id.* at 219.

[83] Butner v. United States, 440 U.S. 48, 54–55 (1979).

same room to resolve their claims, you have to spell out who gets what once they're there.

Finally, bankruptcy requires some system of public *oversight*. This suggestion is not just about court involvement, although to be sure, bankruptcy is in many parts of the world a legal proceeding. It is also because since the legal formalities of bankruptcy law require the creation of an estate to be administered,[84] someone has to do the administering.[85] Most systems around the world involve an official, such as a trustee, administrator, receiver, or even an "insolvency representative," as someone who carries duties not just to the debtor, but to the entire collective.[86] Arguably, a lesser form of this occurs at state law, where the sheriff seizes property under writs of *fieri facias* to realize collection of judgment creditors,[87] but the scale, numerosity of assets, and multiplicity of creditors all make the administration of a full bankruptcy system eminently more complex. Indeed, even the much-celebrated U.S. debtor-in-possession model,[88] which facially appears to reject the external administrator or overseer, explicitly saddles debtors with fiduciary obligations toward nonshareholder corporate constituents (read: creditors).[89] Always, of course, those obligations are overseen by a bankruptcy judge and vigorously scrutinized by a well-funded official committee of unsecured creditors,[90] with the U.S. trustee playing that role in the consumer realm.[91]

In sum, while the keystone of consumer bankruptcy is the concept of a discharge to forgive financial obligations, bankruptcy law arguably entails several other core components. Collectivity is baked into the traditional understanding of consumer bankruptcy law, along with the cognate legal doctrine of an all-inclusive estate, as is the priority and ranking ("treatment") of claims. To operationalize these concepts, the legal mechanism of a moratorium or stay is also central, as is a system of external administration, usually through a trustee in the consumer liquidation scenario overseen by a judicial actor. All these necessary components are part of a system that does not just provide a discharge but, importantly, a discharge tempered by anti-abuse safeguards. These safeguards in the U.S. Bankruptcy Code are doctrinally implemented

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84 11 U.S.C. § 541.

85 *Id.* § 1302(b).

86 U.N. COMM'N ON INT'L TRADE L., *supra* note 67, at 55.

87 *See, e.g.*, VA. CODE ANN. § 16.1-98 (2023).

88 11 U.S.C. § 1107.

89 *See, e.g.*, *id.* §§ 704(a)(1), (7)–(8), 1104(b); Stalnaker v. DLC, Ltd., 376 F.3d 819, 825 (8th Cir. 2004).

90 11 U.S.C. § 1102.

91 *Id.* § 1106.

through, directly, its anti-fraud quasi-punitive provisions, and, indirectly, through the grand bargain buy-ins for Chapter 7 (relinquishment of nonexempt assets) and Chapter 13 (tithing future income), along with residual discretionary power to police good faith.[92] All these constitutive components of a consumer bankruptcy system can be rationalized more or less with any of the normative theories described in the first Section of this Part. Yet as we turn to consider whether a consumer scheme is feasible, we will confront whether some of these traditional constructs of bankruptcy law will have to be sacrificed.

II. THE SCHEME OF ARRANGMENT AND THE BENEFITS OF MODULARITY

A. *Introduction to the Scheme*

Put simply, the British scheme of arrangement is a privately initiated but court-supervised supermajoritarian voting regime for recapitalizing a company in whole or in part. The modern version of the scheme is found in the Companies Act of 2006,[93] which was recently cleaned up and expanded under the Corporate Insolvency and Governance Act of 2020 (CIGA), specifically regarding Part 26 of the UK Companies Act.[94] Many peg the origin of the scheme to an 1862 Act,[95] but as diligent scholars, such as erstwhile Professor Riz Mokal, have explained, its origins, including some continental provenance in French *concordats* (both *amiable* and not) and Italian *salvocondotti*, go back well before that, all of which were aimed at solving the problem of holdout creditors who stymie voluntary private debt relief for a bankruptcy trader.[96] Indeed, the

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92 *Id.* §§ 707(b), 1325(a)(3).

93 Companies Act 2006, c. 46, §§ 895–901 (UK).

94 *Id.* pt. 26A, *amended by* Corporate Insolvency and Governance Act 2020, c. 12 (UK). For the definitive treatment of the scheme of arrangement, see JENNIFER PAYNE, SCHEMES OF ARRANGEMENT: THEORY, STRUCTURE AND OPERATION (2d ed. 2021).

95 Companies Act 1862, 25 & 26 Vict. c. 89 (Eng.).

96 *See* Louis Edward Levinthal, *The Early History of Bankruptcy Law*, 66 U. PA. L. REV. 223, 241–45 (1918); Israel Treiman, *Majority Control in Compositions: Its Historical Origins and Development*, 24 VA. L. REV. 507, 508–10 (1938); Dave De ruysscher, *At the End, the Creditors Win: Pre-Insolvency Proceedings in France, Belgium and the Netherlands (1807–c1910)*, 6 COMPAR. LEGAL HIST. 184, 189 (2018). Mokal self-deprecates his "absurdly abbreviated and deliberately selective canter through European bankruptcy law," but his summary of other historical developments is helpful. Mokal, *supra* note 8, at 425–29, 434–36. What is important is that he shows UK law lagged behind other jurisdictions, notably Italy, that had statutory means of binding minority holdouts to particular compositions. For example, drawing on Levinthal's *Early History*, he notes that medieval *concordat* (composition) procedures with the ability to bind dissidents to a privately negotiated prepack was "peculiarly an Italian institution." *Id.* at 435

anti-holdout inspiration for the English scheme can be seen in 1683's *Alderman Backwell's Case*,[97] in which a composition (a private, consensual adjustment of debt requiring creditor unanimity) was frustrated by a few creditor holdouts who drove Backwell into bankruptcy notwithstanding apparent widespread support of the composition by the vast majority of his other creditors. The case reports exasperation with a "few and unreasonable people,"[98] but Backwell's plea for assistance for help in Chancery from Baron Guillford, the Lord Keeper, was to no avail: the holdouts vetoed the composition and succeeded in procuring a bankruptcy commission.[99]

Perhaps in response to *Backwell*, longing for the days of bills of conformity[100] and a cosmopolitan embrace of the continental trends, Parliament enacted a statute in 1696, self-explanatorily named Act for Relief of Creditors, by making Compositions with their Debtors, in case Two Thirds in Number and Value do Agree.[101] That law lasted only a short time due to perceived fraudulent practices,[102] and so matters returned to the state of nature of private compositions and their required unanimity under what we now would call general contract law.

A second parliamentary crack was attempted in 1825, under which ninety percent of creditors (in amount and value) of a bankrupt trader could agree to a composition (proposed by the debtor or "his Friends") and bind the minority; but this procedure was available, by design, only for a debtor already in bankruptcy proceedings.[103] This act also introduced the two-meeting rule, carried through today, wherein at the first meeting the composition of the bankrupt debtor would be proposed (hence it was a postpetition composition, not a preventative endeavor),

(quoting Levinthal, *supra*, at 243) (noting Genovese law required a three-fifths creditor vote for voluntary bankruptcy cases and seven-eighths for involuntary ones).

97 Backwell's Case (1683) 23 Eng. Rep. 381; 1 Vern. 152.

98 *Id.* at 381, 1 Vern. at 152.

99 *Id.*, 1 Vern. at 153. Prior, English courts dabbled with "protection" orders, reminiscent of French *lettres de répit* and Low Countries *surséances*, which functioned as moratoria to help cajole a composition, and Chancery granted "bills of conformity," which ordered dissident holdouts to go along with majority supporters of a composition. These were abolished in the 1620s, which led to the Lord Keeper's impotence in *Backwell's Case*. Mokal, *supra* note 8, at 435–38.

100 Bills of conformity were precursors to the stay and discharge. *See supra* note 99.

101 Mokal, *supra* note 8, at 438 (citing Composition by Debtors Act, 8 & 9 Will. 3 c. 18 (Eng.)).

102 Mokal notes that the Preamble to the repealing statute complained that "many fraudulent Practices have been committed, by making pretended Agreements with Persons who were not real Creditors." *Id.* at 438–39 (quoting Composition by Debtors (Repeal) Act 1697, 9 Will. 3 c. 29 (Eng.)).

103 *Id.* at 439 (quoting Bankruptcy Act 1825, 6 Geo. 4 c. 16 § 133 (Eng.)). In England between 1570 and 1861, bankruptcy relief was limited to tradesmen. Levinthal, *supra* note 96, at 224 n.10; *see also* Jérôme Sgard, *Do Legal Origins Matter? The Case of Bankruptcy Laws in Europe 1808–1914*, 10 EUR. REV. ECON. HIST. 389, 403–04, 406 (2006).

and at the second meeting the creditors would vote to see whether the ninety percent threshold could be sustained.[104] A positive vote could allow the debtor's bankruptcy petition to be dismissed (formally, his bankruptcy commission to be discharged by the Lord Chancellor).[105] We hence see the involvement of the courts in a nominally private intracreditor affair, at least when the trader was in bankruptcy.[106]

In 1844, the law expanded under a new act to allow prebankruptcy (or nonbankruptcy) deals, similar to modern-day prepacks, enabling debtors to propose debt restructuring arrangements without needing to file bankruptcy. Instead of filing a formal bankruptcy petition to gain jurisdiction, debtors—a class now expanded to include nontraders—could simply request a commissioner to review the composition and its support.[107] If accompanied by agreement of one third of creditors, the commissioner could then convene a meeting to allow them a vote on the composition by all affected creditors. At the second meeting, were the proposal accepted by ninety percent of the creditors, it would become binding on the dissidents.[108] The debtor, however, was divested of assets, which were turned over to an assignee.[109]

In 1849, the bankruptcy laws were still further expanded (for traders and nontraders alike, the distinction by then having lost its historical relevance) under the Act to Amend and Consolidate the Laws Relating to Bankruptcy 1849, to allow both the postbankruptcy compositions (at a ninety percent threshold) and the prebankruptcy composition proposals (at a sixty percent vote), as well as a third procedure with less court involvement: a composition proposal accepted by two-thirds in value of debt and not challenged in court within three months.[110] By this point, these procedures were catching on. In 1861, the next revision to the Bankruptcy Act allowed debtors to retain ownership of assets (not divest them to an assignee), tinkered with the composition acceptance threshold (seventy-five percent in number and value) for discharging a bankruptcy petition, and even allowed prebankruptcy debtors to deed their property to creditors upon certification of approval by seventy-five percent in

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[104] 6 Geo. 4 c. 16, § 133.

[105] *Id.* § 122.

[106] *Id.* §§ 122–133.

[107] Arrangements Between Debtors and Creditors Act 1844, 7 & 8 Vict. c. 70 (Eng.).

[108] *Id.* §§ 1, 4–5. The voting thresholds were more complicated, depending on dollar amount and who actually showed up at the second meeting. Mokal, *supra* note 8, at 439. (In parallel, the first corporate winding-up act was passed.)

[109] 7 & 8 Vict. c. 70, § 8.

[110] Bankrupt Law Consolidation Act 1849, 12 & 13 Vict. c. 106, §§ 211–219, 225, 230 (Eng.).

value.[111] This bound the dissident minority and absolved the debtor of further liability.

Then came the Companies Act 1862, which imported these antiholdout composition bankruptcy procedures into the corporate world (corporations being ineligible for bankruptcy) by extending them to companies in winding-up (liquidation) proceedings. The company could propose an "arrangement" to its creditors, which would become binding upon seventy-five percent approval of creditors (number and value) and seventy-five percent of the stockholding members, that would shift decision-making control from the members to the creditors to engage the winding-up liquidator—and maybe even accept a compromise.[112] Judicial involvement was present but light-touch. For example, no formal approval was structurally required, only the statutory power of the court to vary, amend, or confirm the arrangement upon review of a timely creditor or member objection.[113] An 1870 amendment, the Joint Stock Companies Arrangement Act 1870,[114] strengthened court involvement by granting the power to order creditors to assemble for a meeting and vote on the "scheme." It also expressly included the power to bind dissidents (to the compromise of liquidating debts, not just to the turnover of control to the creditors).[115] In 1900, the Act was amended again.[116] But perhaps the most important revision came in 1907 when, in response to a 1906 Company Law Amendment Committee recommendation,[117] the Act was expanded to allow for arrangements or compromises *beyond corporate liquidation scenarios* (i.e., as a rehabilitation procedure to prevent the need to wind up the company in the first place).[118] The 1906 Committee concluded:

> We think that the provisions of the Joint Stock Companies Arrangement Act, 1870, should be extended so as to enable a company, without going into liquidation, to effect a compromise or arrangement with its creditors subject to the sanction of the Court, and with the safeguards imposed by the Act.[119]

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111 Bankruptcy Act 1861, 24 & 25 Vict. c. 134, §§ 185–192 (Eng.).

112 Companies Act 1862, 25 & 26 Vict. c. 89, § 136 (Eng.).

113 *Id.* § 137.

114 Joint Stock Companies Arrangement Act 1870, 33 & 34 Vict. c. 104 (Eng.).

115 *Id.* § 2.

116 Companies Act 1900, 63 & 64 Vict. c. 48 (Eng.).

117 COMPANY LAW AMENDMENT COMMITTEE, REPORT OF COMMITTEE, 1906, Cd. 3052, ¶ 54 (Eng.).

118 Companies Act 1907, 7 Edw. 7 c. 50, §§ 38–39 (Eng.) (later consolidated into Companies (Consolidation) Act 1908, 8 Edw. 7 c. 69, § 120 (Eng.), then Companies Act 2006, c. 46, § 899(1) (UK)).

119 1906, Cd. 3052, ¶ 54.

The substance of the scheme of arrangement procedure was thus settled by 1907 and is still in essence what is used today. Importantly, not only do the creditors show up and vote on the scheme, they vote by class, designated by the debtor, which designation is subject to approval by the court at the first judicial meeting.[120] Thus, the debtors may restructure one class of debt only, or multiple classes of debt, which is the cornerstone to the scheme's modularity. For example, the scheme can propose an adjustment to a company's financial debt but leave trade debt unaffected.[121]

The corporate scheme of arrangement may be summarized thus: a privately initiated, two-meeting procedure (really, a three-meeting procedure) with a supermajoritarian voting rule that allows a court to "sanction" an approved recapitalization that will bind dissidents. The first (court) meeting is just to confirm the voting classes have been properly constituted and that the debtor can convene the creditors'/members' meeting, "emphatically not . . . to consider the merits and fairness of the scheme[]";[122] the second is the actual (nonjudicial) meeting and vote on the presented plan by the affected stakeholders; and the third is a return to court to report on that vote and seek judicial sanction of the plan, which under the statute the court "may," but not must, do.[123]

Upon sanction, the plan becomes binding on dissidents after deposit at the Companies Registry.[124] This final stage does involve judicial review, which Professors Paterson and Walters characterize as "holistic fairness review."[125] This review allows judicial oversight of claims under a broad discretion but scant legislative guidance—although, to be fair, over a century of jurisprudence.[126] The intervention is deliberately light touch. For example, Justice Snowden's summary of the flexible judicial review conducted at the sanctioning hearing relevantly includes in its multi-factored analysis: "[T]he Court must consider whether the scheme is a fair scheme which a creditor could reasonably approve. Importantly, it must be appreciated that the Court is not concerned to decide whether the scheme is the only fair scheme or even the 'best' scheme."[127] Also: "[T]he Court must consider whether . . . the majority were coercing the

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120 Companies Act 2006 §§ 896, 899.

121 Re The Co-Operative Bank Plc [2017] EWHC (Ch) 2269 (Eng.); *see also* PAYNE, *supra* note 94, at 232–33 ("It is an important and valuable aspect of schemes that companies do not need to deal with all of their creditors . . . ."); Re The Brit. Aviation Ins. Co. [2005] EWHC (Ch.) 1621 [96] (Eng.).

122 Re Telewest Comms. Plc (No. 1), [2004] EWHC (Ch) 924 [14].

123 Companies Act 2006 § 899(1).

124 *Id.* § 901F(6)(b).

125 Paterson & Walters, *supra* note 3 (manuscript at 44).

126 *See id.*

127 Re Noble Group Ltd. [2018] EWHC (Ch) 3092 [17] (Eng.).

minority in order to promote interests adverse to the class whom they purported to represent."[128] This final judicial fairness review is an "important cross-check"[129] and can focus on potential majority exploitation of the minority, including whether the scheme is "unduly favourable to those left outside the Scheme."[130] In other words, since schemes are debtor initiated, it is an abuse-prevention check in the corporate sphere.

* * * * *

Looking at the scheme, which has only become more popular with time, we observe the following characteristics. First, there is *no automatic stay*.[131] Nor is there even an *estate*. Second, there are *no distribution rules*. Unlike U.S. Chapter 11, which has a strict absolute priority rule governing contested corporate reorganizations,[132] a scheme can formally allow creditors to vote for anything; equity need not be wiped out in the face of objection. Third, there is only *minimal court oversight*. Most of the work occurs offstage by the private parties, subject only to the two court hearings. Fourth, there is no requirement of *insolvency*. Indeed, the scheme is a popular mechanism for effecting corporate takeover transactions having nothing to do with financial distress.[133] Most significantly, however, the procedure is *not collective*, at least not in the comprehensive sense.[134] For instance, there are no voidable preferences to be returned to the estate, because there is no estate. Using the constitutive criteria for insolvency proceedings offered in the first part of this Article, it is hard to make the case that these even are insolvency proceedings, a taxonomic point that has caused some jurisprudential heartache in the EU.[135]

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128 *Id.*

129 Paterson & Walters, *supra* note 3 (manuscript at 45) (quoting Re Amicus Finance Plc (In Administration) [2021] EWHC (Ch) 3036 [40] (Eng.)).

130 Sea Assets Ltd. v. Perusahaan Perseroan (Persero) PT Perusahaan Penerbangan Garuda Indon. [2001] EWCA (Civ) 1696 [51] (Eng.).

131 There is a new Part A1 moratorium under the CIGA 2020 that allows a discretionary stay to assist a scheme, Corporate Insolvency and Governance Act 2020, c. 12 (UK), and there is also a stay that can be applied if the debtor files for administration proceedings (more traditional UK corporate reorganization proceedings) alongside its scheme, Companies Act 2006, c. 46 (UK).

132 11 U.S.C. § 1129(b).

133 *E.g.*, Re Jelf Group Plc [2015] EWHC (Ch) 3857 [4].

134 Armada (Sing.) Pte Ltd. v. Shah (*In re* Ashapura Minechem Ltd.), 480 B.R. 129, 141 (S.D.N.Y. 2012); *see infra* note 320 and accompanying text.

135 Under the EU Insolvency Regulation, they are not listed in Annex A, so are not insolvency proceedings as a matter of law. Under UK jurisprudence, however, they may be "insolvency proceedings" for purposes of the insolvency exclusions from, for example, the Brussels Regulations or, in a post-Brexit world, the Lugano Convention. *See* Re Gategroup Guarantee Ltd. [2021] EWHC

To be sure, schemes involve multiple creditors, otherwise there would be no voting thresholds, but they are, in the words of Paterson and Walters, "selective" procedures that often target only part of corporate debt, not all.[136] This contrasts markedly with Chapter 11, which is an "inclusive" procedure that corrals all creditors into a comprehensive reckoning ("the whole shebang").[137] Equally important, however, is that schemes do allow upon court sanction *discharge* of indebtedness by binding dissident minority creditors intraclass. And, relatedly, they provide for *abuse prevention* by means of the holistic fairness review of court oversight at the final stage of the sanctioning hearing, albeit with a much more fluid guardrail than the Chapter 7 and Chapter 13 U.S. consumer grand bargain. In sum, they provide modular abuse-policed discharge.

Schemes are popular. So popular, that the National Bankruptcy Conference in the United States urged a Chapter 16 proceeding for bond debt as a "selective" procedure modeled after the scheme, urging its efficiency in allowing majoritarian debt modification for a creditor class "without triggering the whole panoply of Bankruptcy Code provisions, requirements and limitations that typically accompany the filing of a petition under the Bankruptcy Code."[138] The normative case for these selective debt readjustments comes from the same intuition that drives the current movement of preventative restructuring.[139] Earlier intervention on the "demise curve"[140] of a debtor is likely to be less costly, both for direct and indirect costs,[141] and more likely only to involve single classes of creditors, before incipient financial distress worsens into

(Ch) 304 [109]–[131] (Eng.) (finding Part 26A restructuring proceeding—largely the same as a scheme but with cross-class cramdown powers—to be "insolvency proceedings" for purposes of Lugano).

136 Paterson & Walters, *supra* note 3 (manuscript at 28).

137 *Id.* (manuscript at 19); *see* also 11 U.S.C. § 541 (constituting estate of all debtor's property).

138 NAT'L BANKR. CONF., PROPOSAL FOR A NEW CHAPTER FOR RESTRUCTURING BOND AND CREDIT AGREEMENT DEBT (CHAPTER 16) 2 (2014), http://nbconf.org/wp-content/uploads/2015/07/Proposed-Amendments-to-Bankruptcy-Code-to-Facilitate-Restructuring-of-Bond-and-Credit-Agreement-Debt.pdf [https://perma.cc/5NFH-C66F] (proposing new financial creditors restructuring chapter).

139 *See* EXTERNAL EVALUATION OF REGULATION NO. 1346/2000/EC ON INSOLVENCY PROCEEDINGS, JUST/2011/JCIV/PR0049/A4 (Burkhard Hess, Paul Oberhammer & Thomas Peiffer, eds., 2013), https://op.europa.eu/en/publication-detail/-/publication/4d756fa7-b860-4e36-b1f8-c6640dced486 [https://perma.cc/Z8ZD-5GVE].

140 Paterson & Walters, *supra* note 3.

141 Direct costs include the resources expended to restructure, like multilateral bargaining; indirect costs include the effects on parties not related to the restructuring process, like ensuring customers will be served despite the debtor financial difficulties. *See, e.g.*, *id.* (manuscript at 14–16).

general crisis.[142] The alternative of requiring comprehensive reckoning of all creditors at the same time, as U.S. Chapter 11 requires, is actually a mistake: it can encourage more borrowing to try to finance the way out of crisis rather than discretely focused legal intervention.[143] Finally, perhaps precisely because the procedure is selective and therefore some creditors get to "ride through unimpaired,"[144] the fairness review can focus not just on the terms of the haircut, but on why the compromised class had to take a haircut and the unscathed did not.[145] Thus, the design of the scheme's abuse prevention safeguard is explicitly aware of the potential for mischief by a modular proceeding that only targets one group of stakeholders—a question U.S. law has not (yet) had to confront.[146]

B. *The Case for Modularity*

Modularity is a means of managing complex systems that, among other benefits, reduces interdependency risk by hiving off semiautonomous, simplified "modules" that connect to the whole through limited interfaces.[147] If one module fails, the whole system doesn't collapse. The case for modular consumer insolvency proceedings

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142 *See* Preventative Restructuring Directive, *supra* note 18, recital 24, at 22 ("A restructuring framework should be available to debtors . . . to enable them to address their financial difficulties at an early stage, when it appears likely that their insolvency can be prevented and the viability of the business can be ensured.").

143 Professors Paterson and Walters suggest this defect of Chapter 11 is so distortive it requires synthetic and at times contrived workarounds to achieve the benefits of modular selectivity within the constraint of forced inclusivity. Paterson & Walters, *supra* note 3 (manuscript at 28–41).

144 *Id.* (manuscript at 32).

145 *See, e.g.*, Re Virgin Active Holdings Ltd. [2021] EWHC (Ch) 1246 [266]–[269] (discussing gifting between the senior and junior class as justification for arrangement).

146 *Cf.* 11 U.S.C. § 1129 (preventing unfair discrimination in certain contested reorganizations).

147 *See, e.g.*, Richard N. Langlois, *Modularity in Technology and Organization*, 49 J. ECON. BEHAV. & ORG. 19, 19 (2002). An excellent discussion of modularity in cross-border insolvency law is found in Andrew B. Dawson, *Modularity in Cross-Border Insolvency*, 93 CHI.-KENT L. REV. 677, 679–80 (2018), which contrasts *Game of Thrones* with *Law & Order*. Henry Smith's work on contract boilerplate, Henry E. Smith, *Modularity in Contracts: Boilerplate and Information Flow*, 104 MICH. L. REV. 1175, 1196 (2006), and Cathy Hwang's M&A research, Cathy Hwang, *Unbundled Bargains: Multi-Agreement Dealmaking in Complex Mergers and Acquisitions*, 164 U. PA. L. REV. 1403, 1417–18 (2016), use modularity analysis, which is indeed the premise of the "asset partitioning" strand (dare one say, module?) of corporate scholarship, *see, e.g.*, Henry Hansmann & Reinier Kraakman, *The Essential Role of Organizational Law*, 110 YALE L.J. 387, 399 (2000). For its usage in a broad-reaching normative proposal for micro-, small-, and medium-sized enterprise (MSME) bankruptcy reform, see RONALD DAVIS ET AL., FINANCIAL INSTITUTIONS IN DISTRESS: RECOVERY, RESOLUTION, RECOGNITION (2023).

is anchored in similar justifications that drive the scheme. One such overarching theme is debtor heterogeneity: some debtors may find it to their benefit to restructure a single or only some of their financial affairs without a proceeding that dragoons all their creditors into compulsory collectivity—a concern that invokes the interdependency risk modularity seeks to mitigate. Targeted intervention may also stave off broader financial crisis.[148]

Moreover, cost is an especially salient consideration in consumer affairs. The median attorney cost of a Chapter 7 case is $1,229 and Chapter 13 is $3,217.[149] These are in addition to the statutory filing fees of $335 and $310, respectively.[150] Cost correlates with complexity, and it is well documented in the consumer bankruptcy literature how costs swelled upon passage of the BAPCPA amendments, whose complexity was not only notorious but argued by some to be a feature of intentional design of the legislation.[151] The goal of a modular proceeding would be to simplify a plenary Chapter 7 or 13 by requiring limited involvement of debtor stakeholders (and hence limited paperwork). For example, if only the debtors' landlords were involved in a hypothetical "tenant subchapter scheme," under which the debtors and their landlords would restructure only a residential rent arrearage, there would be no need to involve the debtors' car lenders, credit card issuers, and student loan servicers.[152] It would be, like the British scheme, a selective procedure, involving none of those stakeholders. Fewer participants means fewer pleadings to review and fewer motions to defend for the debtor's counsel, presumably translating into a lower cost of representation and greater access to justice. As many systems around the world grapple with "no income, no

148 *See* Recast Insolvency Regulation, *supra* note 6, recital 24, at 21; Paterson & Walters, *supra* note 3 (manuscript at 3–4).

149 Pamela Foohey, Robert M. Lawless, Katherine Porter & Deborah Thorne, *"No Money Down" Bankruptcy*, 90 S. CAL. L. REV. 1055, 1058 (2017).

150 *Id.* at 1058 n.10; *see also* 28 U.S.C. § 1930; FED. R. BANKR. P. 1006.

151 Ronald J. Mann, *Bankruptcy Reform and the "Sweat Box" of Credit Card Debt*, 2007 U. ILL. L. REV. 375, 398.

152 One scholar actually speculated about such a modular procedure during the subprime housing crisis. Jonathan C. Lipson, *Debt and Democracy: Towards a Constitutional Theory of Bankruptcy*, 83 NOTRE DAME L. REV 605, 692–93 (2008).

asset" cases,[153] the drive for simpler and less expensive debt relief procedures is growing.[154]

The case for a modular system, as mentioned, is mainly premised upon a belief in the benefits of individual tailoring in a heterogeneous-debtor world. The data we do have on usage patterns of the U.S. consumer bankruptcy system indeed support the idea that some consumers have limited need for bankruptcy relief. For example, much classic literature on this point pertains to the "save the home" Chapter 13, where debtors report that the primary usage of the bankruptcy system was not generalized financial relief by way of discharge but to use its automatic stay to shelter a workout on a defaulted home mortgage.[155] Unsurprisingly, several policy proposals over the years have embraced the idea of limited bankruptcy proceedings of some form or other.[156]

Recent data from the Consumer Bankruptcy Project (CBP), the premier empirical study of U.S. consumer debtors,[157] provide the first in-depth report on the specific attributes of car debtors.[158] The granular insight it sheds on the role of automotive debt enhances our knowledge of consumer distress significantly. Among the various findings are that about eighty-three percent of bankruptcy filers own a car and, of that sizable cohort, half have secured debts encumbering their vehicles.[159] Furthermore, one-third reported cars going into repossession, indicating that "car distress" is a frequent phenomenon among U.S. bankruptcy filers.[160]

These data are on the aggregate level. What the authors are also able to find through cluster analysis is even more informative, because their data naturally divide into four debtor groups with different attributes. One cluster, for example, finds debtors, generally better resourced, who

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153 THE WORLD BANK GRP., WORLD DEVELOPMENT REPORT 2022: FINANCE FOR AN EQUITABLE RECOVERY 136–41 (2022), https://documents1.worldbank.org/curated/en/408661644986413472/pdf/World-Development-Report-2022-Finance-for-an-Equitable-Recovery.pdf [https://perma.cc/8PKS-29UW]; U.N. COMM'N ON INT'L TRADE L., *supra* note 67; Recast Insolvency Regulation, *supra* note 6, recital 16 (discussing no income, no asset cases).

154 Other, more technical reasons will also affect the demand for partial bankruptcy. See *infra* note 206 on cross-default and ipso facto clauses and the need to include statutory provisions "inoculating" the scheme from triggering cross-default clauses.

155 *See, e.g.*, Melissa B. Jacoby, *Bankruptcy Reform and Homeownership Risk*, 2007 U. ILL. L. REV. 323.

156 *See, e.g.*, Medical Debt Relief Act of 2021, S. 214, 117th Cong. (2021).

157 *See* Pamela Foohey, Robert M. Lawless & Deborah Thorne, *Portraits of Bankruptcy Filers*, 56 GA. L. REV. 573, 596–98 (2022) [hereinafter Foohey, Lawless & Thorne, *Portraits*].

158 *See* Pamela Foohey, Robert M. Lawless & Deborah Thorne, *Driven to Bankruptcy*, 55 WAKE FOREST L. REV. 287 (2020) [hereinafter Foohey, Lawless & Thorne, *Driven*].

159 *Id.* at 308 tbl.1; Marianne B. Culhane & Michaela M. White, *Debt After Discharge: An Empirical Study of Reaffirmation*, 73 AM. BANKR. L.J. 709, 738 (1999).

160 Foohey, Lawless & Thorne, *Driven*, *supra* note 158, at 294.

combine car ownership with homeownership.[161] But another cluster (two clusters, actually) shows a cohort of debtors with cars as their only major asset.[162] Many of these debtors file reaffirmation agreements with their car lenders (one cluster skewed toward Chapter 7, another, regressively, toward Chapter 13—often with negative equity in their cars).[163] For these debtors—or at the very least, some important subset of them—we can assume that they have car distress financially but not necessarily other financial distress. Indeed, we may also likely assume that a nontrivial portion of the combined car-and-homeowner cluster debtors have car problems without necessarily also having home problems.

The point of describing these cluster findings of the CBP is to underscore that they provide empirical evidence consistent with the intuition of consumer debtor heterogeneity. Some debtors have multiple debts; some debtors have mostly car debt. To force all debtors to go through a one-size-fits-all process adds unnecessary complexity to a system that subjects other creditors to wasteful legal proceedings and debtors to unwarranted costs. Additionally, the ride-through data indirectly support this observation as well, as twenty percent of debtors try to ride through their car debt, meaning that they do not want the bankruptcy system to have anything to do with them.[164] Since nobody files bankruptcy just to ride through on a nondefaulted car loan (what would be the point?), presumably, those debtors are addressing other forms of nonautomotive financial distress (e.g., home mortgage or credit cards) and have neither desire nor need to drag their car lenders through bankruptcy, with the attendant cost and complexity that adding more invitations to the litigation party entails—more evidence of pent-up demand for modularity.

The cost issue does indeed loom large in the empirical literature. Even apart from the racial disparities in Chapter 13 well documented in other studies, the CBP data suggest a cluster of debtors who have negative car equity but nonetheless file Chapter 13, indicating that they are succumbing to the "no money down" 13 where they elect a suboptimal chapter choice solely to finance legal representation.[165] Accordingly, some of the most recent empirical work we have on the consumer

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161 *Id.* at 317–18.

162 *Id.* at 318.

163 *Id.* at 319, 321. Reaffirmation agreements are court-approved contracts between the bankruptcy debtor and a creditor to waive the discharge and reaffirm (on the same or mutually negotiated new terms) a specific debt. 11 U.S.C. § 524.

164 Foohey, Lawless & Thorne, *Driven*, *supra* note 158, at 312, 321. "Ride-through" is when consumer debtors neither reaffirm, redeem, nor surrender collateral securing a debt. It is a robust pattern of ignoring the strictures of bankruptcy law in an attempt to "keep on keeping on."

165 *See id.* at 322; Foohey, Lawless, Porter & Thorne, *supra* note 149, at 1099–100.

bankruptcy system suggests a diverse array of consumer debtors, and also show that many of that diverse array have automotive debt.[166] These "car only" debtors support the idea that modular proceedings, exclusively focused on car relief, could well attract many filers.

III. THE CONSUMER SCHEME OF ARRANGEMENT

While a traditional corporate scheme of arrangement stratifies investment creditors based on their *debt classes* (by tranche or even issuance),[167] a consumer scheme would not have those naturally occurring presorting mechanisms. On the contrary, what is more natural for a consumer scheme would be an *asset-based* sorting, at least for the prevalent secured debt that dominates many indebted consumers.[168] Accordingly, it might be more pragmatic to envision modular consumer bankruptcy relief as being designed around asset classes rather than the creditor classes a traditional scheme of arrangement uses given the prevalence of secured consumer debt.[169] Such an asset-based approach would be unprecedented for the consumer bankruptcy system.[170] The two most prevalent consumer collateral types for consumer secured debt are homes (mortgage debt) and cars (auto debt).[171] This Article will discuss car debt as a simple building block to envision what a restricted-scope "car scheme" might look like. To do so, analysis must begin with the Code's traditional treatment of consumer secured debt and then proceed to consider how that approach would work with both over- and undersecured car loans. But first, an overview of what the proposal envisions. Necessarily, we will get into the weeds of the U.S. bankruptcy law of secured claims; the reader has been warned.

A. *The Car Scheme: An Overview*

Much like a corporate scheme of arrangement debtor who wants to propose a workout to defaulted bonds but otherwise leave its trade creditors unimpaired, a "car scheme" consumer debtor would proceed the same way. The debtor would seek court intervention by filing a

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166 *See* Foohey, Lawless & Thorne, *Driven*, *supra* note 158.

167 *See, e.g.*, Re Hertz UK Receivables Ltd. (2020) EWHC (Ch) 3649 (Eng.).

168 *See* Foohey, Lawless & Thorne, *Portraits*, *supra* note 157, at 604–05.

169 To be sure, the sizable amount of unsecured consumer debt, principally credit cards, requires consideration as well, a question for another day.

170 *Cf.* 11 U.S.C. § 1520 (limiting stay in Chapter 15 to assets physically situated within U.S. territory)

171 Foohey, Lawless & Thorne, *Portraits*, *supra* note 157, at 604–05.

petition to alleviate distress with the car lender but leave all other debts unaffected by this partial bankruptcy. The anticipated car scheme scenario would perhaps involve debtors who have fallen behind on their car payments and maybe even faced imminent or actual repossession.[172] The car scheme would thus allow debtors to file a limited bankruptcy petition *restricted to the car debt*, perhaps under a new subchapter of the Code.

What would such a petition do? At the outset, it would impose a stay, but unlike the automatic stay of a plenary bankruptcy proceeding, this would be an asset-based stay, restricted in effect to the car. This would, like § 362,[173] apply both in rem to the car and in personam for collection actions against the debtor related to the car. The turnover rules in the event the car had been repossessed could be the same,[174] and so debtors presumably would have to ensure adequate protection for the return of a repossessed car.[175] Note that the proposed stay would depart intentionally from the corporate scheme of arrangement, where the stay is not automatic, because of the different dynamics of asset repossession of consumer collateral.[176]

The petition would then proceed more like a traditional Chapter 13 than a Chapter 7. That is, the debtor would propose a "car plan," perhaps commencing payments within a statutory deadline similar to Chapter 13's.[177] Debtors could, in this plan, propose to cure arrearages and could similarly modify the car loan within the confines of protecting the secured creditor's allowed secured claim, just as is generally permissible in current Chapter 13.[178] Upon confirmation of that plan, debtors would receive whatever discharge would be appropriate (more on that below) and the case would be closed. This would be a departure from Chapter 13 practice, where debtors have to complete plan payments before receiving

172 CONSUMER FIN. PROT. BUREAU, SINGLE-PAYMENT VEHICLE TITLE LENDING 23 tbl.7 (2016), https://files.consumerfinance.gov/f/documents/201605_cfpb_single-payment-vehicle-title-lending.pdf [https://perma.cc/U89A-GQP8] (finding one in five auto title loans end in car repossession).

173 11 U.S.C. § 362.

174 *Id.* § 542.

175 *See, e.g.*, City of Chicago v. Fulton, 592 U.S. 154 (2021); United States v. Whiting Pools, Inc., 462 U.S. 198 (1983).

176 *See* Bluecrest Mercantile BV v. Viet. Shipbuilding Indus. Grp. & Ors. [2013] EWHC (Comm) 1146 (Eng.). Personal property repossession of consumer debt, especially cars, is swift, commonplace, and outsourced to a thick market. A collection stay is thus more urgent in the consumer realm than relying upon the genteel restraint of commercial lenders that is found in the traditional scheme.

177 11 U.S.C. § 1322(d).

178 *Id.* § 1322(b).

a discharge.[179] But there is no reason why the scheme-inspired approach could not mimic the faster closure of a Chapter 11 case, which effectively ends at confirmation.

Would such a limited proceeding even be a "bankruptcy" case? So far, this approach sounds like it has at least one primary hallmark of a regular bankruptcy proceeding: a stay. But that is where the ready similarities end. There would be no priority rules (as there would only be one creditor claiming the res of the car), and there would be no collective of creditors. As for public oversight, while there would not be a trustee to take control of the car and liquidate it as there would be in Chapter 7, there would still be a court ensuring compliance with the statute, including protection of secured creditor rights.[180] This should all sound familiar to the reader: it is highly similar to the attributes of a scheme of arrangement. But as for the ultimate aspect of consumer bankruptcy discussed in the theoretical overview above—the discharge—the proposal requires further elaboration. This Article proposes two alternative versions of the outcome of a confirmed ("sanctioned") car scheme: a strong one, in which the debtor's proceeding *culminates in a discharge* of unsecured indebtedness *relating to the car*, and a weaker one, in which the debtor could *restructure* the car debt during the stay-protected breathing spell but *not receive a discharge* of any unsecured car debt.

That's it. The procedure is intentionally designed to be short and sweet: no voluminous collection of schedules and forms,[181] no compulsory credit counselling,[182] and not even necessarily a § 341 hearing,[183] all the hallmarks of traditional U.S. consumer bankruptcy. Nor would there be voidable preferences for trustees to chase or fraudulent preferences to claw back. Debtors would simply get a reprieve from the car distress accorded by the stay and then, subject to a suitably short time frame, either work out a consensual (like a scheme) or unilateral (like a Chapter 13) modified repayment term with the car creditor.

The proposal's ambivalence over discharge in offering both the strong and weak alternatives will be explained in more detail below, but, briefly, there is only a real need for discharge if there remains recourse liability for the underlying obligation.[184] Thus, we can envision two

179 *Id.* § 1328.

180 *See, e.g.*, *id.* § 362(d).

181 *See, e.g.*, FED. R. BANKR. P. 1007(b).

182 11 U.S.C. § 109(h)(1).

183 *Id.* § 341.

184 The authoritative interpretation of the U.S. Code undermines part of the in personam discharge by holding that the lien on collateral continues after Chapter 7 discharge to encumber it for the full amount of the prebankruptcy debt and is not capped by the amount of the allowed secured claim, which is the lower of the outstanding debt or collateral value, 11 U.S.C. § 506(b).

subtypes of car schemes: one in which creditors are undersecured, and so debtors have a deficiency claim to reckon with,[185] and the second in which creditors are oversecured, in which case debtors own equity in the car and thus do not really need a discharge, just a statutory modification power.[186]

This sounds simple as sketched out, but there are thorny problems with both the strong and weak proposal that correspond to both underwater and equity-containing cars. And both these subtypes of car schemes' problems are ones that corporate schemes of arrangement have not had to wrestle with in nearly the same way, requiring us to sail into some uncharted water. Specifically, regarding the underwater car scenario, the system would have to figure out to what extent the debtor can get a discharge of the deficiency claim and, importantly, given the normative analysis of consumer bankruptcy law above, what buy-in would sufficiently police moral hazard in the dispensation of such a discharge. Recall that the scheme of arrangement invokes a supermajoritarian creditor vote to bind dissidents to a haircut. Here, there is only one creditor, the car lender, who presumably is unhappy (otherwise, they would have assented to a consensual workout outside bankruptcy). But there is also the holistic fairness review with a scheme, which might need an analogue here. Regarding the oversecured car scheme, the system would have to wrestle with different issues: constitutional and policy questions as to whether this legal intervention could even be considered a "bankruptcy proceeding," and, if so, what to do fairly with the debtor's equity in the car. These difficulties will be addressed in sequence, beginning with a brief introduction to the treatment of secured debt—such as a car loan—and attendant secured creditor protections in conventional U.S. bankruptcy.

B. *Secured Debt Treatment in Conventional Bankruptcy*

The Bankruptcy Code subjects secured debt, consumer and business alike, to bifurcation into two claims against the bankruptcy estate: an allowed *secured claim* up to the lesser of the value of the collateral or the amount owing the creditor, and an allowed *unsecured claim* for any

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Dewsnup v. Timm, 502 U.S. 410, 417 (1992). Thus, the statement in the text above might be more accurate were it revised to say if the debt remains recourse *and* Dewsnup *is not overruled.* In Chapter 13, the *Dewsnup* issue does not arise because the lien itself is modified under the Chapter 13 plan. 11 U.S.C. § 1325(b)(2). Because the new "scheme" would be its own innovation to the Code, it presumably could borrow the lien modification power of Chapter 13 to avoid the *Dewsnup* problem.

185 The deficiency claim is the amount the lender is still owed after the collateral has been liquidated and applied to the loan balance. U.C.C. § 9-626 (AM. L. INST. & UNIF. L. COMM'N 2022).

186 11 U.S.C. § 1322.

"deficiency" (outstanding debt in excess of collateral value).[187] Thus, for any given car debt, the debtor may have one or two claims against the bankruptcy estate depending on whether the debt is over- or undersecured. Consider, for example, a debtor with a car loan of $10,000 secured by a purchase-money lien on the car. Depending on the correct value of the car—and for now leaving aside the complication of consumer exemptions—the lender could have an additional unsecured claim against the estate if the car note were undersecured.[188] For example, if the car were worth only $8,000, the car lender would have two claims in bankruptcy: a secured claim of $8,000 and an additional unsecured claim for $2,000.

But the creditor may be oversecured. Were the car worth $12,000, the creditor's allowed secured claim would be $10,000, capped at the full amount owing on the outstanding obligation. The additional $2,000 in car value would belong to the bankruptcy estate as "equity" in the car. In a conventional bankruptcy—again, leaving aside the complication of exemptions—that value would be available for distribution to the unsecured creditors pro rata as part of the debtor's estate.[189] In a Chapter 7, it would be liquidated by the trustee if not redeemed by the debtor or consensually reaffirmed with the lender.[190] In a Chapter 13, that equity would remain the debtor's, subject to appropriate income tithing compliance.

In a traditional bankruptcy, the principal importance of the secured claim bifurcation is to lock in the creditor's entitlement of a protected property right in the collateral up to the amount of the allowed secured claim. For example, if the bankruptcy estate uses up the collateral (by depreciation), the creditor is compensated for this loss, but only to the amount of its allowed secured claim.[191] And while the automatic stay prevents a creditor from doing anything *during* the bankruptcy with the collateral in a Chapter 7 case, when the proceeding concludes, the creditor's property rights *resume*, protected by that lien, notwithstanding the discharge of the debtor's in personam liability that implements the fresh start.[192]

Despite these protections, bankruptcy law imposes upon these property rights in at least three important ways. First, as mentioned, the

187 *Id.* § 506.

188 The debtor may exempt from the bankruptcy estate certain minimal amounts of property, which may include the equity of an automobile. *Id.* § 522.

189 *Id.* § 726.

190 *Id.* §§ 704, 722, 524.

191 *Id.* § 506(a)(2).

192 Long v. Bullard, 117 U.S. 617, 620–21 (1886). Chapter 13, by contrast, discharges liens completely, albeit not until plan completion. 11 U.S.C. § 1328.

stay suspends the exercise of property rights during pendency of the proceedings. Second, the traditional bifurcation locks in a valuation of the claim that can mark to market the creditor's leverage in the car. Thus, the protection a secured creditor is entitled to for depreciation of its collateral is limited to the amount of its allowed secured claim (i.e., the current value of the collateral). And there are other consequences to fixing that value in the claim bifurcation process. Consider, for example, the power of *redemption* in Chapter 7. At common law, and under Article 9 of the Uniform Commercial Code, debtors seeking to redeem the collateral must pony up the full amount of outstanding indebtedness (interest, fees, and so on), a luxury few financially distressed debtors can afford.[193] A car loan with a $7,000 outstanding balance requires $7,000 to be redeemed, even if the underlying car is now worth only $4,000. In a bankruptcy proceeding, by contrast, subject to certain constraints, debtors generally can redeem a car by paying its current value (i.e., the amount of the allowed secured claim) and discharge by force of law the encumbrance on the collateral.[194] That same car in bankruptcy can be redeemed for only $4,000, lessening the cash needs of the redeeming debtor. The claims allowance process of bifurcation locks in this important strike price.[195]

A debtor, like most, who does not have the present liquidity for even the lower-price redemption buyout, can always voluntarily *reaffirm* the debt with the creditor to keep the car.[196] But this, of course, is a voluntary contractual renegotiation and requires the assent of two parties. Recall that because the lien on the debtor's car is not discharged—merely suspended—during a traditional Chapter 7 bankruptcy, the creditor whose debtor is in default may, upon conclusion of the case, exercise any appropriate remedies, including repossession and foreclosure.[197] Understandably, this power stales the debtors' fresh starts considerably. This is why many debtors in default seek to work out reaffirmation agreements with their creditors, which can be notoriously exploitative (e.g., demanding more than the original balance).[198] The Code offers some protection, to be sure, such as trying to police carefully the reaffirmation process and, under the best reading of the Code, excusing an ipso facto default of the loan agreement where the only default is the

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193 U.C.C. § 9-623 (AM. L. INST. & UNIF. L. COMM'N 2022).

194 11 U.S.C. § 722.

195 Redemption, unsurprisingly, is rare. Foohey, Lawless & Thorne, *Driven*, *supra* note 158, at 321 (finding 1.3% incident rate).

196 11 U.S.C. § 524(c), (d), (k).

197 *Long*, 117 U.S. at 620–21.

198 *See, e.g.*, *In re* Latanowich, 207 B.R. 326, 330–31 (Bankr. D. Mass. 1997).

very filing of the bankruptcy petition.[199] Moreover, many debtors remain current on their loans, and so the prospect of postbankruptcy seizure is minimal (few lenders clamor to seize used consumer assets to punish performing loans). But the larger point remains for a good chunk, perhaps the majority, of Chapter 7 debtors: they risk losing their cars after bankruptcy if they cannot get the lender to assent to a reaffirmation agreement. This is why many debtors with asset-based woes seek protection under Chapter 13.

This risk of eventual collateral loss underscores the significance of the third, and not remotely subtle, aspect of the Bankruptcy Code's bifurcation power mentioned above: to alter the rights of the secured creditor in some circumstances. Chapter 13, just as Chapter 11 in the corporate context, allows debtors to alter the legal rights of their secured creditors' allowed secured claims under their bankruptcy plans.[200] This power is significant, because unlike a reaffirmation, such an alteration can be crammed down an objecting creditor's throat. The most natural type of relief would be an extension, where the debtor could stretch out payments over a revised timeline. A three-year repayment term can be refinanced to a five-year one, provided the debtor assures payment of the value of the allowed secured claim. To be sure, Congress has built in some checks on this modification power, most significantly the proscription on alteration of a home residence mortgage (and certain "new-ish" car loans thanks to a powerful Detroit lobby), but for the most part, so long as the value of the allowed secured claim is respected, the debtor can modify its legal repayment obligations of secured debt in Chapter 13.[201] Equally importantly, once the repayment plan is completed on the secured debt as modified, the lien is extinguished from the debtor's property and the fresh start is complete.[202] As a corollary, the adjustment power of Chapter 13 allows the debtor to cure any defaults as part of the repayment plan as well, such that the creditor, especially if irked by a forced refinancing, cannot repossess the debtor's car on account of the prebankruptcy default that may have precipitated the case in the first place (e.g., two months' missed payments).[203]

199 Riggs Nat'l Bank of Washington, D.C. v. Perry, 729 F.2d 982, 985 (4th Cir. 1984). In the event such ipso facto defaults are unexcused under Chapter 7 (they can be cured under Chapter 13), state waiver doctrines step in to constrain calling performing loans postbankruptcy. Pac. Cap. Bancorp v. Schwass (*In re* Schwass), 378 B.R. 859, 862 (Bankr. S.D. Cal. 2007); *see also infra* note 206 (discussing effect of cross-default clauses).

200 11 U.S.C. § 1322.

201 *Id.* §§ 506(a), 1325(a)(5)(B)(i)(I).

202 *Id.* §§ 1325(a)(5)(B)(i)(I)(bb), 1327(c).

203 *Id.* §§ 362, 1322(b).

C. *Secured Debt Treatment in a Car Scheme*

In light of these aspects of the treatment of secured debt in a traditional bankruptcy proceeding, what would happen to the secured claim in a "car scheme"? Initially, the primary point is nothing different from a conventional consumer bankruptcy. Just as with a regular bankruptcy, debtors would be required to protect the creditor's interest in the allowed secured claim against depreciation during the proceedings. (Given that these limited proceedings are intended to be quick, that would presumably not generate an onerous obligation on the debtor.) Debtors could enjoy the automatic stay's breathing spell during this time by being accorded protected space to work out the problem with the car payments that are presumably not widespread to the debtor's other financial relationships—perhaps even ultimately executing a voluntary reaffirmation agreement with the lender.[204]

As for the mark-to-market power, a car scheme would again treat the creditor no differently from a conventional Chapter 7. Thus, the lucky but fancifully stylized debtor who had fallen behind on car loans, faced repossession, but happened to have access to $4,000 in cash could redeem the clunker worth that amount, even on a $7,000 loan balance, upon prompt payment of that amount. (It is not clear why such a debtor would not use that liquidity to prevent default in the first place, but the doctrinal point remains.)

Third, the car scheme would accord the debtors the Chapter 13 powers to modify the loan under the proposed plan without risk of losing the collateral upon the case's conclusion at confirmation of the "car plan." This third and most significant function of a car-only proceeding thus would be to exercise the Chapter 13 power to rewrite ("modify," in bankruptcy parlance) the loan, subject to the constraints of respecting the value of the allowed secured claim.[205] As such, similar to scheme of arrangement debtors, car borrowers in trouble could adjust their loan terms under the watchful gaze of a bankruptcy court *without subjecting all their other liabilities to acceleration and default*.[206] This means, as

204 Proceedings restricted to cars would make importation of the ability-to-pay reaffirmation analysis infeasible. *Id.* § 524(c)(3).

205 *Id.* § 505(a).

206 Consumer bankruptcy is perilous even regarding performing loans for more technical reasons. First, the statutory acceleration of all debts, *id.* § 502, puts many debts into default, hence the modularity needed to prevent default on one loan from triggering default on the whole portfolio. Although such ipso facto defaults are excused regarding executory contracts, *id.* § 365, and can be cured in Chapter 13, *id.* § 1322(b)(5), the scope of their excuse in Chapter 7 is vaguer, relying upon caselaw, Riggs Nat'l Bank of Washington, D.C. v. Perry, 729 F.2d 982 (4th Cir. 1984). A modular proceeding would solve this problem but might still run afoul of the widespread cross-default clause, where a genuine default on the limited-proceeding debt might trigger default on an

mentioned, that the modular, car-limited proceeding used here would more likely replicate Chapter 13 than Chapter 7 (absent, perhaps, the redemption power). But that is as it should be. Chapter 7 is a complete reboot, where the debtor wants to give up everything and start over. By contrast, a modular proceeding restricted to one asset's distress is not a comprehensive reboot; it is "selective." Accordingly, the absence of a comprehensive discharge and the concomitant retention of all other obligations hanging over the debtor's head would be a feature, not a bug, of the car scheme. Nor would it make sense to talk of a debtor "giving up all their assets" as a grand bargain abuse check in a car-only bankruptcy proceeding, because presumably the only relevant asset would be the car that the debtor was trying to save, making its surrender a curiously excessive price to pay. Moreover, Chapter 13, unlike Chapter 11, has built-in time limits on how far a loan's rewritten terms can be stretched out,[207] and so, too, could a car scheme have a maximum "car repayment term" of, say, five years (matching Chapter 13's)—which as an empirical matter should be more than sufficient for a car note that the debtor already had outstanding long enough to get into financial trouble on.[208]

IV. MODULARITY'S CHALLENGES FOR THE SCHEME

The foregoing discussion might suggest that the car scheme would not require that radical a departure from traditional consumer bankruptcy regarding the treatment of car debt—it's just like a mini-Chapter 13. Were it only so simple.

A. *The Problem of a Discharge for Deficiencies*

To begin, in addition to whatever changes to the lien on the car pursuant to the allowed secured claim the debtor might seek under modification powers that build upon traditional Chapter 13, the debtor may also want escape from any deficiency liability to accord comprehensive car relief. In other words, the debtor may also want a discharge. But vindication of that desire in a modular proceeding is far more problematic from a policy perspective. Harkening back to the

unaffected loan. Accordingly, a coherent modular scheme proposal should include § 365-like statutory provisions expressly excusing cross-defaults.

207 11 U.S.C. § 1325(b)(4).

208 Foohey, Lawless & Thorne, *Driven*, *supra* note 158, at 292 ("The 'average new-car loan term is 68.8 months,' as compared to 48 months in 2012." (quoting Jeff Gitlen, *Auto Loans Outstanding Hits Record in the United States*, LENDEDU (Oct. 11, 2017), https://web.archive.org/web/20190212145850/https://lendedu.com/blog/outstanding-auto-loans-market-hits-record)).

theoretical overview of consumer bankruptcy law earlier in this Article, and specifically its need to police moral hazard of its insurance function, we can see immediately the problem from the creditor's perspective: what buy-in would the debtor be offering in exchange for this "car discharge"?

A traditional scheme of arrangement requires a holistic fairness review within the context of a supermajoritarian approving vote. Here, there is no vote, so one must turn to the traditional consumer bankruptcy grand bargain buy-ins as the presumptive tools to police abuse. Recall that in a traditional Chapter 7, debtors forfeit their nonexempt assets to the bankruptcy estate for creditor recovery. Here, however, there is no bankruptcy estate, let alone assets thereof to forfeit. It would surely be letting debtors have their cakes and eat them too were we to allow a discharge from the unsecured portion of an auto loan without any concomitant sacrifice of either asset relinquishment (Chapter 7) or pledge of future income (Chapter 13). On the other hand, if we were to force the debtor to tithe income over the course of the modified car loan's term, as we would in a traditional Chapter 13, the debtor would protest—with good reason—that such a tithe would be excessive since any discharge would be restricted to automotive debt and not all other unsecured obligations (as would occur at the end of a traditional Chapter 13 plan). Both objections are valid.

1. The Weak Proposal: No Discharge

At least three possible solutions present themselves, albeit with varying attraction, to the problem of how to treat the unsecured deficiency claim in a car scheme. First, we could succumb to the problem as fatal to the prospect of modular bankruptcy relief, retreating to the collectivity shibboleth and saying it's just not possible to think of consumer bankruptcy with such atomization. The most readily apparent virtue of such an approach would be to shorten the length of this Article. (Sadly, this will not be the case, as discussed below.) This is what we can consider the "weak" version of the car scheme: a moratorium-protected chance to work out a new deal with the car lender (in the shadow of a crammed-down modification), but no power to discharge any unsecured indebtedness. Note that this outcome would in many instances mirror what occurs in reaffirmation agreements under the current Code—assumption of the full car debt, including the deficiency, as a voluntary exception from the debtor's discharge (or at least as voluntary as consumer car loan terms are).

This weak scheme may strike some as *too* weak. Some might call it gibberish to talk of a "car scheme" that is intended only to resolve the car debt, but, by lack of a discharge of the unsecured component thereof, does

not even fully resolve debtors' financial problems regarding their cars. Isn't that taking modularity a bit too far? The answer is a resounding not necessarily. This is because debtors could restructure not just the secured portion but also the unsecured portion of the note in a car proceeding. Indeed, the ability to cure an arrearage could help debtors,[209] even if those debtors' preferences were to retain the asset "irrationally" (i.e., when its remaining price exceeds its value).[210] This is the purpose of reaffirming undersecured debt. All that matters for present purposes is that it is not implausible to establish a car scheme that allows the debtor a stay-conferred breathing spell to fix an arrearage, cure a default, but otherwise maintain an obligation without discharge of any deficiency.[211] The doctrinal mechanics of the weak claim are complicated because presumably the deficiency claim would have to remain secured by the car.[212] To be sure, it could become completely untethered as an unsecured claim, but it might just remain attached by lien.[213] Therein lies the real power, which is not insubstantial, of the weak scheme: to effect a forced extension.

2. The Strong Proposal: Discharge

Second, we could say that debtors do indeed get a discharge of the car debt in the name of simplicity and repose, and comfort ourselves by pointing to other doctrinal levers to police moral hazard beyond the grand bargain's asset relinquishment or income pledge.[214] For example, we could beef up *access barriers* to restrict relief to a subset of debtors deemed worthy.[215] Screens for admission to a car subchapter might include means-tested income (hopefully better implemented than BAPCPA),[216] or automobile valuation, age, or even debt-to-value ratio, all of which could be progressively designed. That is, we could say only debtors under *X*% of the median income could file a car scheme petition,

209 *See* 11 U.S.C. § 1322(b)(5).

210 It is not always irrational. Even leaving aside idiosyncratic valuation, sometimes the debtor's switching costs might exceed the deficiency overhang.

211 *See* 11 U.S.C. § 1322(b)(5).

212 This is true only if *Dewsnup* is not overruled or modified by statute, which for many reasons, not least of which the opinion's indefensibility, is the easiest solution.

213 This issue quickly gets technical. It could be, for example, that any car subchapter would require an analogue to 11 U.S.C. § 1111(b) to ensure minimum payments determined both by the value of the allowed secured claim and the notional amount of the total claim (including deficiency).

214 *See, e.g.*, *id.* §§ 707, 1328.

215 *See id.* § 707(b)(2) (implementing means-based eligibility screen for Chapter 7).

216 *See* Lawless et al., *Reform Fail?*, *supra* note 25, at 352–53.

or we could say only debtors with cars worth less than $*Y* or more than *Z* years old could do so.[217]

Ratcheting up the complexity, we could even envision a more searching enquiry. For example, we might restrict car schemes to debtors who have paid their car loans for a minimum of *A* years or retired *B* percent of the principal balance. Or even more finely, we could throw in some flexible standards rather than strict rules, such as restricting car scheme access to debtors whose cars are "necessary for work-related commuting."[218] The idea at this juncture, of course, is not to design what the optimal screens might be for modular car scheme access, but simply to flag that there are alternatives to our bankruptcy system's traditional approach to pledging all nonexempt assets in Chapter 7 or tithing all disposable income in Chapter 13, both of which require the comprehensive constitution of an estate to function as the quasi-analogue of a corporate scheme's supermajoritarian vote.[219] Still, the broader point would remain: debtors, once clearing whatever hurdle Congress saw fit to impose, would be discharged of all car-related debt under the car scheme. This is the *strong* version of the car scheme's treatment of unsecured deficiency debt: blanket discharge.

3. The Semistrong Proposal: Prorated Discharge

This brings us to a third possibility to no discharge and full discharge. (Shoehorning this into the evocative taxonomy offered might involve calling this a *semistrong* proposal—perhaps a "dad bod"?) We could strive toward greater accuracy at the cost of increased complexity by implementing a novel norm of *discharge proration*—letting no baby be left unsplit. Under this approach of partial discharge, debtors proposing a car scheme could discharge the unsecured car debt, but only with a *synthetic approximation* of the pain inflicted during a full bankruptcy proceeding by the traditional doctrinal levers that police abuse. For example, if a quick and dirty filing of financial schedules of the debtor's full assets and liabilities revealed a bankruptcy estate subject to distribution of $*X* in nonexempt assets over a total of $*Y* in unsecured

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[217] *Cf.* 11 U.S.C. § 109(e) (restricting Chapter 13 access to debtors with debts below certain thresholds).

[218] *Cf. id.* § 362(d)(2) (requiring court to grant relief from automatic stay of act against property if debtor lacks equity in collateral and it is not "necessary to an effective reorganization").

[219] To be sure, an income tithe would not necessarily require the constitution of an estate, but it would raise its own issues. That is, the current Chapter 13 bargain is a tithe of net income in exchange for a full discharge of unsecured debt. Were the discharge to be restricted modularly to car debt alone, the tithe level would probably require similar proration. That task would not be impossible, but unduly complicated.

claims,[220] then debtors could discharge car debt if, and only if, they contributed nonexempt assets to the car lender in an amount equal to the proportion of the discharged car debt (say, a $2,000 deficiency) to total unsecured debt (here, $\$2,000/Y$) multiplied by the total available assets for distribution (here, X)—i.e., on the numbers in this example, $X(\$2,000/Y)$. More simply, if your car deficiency is ten percent of your total unsecured indebtedness, you only get to discharge it if your car scheme provides for a contribution of ten percent of your nonexempt assets to your car lender.

To be sure, the math could be varied. For example, one might tax a modularity premium, recognizing that the secured debt is also being adjusted to the debtor's benefit, and so require a greater contribution than the strict proration output would dictate (i.e., a gross-up multiplier). Regardless of the details, the general point holds that the system could be designed without abandoning the Code's traditional consumer bankruptcy moral hazard screens of asset pledge or income tithe to ground a fair exchange for the discharge of a limited—intentionally not comprehensive—amount of unsecured consumer indebtedness.

As is perhaps expected, the more sophisticated tailoring of a prorated discharge (either by asset contribution or future income pledge) would come at the cost of simplicity and speed. Indeed, the proration formula would require a complete scheduling of assets and claims to generate the proper inputs. If that is the case, one might wonder whether the hypothesized benefits of a car scheme's modularity are sacrificed or at least substantially diluted by such information gathering. (Recall that the envisioned "car petition" is supposed to be a short and sweet one-pager.) This critique is well taken, as one of the presumed benefits of modular debt relief is only having to deal with one specific debtor-credit relationship. Corralling all the utility bills and so on takes time.[221]

Does this mean proration is too clever by half as a proposal to deal with the car deficiency debt? Quite possibly. But that ultimately requires some empirical analysis and conclusions on the marginal costs of comprehensive asset disclosure atop the fixed costs of preparing information on the car loan for the car petition. My own priors are to doubt those costs would be daunting, but I also would be hesitant to endorse full-throatedly a policy prescription in the absence of acquiring

220 Debtors are required to submit comprehensive schedules of assets and liabilities with their petitions. U.S. BANKR. CT., INSTRUCTIONS: BANKRUPTCY FORMS FOR INDIVIDUALS 7, 16–33 (2022), https://www.uscourts.gov/sites/default/files/instructions_individuals.pdf [https://perma.cc/QD5M-E8RZ].

221 *See* Richard M. Hynes & Nathaniel Pattison, *A Modern Poor Debtor's Oath*, 108 VA. L. REV. 915, 917 (2022) (reporting that typical no-asset Chapter 7 bankruptcy filing requires over twenty forms).

more data.[222] Note that the bankruptcy system is already well acquainted with running hypothetical analyses, such as the statutory requirement of assuring a proposed Chapter 13 plan pays as much to the creditors as they would get in a hypothetical Chapter 7 liquidation.[223] So although it would be concededly more complicated than either the fully strong or weak versions of the proposal, the semistrong one would not subject the consumer bankruptcy system and actors to wholly uncharted terrain.

4. Summary

Thus, the imagined car scheme could, if strong (but need not, if weak), offer debtors discharge relief on the unsecured portion of their car note upon confirmation of their scheme, albeit with constraints to mimic the safeguards against moral hazard that would otherwise obtain in a traditional consumer bankruptcy proceeding. As the foregoing discussion has demonstrated, however, it may require some serious additional thinking about the necessity of discharge to providing meaningful consumer relief.

Thus far, this Article has remained coyly uncommitted to which policy proposal (strong or weak) is preferable, retreating to the apparent comfort of insisting its role is limited to sketching out alternatives. Further analysis of that question would perhaps start by noting a stark empirical reality: data on the consumer bankruptcy system indicate that the median asset value available for distribution from the estate to the unsecured creditors is zero.[224] If this is so, then the fancy proration approach seeking to find a middle ground between full and no discharge would, as an empirical matter, collapse into full discharge because any proration of a zero-asset dividend is necessarily zero. If so, then one could achieve a majoritarian rule—at a fraction of the administrative cost—by biting the bullet and going with the strong version of the proposal for full discharge of the deficiency claim in a car scheme. The only hesitancy with jumping in thus would be theoretical concern over a potential demand effect, where the traditional moral hazard prevention buy-in of the asset pledge or the income tithe might dissuade a would-be filer from a plenary petition but might entice her to a car petition, knowing that there

[222] *See generally* Elizabeth Warren, *The Market for Data: The Changing Role of Social Sciences in Shaping the Law*, 2002 WIS. L. REV. 1 (2002) (extolling policymaking virtues of data collection).

[223] 11 U.S.C. § 1325(a)(4) (prohibiting plans where unsecured creditors receive less than they would under Chapter 7 liquidations); *see also id.* § 1129(a)(7) (same).

[224] *See* Hynes & Pattison, *supra* note 221, at 920, 932 (finding ninety-five percent of Chapter 7 petitions involve no general creditor distribution); Lawless et al., *Reform Fail?*, *supra* note 25, at 360 n.50.

effectively would be a "free" car deficiency discharge. To be sure, this risk presents a moving target, because, as proposed above, a car petition could also have additional access screens to provide deterrence from overuse in the absence of the grand bargain, and so aggregate incentive effects are uncertain. But, at least theoretically, if these additional deterrence devices could be deployed and properly calibrated to address the possible "marginal" car filer, then the strong version of the proposal could be adopted without undue concern.

B. *The Problem of Surplus Equity and "Bankruptcy" Law*

As if the policy questions regarding debtor deficiency and discharge were not vexing enough, even further problems arise regarding a "car debtor" without sizable unsecured car debt in need of relief.

1. Oversecured Debt—Is There Even a Need?

Not all debtors want or need to discharge their unsecured indebtedness. Many debtors, including those who file for bankruptcy, have equity built up in their cars.[225] This is especially so if we incorporate a role for personal property exemptions, which this Article has elided.[226] Some debtors may indeed want to use the bankruptcy system for relief on *oversecured* cars. This may strike some readers as counterintuitive. Surely, they might reason, consumer debtors who need financial relief are those so hopeless that if they tried to walk away from their cars, they would end up still owing money to their lenders (and be out of a car, to boot). But this is not necessarily the case at all as to why a consumer might be in financial distress regarding *even just one asset in which they have built up some equity*. To use one realistic example, imagine a consumer who has been dutifully paying down a car note for three years and now faces a liquidity constraint due to employment dislocation.[227] Having exhausted their savings, they now can't make the monthly car payment, devoting all that they can to keep the home mortgage current. They seek to avoid default and repossession with a recalcitrant or impatient car lender uninterested in negotiation. Thus, it is eminently possible that a substantial portion of debtors may want to use a car scheme not to *discharge unsecured debt* overhang but to *protect the equity* of their car in the event of default triggered by financial distress, where that equity

225 Foohey, Lawless & Thorne, *Driven*, *supra* note 158, at 308 tbl.1.

226 The larger the exemption, the less likely the creditor's claim to any equity.

227 *See* SULLIVAN, WARREN & WESTBROOK, *supra* note 28, at 16–23.

value will quickly evaporate absent legal intervention. Recall, too, the data from the CBP showing many debtors with car equity but no home mortgages.[228]

As suggested, such default is most likely to be a missed payment, which in turn means that the debtor is experiencing liquidity distress. But, again borrowing from insights of the corporate bankruptcy world, a mere liquidity crisis does not mean the debtor is insolvent or requires shutdown.[229] Rather, it means that the debtor could well have temporary distress marring an otherwise sound business model (so to speak)—distress sufficient to prevent timely refinancing even in the presence of some equity value.[230] Just as we do not want to close such a business down, thereby destroying goodwill in a deadweight social loss, so, too, do we not want to let temporary financial distress destroy the consumer debtor's equity in valuable personal property, such as a car.[231]

In the world of consumer default on secured debt, protracted nonpayment will trigger repossession and eventual resale of the collateral.[232] That realization event destroys value. The same way a sheriff's real estate auction never fetches anything close to the "true" value of the collateral,[233] Article 9 repossession sales, even when fulfilling the statutory obligation of being conducted in a commercially reasonable manner, rarely get full value for the collateral—the best outcome is likely to be a dealer's auction bid premised on flip resale profit.[234] To be sure, unlike with the destruction of the going-concern surplus of an intemperately liquidated business, strictly speaking, when a debtor loses her car, the value is not "lost." It is transferred from struggling debtor to purchaser (the lender in the common credit bid situation). But this artificial realization event at a depressed value often results in a regressive redistribution from one who can afford it least, a debtor in temporary

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228 Foohey, Lawless & Thorne, *Driven*, *supra* note 158, at 308 tbl.1.

229 *E.g.*, Edward R. Morrison, *Bankruptcy Decision Making: An Empirical Study of Continuation Bias in Small-Business Bankruptcies*, 50 J.L. & ECON. 381, 396–97 (2007) (articulating general economic principle in corporate insolvency distinguishing economic from financial distress and reminding that only former requires shutdown).

230 Preventative Restructuring Directive, *supra* note 18, recital 2, at 18 ("Preventive restructuring frameworks should, above all, enable debtors to restructure effectively at an early stage and to avoid insolvency, thus limiting unnecessary liquidation.").

231 *See* Melissa B. Jacoby & Edward J. Janger, *Tracing Equity: Realizing and Allocating Value in Chapter 11*, 96 TEX. L. REV. 673 (2018).

232 U.C.C. § 9-610(a) (AM. L. INST. & UNIF. L. COMM'N 2022).

233 LYNN M. LOPUCKI, ELIZABETH WARREN & ROBERT M. LAWLESS, SECURED TRANSACTIONS: A SYSTEMS APPROACH 57 (9th ed. 2020) ("[C]ollateral frequently sells for much less than its value. But for most purposes, the law clings to the legal fiction that the price paid in an auction foreclosure sale is the collateral's value.").

234 U.C.C. § 9-610(b) ("Every aspect of a disposition of collateral . . . must be commercially reasonable."); *see also* LOPUCKI, WARREN & LAWLESS, *supra* note 233, at 57–58, 72.

financial distress, to a diversified lender. Thus, in addition to losing a way to drive to work, a debtor with oversecured equity in the family car may fear value stripping in the event of default—and hence seek the legal protection of bankruptcy as a safeguard. By allowing "above water" car debtors access to modular relief, a car scheme could help the debtor preserve value while paying off the restructured original loan. Accordingly, the demand for (and benefits of) such assistance are far from imagined for such equity-holding debtors.

2. What to Do with the Equity?

Having made the case for demand for car schemes beyond underwater car debtors to equity-holding car owners as well, we now have to puzzle through just what would happen to that surplus equity in a car-only proceeding. One approach would be simply to avoid the question altogether by restricting car schemes to the most wretched of the wretched by requiring a loan-to-value ratio on the car of greater than one hundred percent (i.e., underwater cars). But why do that? The purpose of bankruptcy law is to help the "honest but unfortunate debtor" in financial distress.[235] We do not make formal insolvency a precondition for business bankruptcy,[236] so there is no reason to discriminate negatively against the consumer. Indeed, the scheme of arrangement procedure may be engaged by fully solvent companies.[237] Nor is there any reason the precise loan-to-value ratio should be a dealbreaker; the immediately preceding discussion suggests meaningful demand for such relief by oversecured car debtors. Accordingly, it seems the presumptive solution would simply be to let debtors keep that equity, unfettered by any requirement of its forfeiture.

This outcome seems to diverge conspicuously from the traditional Chapter 7 grand bargain buy-in of nonexempt asset relinquishment, but can nonetheless be justified. First, because a car scheme is by design a limited, selective proceeding, there is no "estate" of property to satisfy the claims of all creditors in one comprehensive resolution. No trustee needs to round up all the debtor's nonexempt property, and so the "omission"

235 Loc. Loan Co. v. Hunt, 292 U.S. 234, 244 (1934) ("This purpose of the act has been again and again emphasized by the courts . . . [and] gives to the honest but unfortunate debtor who surrenders for distribution . . . a new opportunity in life . . . .").

236 We indirectly police financial condition by requiring genuine financial distress as a precondition to filing in good faith. *In re* LTL Mgmt., LLC, 58 F.4th 738, 753–58 (3d Cir. 2023) (holding that petitions are subject to dismissal under 11 U.S.C. § 1112(b) unless filed in good faith, which requires financial distress).

237 *See, e.g.*, Re Rodenstock GmbH [2011] EWHC (Ch) 1104 [19] (Eng.) (finding English courts may wind up solvent company).

of the car equity from such a nontrustee nonestate is almost a non sequitur. There is no place in a car scheme to contribute the debtor's surplus to, no constituents to benefit, and no purpose for so doing. Indeed, as discussed above, a car scheme has more in common with Chapter 13 than Chapter 7, and, in Chapter 13, debtors get to keep all their assets.[238]

Yet, as also discussed above, the debtor in Chapter 13 is supposed to tithe future income in exchange for asset retention. Would allowing the oversecured car borrower to keep her equity in the car without an income tithe raise the specter of windfall—getting something for nothing in violation of the consumer bankruptcy grand bargain? No. Both the asset forfeiture in Chapter 7 and the income tithe in Chapter 13 buy-ins are designed to police against the moral hazard of the bankruptcy discharge. But with an oversecured car loan, and a debtor seeking no relief beyond restructuring the car note, there is no unsecured car debt in need of discharge. For this subset of debtors, there is no worrisome remedy in need of policing. Consequently, debtors should not have to contribute anything close to the traditional Chapter 7 or 13 "admission price."

Of course, there is *some* moral hazard. Debtors might decide simply to stop paying their car loan out of spite or greed and, upon the exercise of default remedies by the creditor, file a car petition. Indeed, particularly savvy debtors might try to exploit a drop in interest rates and involuntarily refinance the car by way of a scheme solely to exploit the lower rate.[239] Much like the policymakers wrestling with BAPCPA, the concern here would be on sorting debtors who can, but don't want to, pay their car loans from those who cannot without undue hardship.[240] One should not deny the potential for these moral hazard concerns. On the other hand, one can equally take solace in discretionary ex post relief in the form of bankruptcy judges' dismissal power for lack of good faith, which is probably sufficient to combat these evils that are more likely to be hypothesized than real.[241] The fairness review of the scheme's sanctioning hearing also returns to mind, which essentially already finds its outlet in this good faith test that similarly constrains confirmation of a consumer Chapter 13 plan (just as it does a corporate Chapter 11).[242]

238 11 U.S.C. § 1327. There is an estate in Chapter 13, *id.* § 1306, and indeed a trustee, *id.* § 1302, because the proceeding is "inclusive" in Paterson-Walters terminology, *see* Paterson & Walters, *supra* note 3 (manuscript at 18–19).

239 *See, e.g.*, Kris Gerardi, Christopher Foote & Paul Willen, *Did Nonrecourse Mortgages Cause the Mortgage Crisis?*, FED. RSRV. BANK OF ATLANTA (Feb. 18, 2010), https://www.atlantafed.org/blogs/real-estate-research/2010/02/18/did-nonrecourse-mortgages-cause-the-mortgage-crisis [https://perma.cc/LX6D-AH4C].

240 *See, e.g.*, 11 U.S.C. § 707(b) (attempting to do so poorly).

241 See discussion of behavioral limitations *supra* note 29 and accompanying text.

242 11 U.S.C. §§ 1325(a)(3), (a)(7), 1129(a)(3). For the Chapter 7 analog, see *id.* § 707.

Were policymakers truly concerned that car-solvent borrowers would be inclined to fabricate financial distress, they could conceivably demand a "co-pay" (e.g., payment of *X*% of the debtor's postexemption equity in the car to the secured party in exchange for the statutory relief of a loan extension), although the valuation and administration costs alone might dwarf any moral hazard reduction potential with such a safeguard.

Having accepted the situation of what to do with the surplus equity in a car scheme—let the debtor keep it—one might be inclined to celebrate that we have solved the last design question regarding how a car scheme might work. We have, but that solution itself unfortunately raises an even more theoretically troubling problem. By allowing modular bankruptcy relief regarding just one automotive creditor of a debtor who, with regard to that one asset, can be considered solvent, have we now exceeded the scope of bankruptcy law—doctrinally, theoretically, and even constitutionally? That is perhaps an even trickier question than whether and how to allow the underwater car debtor a discharge. For if we are committed to allowing oversecured car borrowers bankruptcy relief, we must correspondingly refine what "bankruptcy" relief even means in a nondischarge world. More pointedly, because the relief of an oversecured car debt could involve a cramdown refinancing, a car scheme, without restrictions, could raise concerns of bankruptcy law running roughshod over the private agreement of parties by contract. That is, if the parties agree to a contract and want to amend it, then at common law, both must consent to amend.[243] The scheme of arrangement alters this rule upon a supermajoritarian vote of a class of creditors with an antiholdout justification that dates back to well before *Backwell's Case*. If we allow bankruptcy law to provide special proceedings over what might be viewed as nothing more than a simple contract dispute between two private parties, we run the risk of a forced amendment at the behest of one party (the debtor) unilaterally—and perhaps if we are too far afield from bankruptcy, we may even raise the specter (in the United States) of the Contracts Clause.[244]

243 RESTATEMENT (SECOND) OF CONTRACTS § 279 (AM. L. INST. 1981) (requiring mutual assent for a substituted contract).

244 U.S. CONST. art. I, § 10, cl. 1; Lynch v. United States, 292 U.S. 571, 580 (1934) ("Contracts between individuals or corporations are impaired within the meaning of the Constitution whenever the right to enforce them by legal process is taken away or materially lessened." (citation omitted) (first citing W.B. Worthen Co. v. Thomas, 292 U.S. 426 (1934); and then citing Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398 (1934))). Jurisprudence has largely denuded the Contracts Clause, *e.g.*, *Blaisdell*, 290 at 447–48, but we are in uncharted terrain.

C. *The Boundaries of "Bankruptcy" Law*

1. The Contours of the (U.S.) Law

One source of defining "bankruptcy" might be the U.S. Constitution's allocation to Congress of the power to legislate uniform laws "on the subject of Bankruptcies."[245] But the jurisprudence on the Bankruptcy Clause has been, to say the least, complex.[246] It involves not just consideration of that specific constitutional provision, but also its interaction with the Contracts Clause (including the reverse incorporation thereof),[247] the (first) Due Process Clause,[248] including its just compensation component, and the later-enacted Fourteenth Amendment.[249] Indeed, respected bankruptcy historian Professor Stephen Lubben has described the Supreme Court's early holdings on the scope of federal bankruptcy authority as a "Venn diagram" involving the Bankruptcy Clause, the Contracts Clause, and the federal common law of procedure that preceded the Fourteenth Amendment.[250] Much excellent historical work has been done on this, and the absence of discussion in the constitutional debates is partially made up for by the prolific historical treatise work.[251] Most of the constitutional analysis of the Bankruptcy Clause has been focused on its uniformity obligation, however, with the Supreme Court's only intervention striking down a congressional statute for violating the Clause grounded on that aspect of it.[252] In the early days, there were also muddled and awkward forays into its federalism/preemption aspects,[253] inspiring Lubben to discuss with

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[245] U.S. CONST. art. I, § 8, cl. 4.

[246] *See, e.g.*, Stephen J. Lubben, *A New Understanding of the Bankruptcy Clause*, 64 CASE W. RSRV. L. REV. 319, 357–58 (2013) (citing DAVID P. CURRIE, THE CONSTITUTION IN THE SUPREME COURT: THE FIRST HUNDRED YEARS, 1789–1888, at 154–55 (1985)); Conrad Reno, Ogden v. Saunders *Reviewed*, 36 AM. L. REG. 611, 612–16 (1888).

[247] Although not incontrovertible, the prevailing view is that the Contracts Clause has been "reverse incorporated" against the federal government. Jay S. Bybee, *The Congruent Constitution (Part Two): Reverse Incorporation*, 48 BYU L. REV. 303, 314–38 (2022).

[248] Lubben, *supra* note 246, at 348 (citing Michael G. Collins, *October Term, 1896—Embracing Due Process*, 45 AM. J. LEGAL HIST. 71, 74–76 (2001)).

[249] *Id.* at 384.

[250] *Id.* at 348.

[251] *See, e.g.*, THEODORE SEDGWICK, A TREATISE ON THE RULES WHICH GOVERN THE INTERPRETATION AND APPLICATION OF STATUTORY AND CONSTITUTIONAL LAW (New York, John S. Voorhies 1857); *see also* MANN, *supra* note 14, at 187 (observing that Madison "skipped lightly" over the Clause in his notes).

[252] *See* Ry. Lab. Execs. Ass'n v. Gibbons, 455 U.S. 457, 465 (1982).

[253] *See, e.g.*, Ogden v. Saunders, 25 U.S. (12 Wheat.) 213, 368 (1827); Sturges v. Crowninshield, 17 U.S. (4 Wheat.) 122, 190 (1819).

tongue only partly in cheek the possibility of a "dormant Bankruptcy Clause,"[254] as the Court wrestled with the constraints on Congress's power in the context of there being only sporadic, time-limited federal bankruptcy laws passed in response to panics and widespread state insolvency laws.[255] Accordingly, extended debate over the substantive scope of the Clause—what *are* matters "on the subject of Bankruptcies" that Congress can regulate under Article I, Section 8?—has been much more limited.

Professor Kurt Nadelmann offers an account of the conventional debates on the Bankruptcy Clause, concluding that its scant discussion and assignment to the Committee on Style suggests it was originally intended as an adjunct of the Full Faith and Credit Clause (focusing on the "uniformity" requirement), ensuring not so much that Congress should have legislative authority but rather that it could police states.[256] The dominant view, however, is one that envisioned the nascent republic vesting full lawmaking power with the central government.[257] One Framer objected to the Clause's inclusion, but over concern the federal government might impose the death penalty, as had been done under various English bankruptcy acts.[258] But there was not, at first, an embrace of what Lubben calls the robustly "Hamiltonian" view that the federal government's power should preempt the states'.[259]

Indeed, state bankruptcy and insolvency laws abounded in the colonial era and, in the absence of Supreme Court resolution, persisted post-1787.[260] The short-lived 1800 Act felt the need to pronounce it did not supersede state laws absent direct conflict.[261] Thus, the early jurisprudence focused on the scope of these state laws in light of the new Constitution, with the Supreme Court seeming to accept them. For example, in *Sturges v. Crowninshield*, the Court evaded the Bankruptcy Clause in favor of the Contracts Clause as the grounds for invalidating a New York statute that discharged debtors from obligations incurred before the law's passage; the clear implication was that state discharge

254 Lubben, *supra* note 246, at 357–58.

255 *See, e.g.*, Bankruptcy Act of 1800, ch. 19, 2 Stat. 19, *repealed by* Act of Dec. 19, 1803, ch. 6, 2 Stat. 248; Bankruptcy Act of 1841, ch. 9, 5 Stat. 440, *repealed by* Act of Mar. 3, 1843, ch. 82, 5 Stat. 614; Bankruptcy Act of 1867, ch. 176, 14 Stat. 517, *repealed by* Act of June 7, 1878, ch. 160, 20 Stat. 99; *see also* Charles Jordan Tabb, *The History of the Bankruptcy Laws in the United States*, 3 AM. BANKR. INST. L. REV. 5, 15–21 (1995) (discussing state laws).

256 Kurt H. Nadelmann, *On the Origin of the Bankruptcy Clause*, 1 AM. J. LEGAL HIST. 215, 226–27 (1957).

257 Lubben, *supra* note 246, at 341.

258 Nadelmann, *supra* note 256, at 217 n.9.

259 Lubben, *supra* note 246, at 408.

260 *See, e.g.*, Act of Apr. 25, 1785, ch. 87, 1785 N.Y. Laws 167.

261 Bankruptcy Act of 1800, ch. 19, § 61, 2 Stat. 19, 36 (repealed 1803).

laws applying only to prospective debts would be fine.[262] The follow-up attempt at clarification in 1827's *Ogden v. Saunders* (with *Crowninshield*'s author, Justice Marshall, in dissent) was a badly fractured shifting 4-3 majority mess, holding that although prospective state bankruptcy laws could be enacted and allow discharge without offending the Constitution, they could only be limited to debtors within that state's physical borders.[263] Lubben correctly points out that the constitutional provenance for such a geographical restriction (under the Contracts, Bankruptcy, or some other Clause) is mysterious.[264]

Crowninshield did, however, offer the first helpful pronouncement on the scope of the Bankruptcy Clause in dictum, by rejecting one attempt at a restrictive definition. Before they were consolidated, English laws distinguished between *bankruptcy* and *insolvency* laws.[265] Traditionally, bankruptcy laws were creditor focused and restricted to merchants while insolvency laws were focused on debtor relief and discharge from prison, although, as Professor Thomas Plank notes, there was much play in the joints of shoehorning debtors into the definition of merchant, so much so that the distinction eventually "died of exhaustion."[266] A textual argument, accepted by some, was thus raised that the federal government's authority was limited to the former.[267] This was put to rest: "This difficulty of discriminating with any accuracy between insolvent and bankrupt laws, would lead to the opinion, that a bankrupt law may contain those regulations which are generally found in insolvent laws; and that an insolvent law may contain those which are common to a bankrupt law."[268]

With that low-hanging fruit grabbed, debate over what was a law "on the subject of Bankruptcies" did not flourish again until the Bankruptcy Act of 1841, which allowed for voluntary petitions, unlike English law, upon which the 1800 Act was extensively based, which required creditor initiation.[269] Some lower courts struck down the 1841 Act as beyond the scope of "bankruptcy," but most were reversed, with one such appellate decision offering the following formulation:

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262 17 U.S. (4 Wheat.) 122, 178 (1819). Note this decision came during state-law dominance of bankruptcy laws prior to permanent federal legislation.

263 25 U.S. (12 Wheat.) 213, 368–69 (1827).

264 Lubben, *supra* note 246, at 357–58.

265 *See, e.g.*, Mokal, *supra* note 8, at 440.

266 Thomas E. Plank, *The Constitutional Limits of Bankruptcy*, 63 TENN. L. REV. 487, 510 (1996) (quoting Robert Weisberg, *Commercial Morality, the Merchant Character, and the History of the Voidable Preference*, 39 STAN. L. REV. 3, 33 (1986)).

267 *See, e.g.*, Adams v. Storey, 1 F. Cas. 141 (C.C.D.N.Y. 1817) (No. 66); Golden v. Prince, 10 F. Cas. 542 (C.C.D. Pa. 1814) (No. 5,509).

268 Sturges v. Crowninshield, 17 U.S. (4 Wheat.) 122, 195 (1819).

269 U.S. CONST. art. I, § 8, cl. 4; Bankruptcy Act of 1841, ch. 9, 5 Stat. 440 (repealed 1843).

> Congress shall have power to establish uniform laws on the subject of any person's general inability to pay his debts . . . . [A narrower interpretation would be] utterly regardless of those obvious vicissitudes in a world full of changes, which might call for a corresponding enlargement or contraction of the bankrupt[cy] system.[270]

Justice Cantron (riding circuit) took a similarly expansive view: "[I]t extends to all cases where the law causes to be distributed the property of the debtor among his creditors; this is its least limit. Its greatest is discharge of the debtor from his contracts."[271] (This language was later adopted by the Supreme Court in *Louisville Joint Stock Land Bank v. Radford*.)[272]

Then, after further expansions of bankruptcy power in the also short-lived 1867 Act (which allowed corporations to file and, by 1874 Amendment, compositions to bind holdouts upon seventy-five percent dollar amount vote modeled after the English 1869 Act), challenges recurred that this had gone too far beyond Congress's authority to pass laws on the subject of bankruptcies.[273] But then-Judge Blatchford, in trial court, once again articulated the permissive view that bankruptcy laws were not ossified in the Georgian era and were to be interpreted expansively: "But the question recurs—what is the subject? The subject is 'the subject of bankruptcies.' What is 'the subject of bankruptcies?' It is not, properly, anything less than the subject of the relations between an insolvent or non-paying or fraudulent debtor, and his creditors, extending to his and their relief."[274]

After permanent legislation was enacted in 1898, the Supreme Court was by this point singing from a common hymnal upon constitutional challenges: "Congress may prescribe any regulations concerning discharge in bankruptcy that are not so grossly unreasonable as to be incompatible with fundamental law."[275] To be sure, in the significant legislative expansions in the 1930s to reorganizations (corporate and individual), which allowed technically *solvent* entities to file,

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270 Kunzler v. Kohaus, 5 Hill 317, 321–23 (N.Y. 1843).

271 *In re* Klein, 14 F. Cas. 716, 718 (C.C.D. Mo. 1843) (No. 7,865).

272 295 U.S. 555, 588 n.18 (1935).

273 *See* Tabb, *supra* note 255, at 19–21.

274 *In re* Reiman, 20 F. Cas. 490, 496 (S.D.N.Y. 1874) (No. 11,673); *see also* 2 JOSEPH STORY, COMMENTARIES ON THE CONSTITUTION OF THE UNITED STATES § 1113, at 53 n.2 (2nd ed. 1851) ("Perhaps as satisfactory a description of a bankrupt law, as can be framed, is, that it is a law for the benefit and relief of creditors and their debtors, in cases, in which the latter are unable, or unwilling to pay their debts. And a law on the subject of bankruptcies, in the sense of the constitution, is a law making provisions for cases of persons failing to pay their debts.").

275 Hanover Nat'l Bank of the City of N.Y. v. Moyses, 186 U.S. 181, 192 (1902).

exasperation boiled over once again.[276] Commentators complained that such innovations rendered the amendments subject to constitutional attack,[277] with one decrying that the expansion "creates a most novel proceeding, totally non-germane to the 'subject of bankruptcies,' and endeavors to extend the jurisdiction of the Federal Courts by forcibly making it a part of the bankruptcy law."[278] Still, the Court held firm, with Justice Sutherland apparently praising the law as "radically progressive" and demonstrating "in a very striking way the capacity of the bankruptcy clause to meet new conditions" and attend to the demands of "tremendous growth of business," concluding that each successive historical expansion did not go "beyond the limit of congressional power; but rather have constituted extensions into a field whose boundaries may not yet be fully revealed."[279] The power, it was described broadly, covered "any person's general inability to pay their debts."[280]

The lenient treatment of the Bankruptcy Clause's limitations had thus become entrenched in U.S. jurisprudence. Indeed, in *Wright v. Union Central Life Insurance, Co.*, another New Deal case challenging the Frazier-Lemke Act (a five-year farm foreclosure moratorium),[281] the Court had to rely on the Takings Clause to do the work, candidly conceding contemporaneously on the Bankruptcy Clause that "[t]he subject of bankruptcies is incapable of final definition. The concept changes."[282]

This quick march through the United States' difficulty of defining "bankruptcy law," at least for constitutional purposes, is not intended to demoralize the reader with nihilism. There are some limits on what is "on

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276 Vincent L. Leibell, Jr., Comment, *The Chandler Act—Its Effect Upon the Law of Bankruptcy*, 9 FORDHAM L. REV. 380, 400 (1940).

277 *See, e.g.*, John Gerdes, *Constitutionality of Section 77B of the Bankruptcy Act*, 12 N.Y.U. L.Q. REV. 196, 196 (1934); Albert K. Stebbins, *Constitutionality of the Recent Amendment to the Bankruptcy Law*, 17 MARQ. L. REV. 163, 172 (1933); James R. Morford, *Federal Legislation for Corporate Reorganization; A Negative View*, 19 A.B.A. J. 702, 703 (1933).

278 Stebbins, *supra* note 277, at 172 (quoting U.S. CONST. art. I, § 8, cl. 4).

279 Cont'l Ill. Nat'l Bank & Tr. Co. of Chi. v. Chi., R.I. & Pac. Ry. Co., 294 U.S. 648, 671 (1935).

280 *Id.* at 670 (quoting Kunzler v. Kohaus, 5 Hill 317, 321 (N.Y. 1843)). The only limit offered was this cryptic near tautology:

> But, while it is true that the power of Congress under the bankruptcy clause is not to be limited by the English or Colonial law in force when the Constitution was adopted, it does not follow that the power has no limitations. Those limitations have never been explicitly defined, and any attempt to do so now would result in little more than a paraphrase of the language of the Constitution without advancing far toward its full meaning.

Id. at 669–70.

281 *See* Wright v. Vinton Branch of Mountain Tr. Bank of Roanoke, 300 U.S. 440, 456–57 (1937).

282 Wright v. Union Cent. Life Ins. Co., 304 U.S. 502, 513 (1938).

the subject of Bankruptcies."[283] As Plank quips, it is doubtful Congress could ban hand guns within one hundred feet of schools under the Bankruptcy Clause.[284] He also argues, normatively, that Congress could not conscript private citizens to fund a debtor's rehabilitation under the Bankruptcy Clause, although that is less clearly historically compelled.[285] In a thoughtful piece, Professor Jonathan Lipson offers a hypothetical subprime mortgage chapter of the Code and provides a framework for assessing its propriety (turning on public interests and invoking the *Regional Rail Reorganization Act Cases*' Takings Clause test) that gets closer to the consumer scheme envisioned by this Article, although he is ultimately cagey on whether such a chapter would be constitutional on even his own test.[286] Trying to cull a general test from the jurisprudence presented above, we do see some focus on, broadly, the relationship between a financially distressed debtor and his creditors (plural).

On the scholarly side, Plank advocates for the following normative test: a law "on the subject of Bankruptcies" must be restricted to one in which (1) the debtor is insolvent and (2) the only parties subject to legal adjustment are the debtor and creditors (pointedly, not third parties).[287] Plank's proposed test is serviceable, though not inexorable.[288] For example, one does worry about a possible third requirement intrinsic in the plural reference to *creditors* in the U.S. cases canvassed above: a collectivity component. Indeed, earlier in this Article, collectivity was proposed as a possibly essential attribute of a bankruptcy system.[289] Might we need to modify Plank's test to include a third component and possibly elevate collectivity to constitutional status in the United States? Other scholars writing outside the U.S. context, such as Professor Horst Eidenmüller (channeling Professor Thomas Jackson), would normatively insist that we do so.[290]

283 U.S. CONST. art. I, § 8, cl. 4.

284 Plank, *supra* note 266, at 491.

285 *Id.* at 564. Such a law might already violate other constitutional provisions regarding Due Process and taxation. *Cf.* Ry. Lab. Execs. Ass'n v. Gibbons, 455 U.S. 457, 466–67 (1982) (dictum) (Commerce Clause cannot rescue Bankruptcy Clause–violating laws).

286 Jonathan C. Lipson, *Debt and Democracy: Towards a Constitutional Theory of Bankruptcy*, 83 NOTRE DAME L. REV. 605, 692–94 (2008) (discussing *Regional Rail Reorganization Act Cases*, 419 U.S. 102, 137 (1974)).

287 Plank, *supra* note 266, at 545.

288 Also, as Plank himself notes, the 1570 Statute of Elizabeth required half the fraudulent debtor's assets to be forfeited to the State, regardless of the State's status as a creditor, which seems to undermine a historical "no-noncreditor-interests" rule. *Id.* at 559; 13 Eliz. c. 5 § 3 (1570) (Eng.).

289 European scholars are showing the way on defining "insolvency." *See, e.g.*, Stephan Madaus, *Leaving the Shadows of the US Bankruptcy Law: A Proposal to Divide the Realms of Insolvency and Restructuring Law*, 19 EUR. BUS. ORG. L. REV. 615, 616–18 (2018).

290 Eidenmüller, *supra* note 68, at 56, 66–67 (citing JACKSON, LOGIC AND LIMITS, *supra* note 31).

Reconsider the car scheme in light of the constraints of a "Modified Plank Test," or perhaps a "Plank-Eidenmüller Test."[291] Taking the lowest hanging fruit first, it would not raise third-party concerns because the car petition would be straight in the wheelhouse of the debtor and a creditor. (Plank's concerns, anyway, were mostly directed at the mischief of the federal government using the Bankruptcy Clause as an end run around the Commerce Clause to regulate intrastate economic activity, under the veneer of preventing bankruptcy.)[292]

2. Collectivity?

Shifting to the suggestion of a possible collectivity component, the car scheme appears to be on shakier ground. Given the uncertainty of the Supreme Court's pronouncements, of course, one might be loath to overread the plural usage of "creditors" as signaling a mandatory component of the scope of the federal bankruptcy power, especially in light of an overarching disposition toward congressional deference. But even if not constitutionally dispositive, the concept of collectivity is, as argued above, central to many understandings of a bankruptcy system.[293] As Congress itself has reported, "[T]he nature of bankruptcy is to sort out all of the debtor's legal relationships with others."[294] Also recall that the corporate scheme of arrangement, while not "inclusive," still has a collective class voting on debt adjustment.[295] It is from that perspective that one must assess whether a car scheme—with its intentionally one-on-one design—is simply too far afield to be meaningfully considered

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291 The subsequent discussion is not intended as a normative endorsement of their theories. For persuasive rebuttal, see Mokal, *supra* note 8, at 426–29. Rather, it is to address the viability of a consumer scheme under U.S. constitutional law using their more restrictive conceptions of "insolvency proceedings." *Cf.* Lubben, *supra* note 246, at 337 ("In the American colonies, many early debtor-creditor laws lacked the collective nature of bankruptcy as it had already developed in England.").

292 Plank, *Limits*, *supra* note 266, at 556. Of special irritation to Plank was the purported justification of federal anti–loan-sharking provisions of the Consumer Credit Protection Act of 1968, where the House conferees explained that extortionate debts "deprive the debtor of a Federal statutory right" to bankruptcy and hence enacting a federal criminal law proscribing loan-sharking "seems clearly within the power of Congress to protect the . . . right, and to assure that the bankruptcy laws will be carried into execution." *Id.* at 556–57 (quoting H.R. REP. NO. 90-1397, at 2026 (1968) (Conf. Rep.)). When the Supreme Court upheld the law under the Commerce Clause, it avoided the Bankruptcy Clause justification. *See* Perez v. United States, 402 U.S. 146 (1971).

293 *See* Warner, *supra* note 69. In his excellent historical study, Plank claims (sadly, without direct citation) that some colonial-era laws allowed initiation of a proceeding by a debtor "against a single creditor." Plank, *supra* note 266, at 526.

294 H.R. REP. NO. 95-595, at 10 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5963, 5971.

295 Although this was not good enough to count as insolvency proceedings for *In re Ashapura Minechem Ltd.*, 480 B.R. 129, 141 (S.D.N.Y. 2012).

related to bankruptcy. And this collectivity concern is not restricted to oversecured car debt; it applies equally to the underwater car debtor seeking a discharge.

The role, and especially its essentialism, of collectivity is a remarkably complicated question that is currently at the vanguard of cross-border corporate insolvency theory, which provides a helpful domain to search for an answer to transplant (if the transplant takes) to the consumer realm. Accordingly, assessing the car scheme's normative "propriety" (a term to broaden the U.S. significance of "constitutionality")[296] requires a brief excursion into the unruly field of international bankruptcy.

When the modern era of cross-border insolvency law was birthed in the late 1990s, one of the knotty difficulties was how to confront the difference of substantive insolvency law systems around the world, which often came with grandiose claims of all-encompassing in rem jurisdiction.[297] Among the vectors of variance were the degree of private party control (e.g., secured creditor receiverships, divestment of debtor assets), that were challenged by some aspects of, in particular, U.S. law, such as the automatic stay and the debtor-in-possession (DIP) model. When UNCITRAL promulgated its successful Model Law on Cross-Border Insolvency,[298] and the EU promulgated its first Insolvency Regulation,[299] many of these difficult questions were elided. Instead, the solution was based on recognition and assistance of foreign insolvency proceedings by a domestic court, sidestepping (at least in the UNCITRAL project) the question of applicable law.[300]

This focus on foreign insolvency proceedings gave rise to its own definitional question of what constitutes an "insolvency proceeding" worthy of recognition. Both UNCITRAL (implemented in U.S. law as Chapter 15)[301] and the EU Regulation bake into their definitions a

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296 Mokal reminds that a purposive definition of "insolvency proceeding" can serve different functions in different contexts. Mokal, *supra* note 8, at 425.

297 *See, e.g.*, Frederick Tung, *Passports, Private Choice, and Private Interests: Regulatory Competition and Cooperation in Corporate, Securities, and Bankruptcy Law*, 3 CHI. J. INT'L L. 369, 375–76 (2002).

298 G.A. Res. 52/158, Model Law on Cross-Border Insolvency of the United Nations Commission on International Trade Law (Jan. 30, 1998).

299 Council Regulation 1346/2000, 2000 O.J. (L 160) 1 (EC).

300 UNCITRAL is now confronting that beast. U.N. Comm'n on Int'l Trade L., Working Grp. V (Insolvency L.), Applicable Law in Insolvency Proceedings, U.N. Doc. A/CN.9/WG.V/WP.183 (Oct. 7, 2022).

301 11 U.S.C. § 101 ("'[F]oreign proceeding' means a *collective* judicial or administrative proceeding . . . under a law relating to insolvency . . . in which proceeding the assets and affairs of the debtor are subject to control or supervision by a foreign court, for the purpose of reorganization or liquidation." (emphasis added)).

concept of collectivity, set out in the margin.[302] In evaluating whether a given proceeding is collective for the purpose of the Model Law, for example, a key consideration is whether "substantially all of the assets and liabilities of the debtor are dealt with in the proceeding."[303] Quintessentially excluded would be an individual enforcement action initiated by a single creditor (or creditors) to collect on a delinquent debt: "It is not intended that the Model Law be used merely as a collection

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> 1. This Regulation shall apply to public *collective proceedings*, including interim proceedings, which are based on laws relating to insolvency and in which, for the purpose of rescue, adjustment of debt reorganizationion or liquidation:
>
> (a) a debtor is totally or partially divested of its assets and an insolvency practitioner is appointed;
>
> (b) the assets and affairs of a debtor are subject to control or supervision by a court;
>
> (c) a temporary stay of individual enforcement proceedings is granted by a court or by operation of law, in order to allow for negotiations between the debtor and its creditors, provided that the proceedings in which the stay is granted provide for suitable measures to protect the general body of creditors, and, where no agreement is reached, are preliminary to one of the proceedings referred to in point (a) or (b).
>
> Where the proceedings referred to in this paragraph may be commenced in situations where there is only a likelihood of insolvency, their purpose shall be to avoid the debtor's insolvency or the cessation of the debtor's business activities.
>
> The proceedings referred to in this paragraph are listed in Annex A.

Recast Insolvency Regulation, *supra* note 6, art. 1, ¶ 1, at 29 (emphasis added); *see also id.* art. 2, ¶ 1, at 29 ("'[C]ollective proceedings' means proceedings which include all or a significant part of a debtor's creditors, provided that, in the latter case, the proceedings do not affect the claims of creditors which are not involved in them . . . ."). Warner aptly characterizes this ungainly definition as treating "factors like collectivity that are merely common to many insolvency proceedings as essential attributes but then pragmatically tacks on exceptions to add back in non-collective proceedings that the revision was designed to cover." Warner, *supra* note 69, at 162 (footnote omitted). Recital 14 expands:

> The collective proceedings which are covered by this Regulation should include all or a significant part of the creditors to whom a debtor owes all or a substantial proportion of the debtor's outstanding debts provided that the claims of those creditors who are not involved in such proceedings remain unaffected. Proceedings which involve only the financial creditors of a debtor should also be covered. Proceedings which do not include all the creditors of a debtor should be proceedings aimed at rescuing the debtor. Proceedings that lead to a definitive cessation of the debtor's activities or the liquidation of the debtor's assets should include all the debtor's creditors. Moreover, the fact that some insolvency proceedings for natural persons exclude specific categories of claims, such as maintenance claims, from the possibility of a debt-discharge should not mean that such proceedings are not collective.

Recast Insolvency Regulation, *supra* note 6, recital 14.

303 U.N. COMM'N ON INT'L TRADE L., UNCITRAL MODEL LAW ON CROSS-BORDER INSOLVENCY WITH GUIDE TO ENACTMENT AND INTERPRETATION, at 40, U.N. Sales No. E.14.V.2 (2014) [hereinafter MLCBI Guide]; *see also id.* ("A proceeding should not be considered to fail the test of collectivity purely because a class of creditors' rights is unaffected by it.").

device for a particular creditor or group of creditors who might have initiated a collection proceeding in another State."[304] Indeed, this Article above styles collectivity as a possibly canonical component of bankruptcy law. Where the rubber hit the road, however, on the cross-border scene was precisely with the noncomprehensive scheme of arrangement that was the inspiration for this proposal. How, then, did the international crowd address the scheme?

The initial answer is not warmly. Indeed, the original EU Insolvency Regulation excluded the scheme from its Annex A (more precisely, the United Kingdom did not include it) of recognized insolvency proceedings subject to its scope, an exclusion that carried through to its recast regulation (Recast).[305] But almost as soon as the scheme was left out in the cold, the market lust for the procedure could not be ignored. The Americans, with their cooperation-forward jurisprudence, started to recognize schemes as foreign insolvency proceedings under Chapter 15.[306] So solicitous is the case law that a seminal Chapter 15 case on collectivity, *In re Betcorp Ltd.*, recognized an Australian proceeding that even the Australians themselves thought might not fit under the statute.[307] The collectivity requirement was denuded in *Betcorp* into an obligation only that general creditors' interests be "considered" in the proceeding, which may be formally restricted to fewer constituents than the whole.[308]

It is thus no surprise that when the EU recast its Insolvency Regulation in 2015,[309] it relaxed the collectivity requirement in the definition of an insolvency proceeding from requiring "all" the creditors

304 *Id.* at 39; *see also In re* Betcorp Ltd., 400 B.R. 266, 281 (Bankr. D. Nev. 2009) ("This is in contrast, for example, to a receivership remedy instigated at the request, and for the benefit, of a single secured creditor."); *In re* Gold & Honey, Ltd., 410 B.R. 357, 370 (Bankr. E.D.N.Y. 2009) (excluding receivership as "more akin to a individual creditor's replevin . . . action").

305 Recast Insolvency Regulation, *supra* note 6, annex A, at 60–63. That the scheme is omitted from Annex A does not mean, oddly, that it is not an "insolvency proceeding." In the landmark *Gategroup* decision, the UK High Court held that a Part 26A Restructuring Plan (which for present purposes can be thought of as a scheme) is an insolvency proceeding for purpose of the insolvency exclusion of the Lugano Convention—pursuant to an analysis conducted under the EU Insolvency Regulation's criteria! Re Gategroup Guarantee Ltd., [2021] EWHC (Ch) 304 [57], [137] (Eng.). Thus, litigation persists over the scheme's status.

306 *See, e.g.*, *In re* Avanti Commc'ns Grp. PLC, 582 B.R. 603, 613 (Bankr. S.D.N.Y. 2018) (recognizing single bond class scheme under Chapter 15).

307 400 B.R. at 281 ("A collective proceeding is one that *considers* the rights and obligations of all creditors." (emphasis added)). Warner (rightly) pounces on this and notes that the "'consider' test is a minimal one that does not require the formal involvement of all creditors." Warner, *supra* note 69, at 167.

308 *Betcorp*, 400 B.R. at 281.

309 Recast Insolvency Regulation, *supra* note 6.

be involved to only "all *or a significant part*" of the creditors.[310] Collectivity became partial collectivity. Moreover, the Recitals to the Recast clarify a complex constellation of factors that can constitute collectivity, including that those creditors not included in the plan remain unaffected; that plans may restrict themselves only to "financial" creditors; that collectivity has lesser relevance in the reorganization (versus liquidation) context; and that the public (versus private) nature of the proceeding may also be relevant.[311] This has allowed the Europeans to follow the Americans at whittling away at full collectivity as a constitutive aspect of a foreign insolvency proceeding under this multifaceted definition.

The final European blow came with the 2019 Preventative Restructuring Directive (2019 Directive),[312] where scheme-like procedures were embraced,[313] DIPs that do not divest the debtor of control over assets heralded,[314] and numerous other aspects of "traditional" insolvency law for many wiped away by Directive-compulsion. Indeed, prominent European scholars have seen this as madness, worrying that French *sauveguardes* will follow English schemes into cross-border insolvency recognition tolerance, noting that a "restructuring" could technically encompass one creditor.[315] In the United States, Professor Ray Warner also pronounced the "death" of collectivity based on the trend line of cross-border insolvency cases.[316] That augur indeed appears correct. The recent UK "restructuring plans" under Part 26A of CIGA,[317] which effectively implement the mandate of the 2019 Directive and bear considerable similarity to the scheme of arrangement, have been adjudicated by UK courts as being "insolvency proceedings" for purposes of exclusion from the Lugano Convention.[318] Thus, although the scheme never made it formally into the EU Recast Annex A, its success heavily influenced the 2019 Directive. It may have

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310 *Id.* recital 14, at 20 (emphasis added); *id.* art. 2, ¶ 1, at 29.

311 *Id.* recitals 12–16, at 20.

312 Preventative Restructuring Directive, *supra* note 18.

313 *See, e.g.*, *id.* recitals 3–4, at 19 (embracing "[p]reventive solutions" rather than allowing restructuring only at "a relatively late stage").

314 *Id.* art. 2, ¶ 3, at 30.

315 Eidenmüller, *supra* note 68, at 59. Eidenmüller wrote when the Directive was still in its formative stage, but he saw the writing on the wall.

316 Warner, *supra* note 69, at 167.

317 Companies Act 2006, c. 46, pt. 26A, *amended by* Corporate Insolvency and Governance Act 2020, c. 12 (UK).

318 In *Gategroup*, Swiss law governed the debt being restructured. English courts could not ordinarily exercise jurisdiction over this debt, but the Court held that it had jurisdiction because Gategroup's restructuring plan under Part 26A fell into the bankruptcy exclusion in Article 23 of the Lugano Convention. Re Gategroup Guarantee Ltd. [2021] EWHC (Ch) 304 [137] (Eng.).

lost the battle but won the war, in other words, and its fatal influence on collectivity as a constitutive element of insolvency law in the cross-border context is difficult to overstate.

To be sure, collectivity has not disappeared altogether as a requirement of an insolvency proceeding; it is still formally on the books in Chapter 15.[319] But what the scheme-animated trend line of the corporate international jurisprudence has done is refocus collectivity away from a wooden fixation on numerosity into one trained on absentee fairness.[320] It is not so much that bankruptcy proceedings cannot leave some creditors uninvolved and still be "insolvency proceedings," it is more that *if* they leave some creditors uninvolved, *then* those proceedings cannot impair the rights of the absentees,[321] as the EU Recast Recitals expressly contemplate. Warner aptly captures this trend: "Moving even further from the traditional conception of collectivity [the Recast] expands it from a numerosity requirement into a procedural due process requirement."[322] Were the Supreme Court—which has already trumpeted methodologically regarding the Bankruptcy Clause that it prefers deference to Congress's assessment of the pragmatic exigencies of the day over historical usage of terminology—to consider whether strict collectivity were required as a necessary component to a law being "on the subject of Bankruptcies" for U.S. constitutional purposes, it would (assuming consistency) likely turn to these modern developments to buttress a progressive solicitude.

The normatively inclined reader may bristle at the pragmatic revisionism on display. One could understand intellectual dissatisfaction at the circularity of being told schemes meet the definition of "insolvency proceedings" because the conception of insolvency proceedings as necessarily including a collective component has been eroded to ensure that schemes of arrangement, due to their practical popularity in the international corporate world, can be included within the definition of insolvency proceedings. "This is a pragmatic approach that may be considered appropriate in a political setting. However, from a conceptual and scholarly perspective this approach is unsatisfactory because it lacks a consistent and convincing normative basis."[323] But we should not succumb to this grumpiness. Digging deeper into the basis of collectivity, as Mokal has elegantly done in a recent article, one can appreciate that collectivity and indeed the very definition of an insolvency proceeding is

319 *See, e.g.*, *In re* Ashapura Minechem Ltd., 480 B.R. 129, 141 (Bankr. S.D.N.Y. 2012) (suggesting in dictum that single-class proceedings would not be collective).

320 *See, e.g.*, *In re* Brit. Am. Ins. Co., 425 B.R. 884 (Bankr. S.D. Fla. 2010).

321 *Ashapura*, 480 B.R. at 140–41.

322 Warner, *supra* note 69, at 164.

323 Eidenmüller, *supra* note 68, at 60.

"scalar" (non-dichotomous) in his terms.[324] This more nuanced understanding allows seeing the refocus of collectivity onto due process issues not as an end run around purpose but as a normatively consonant refinement of doctrine. Indeed, it allows all the factors (private versus public proceeding, rescue versus liquidation) to contextualize the meaning of "collective" that serves in the definition of an insolvency proceeding.[325]

Moreover, in offering as the anti-example of an insolvency proceeding an *individual creditor's action* collecting on a debt,[326] UNCITRAL suggests room for a protective, debtor-initiated, rescue/reorganization proceeding (as embraced in the new Restructuring Directive) to serve as a contrast from the anti-example. In other words, it is not the *number* that matters so much as the *purpose*. Bankruptcy, anchored in the consumer context by the abuse-policed discharge, is about financial relief, and that relief may be needed from all, most of, or even in appropriate circumstances, just one of the debtor's creditors.[327] It may be that debtors cannot find meaningful reorganization prospects without adjusting the debts of a single creditor. From the due process perspective, so long as none of the other creditors has any rights imperiled, numerosity for the sake of itself seems almost arbitrary.[328] Thus, there are compelling reasons why a single-creditor consumer scheme of debt adjustment may be sufficiently "collective" (if that word still makes sense to use) to be an "insolvency proceeding." As such, we should resist concern that the one-off nature of a proposed consumer scheme should render it subject to constitutional suspicion in the United States as exceeding the bankruptcy power of the federal government.[329]

324 Mokal, *supra* note 8, at 421 ("[I]nsolvency is a scalar attribute, that is, it is a matter of degree. We can make this point by first considering solvency, another scalar attribute. While two debtors, *X* and *Y*, may both be solvent, *X* may be *more* solvent than *Y* because (say) the value of its liquid assets exceeds the quantum of its liabilities as they fall due to a far greater degree than is the case with *Y*. The same holds *mutatis mutandis*, for insolvency."); *see also In re* LTL Mgmt., LLC, 58 F.4th 738, 761 (3d Cir. 2023) (referring to "highly solvent" debtor).

325 Mokal would perhaps consider this a "purposive" definition of collectivity.

326 MLCBI Guide, *supra* note 303, at 39.

327 Preventative Restructuring Directive, *supra* note 18, recital 21, at 22.

328 *See* Recast Insolvency Regulation, *supra* note 6. A corollary might be the holistic fairness review of the scheme sanctioning hearing to make sure that the one creditor is not being unfairly treated. Paterson & Walters, *supra* note 3 (manuscript at 45).

329 *See infra* notes 337–38 and accompanying text (discussing cases where filing for bankruptcy to avoid single creditor constitutes bad faith).

3. Insolvency?

The foregoing analysis has sought to assuage concerns that a car scheme's "minimally collective" posture takes it outside the scope of bankruptcy law. Unfortunately, for oversecured car debts, there remains the third constitutive component proposed by the Plank-Eidenmüller Test: insolvency. Thus, a car scheme may be on sufficiently firm footing when applied to an underwater debtor who needs discharge from unmanageable car debt, because discharge is central to the federal bankruptcy power, even if only with one creditor.[330] So while we have perhaps solved the problem of a one-off creditor scheme in terms of collectivity, would application of that regime to *fully solvent* debtors be too much (e.g., those with oversecured car debt who have fallen behind on their payments)? This is, concededly, a harder row to hoe, and may drive much of the skepticism over the scheme's proper classification.

To be sure, a quick doctrinal answer might involve pointing to the longstanding U.S. rule (and now UK restructuring proceeding rule) that insolvency is no longer, paradoxically for some, a requirement to open insolvency proceedings.[331] Indeed, one of the doctrinal reasons for relaxing insolvency as a rigid requirement in Europe is the goal of the Preventative Restructuring Directive—namely, to nip financial distress in the bud before it cascades into a broader crisis and its attendant negative externalities.[332] As such, the looser U.S. approach of looking at "financial distress" more broadly than strict "insolvency" seems attractive.[333]

330 *See* Michelle M. Harner, *Rethinking Preemption and Constitutional Parameters in Bankruptcy*, 59 WM. & MARY L. REV. 147, 164–65 (2017).

331 *See, e.g.*, Fields Station LLC v. Capitol Food Corp. of Fields Corner (*In re* Capitol Food Corp. of Fields Corner), 490 F.3d 21 (1st Cir. 2007).

332 Preventative Restructuring Directive, *supra* note 18, recital 2, at 18 ("Restructuring should enable debtors in financial difficulties to continue business, in whole or in part, by changing the composition, conditions or structure of their assets and their liabilities . . . ."); Companies Act 2006, c. 46, § 901A (UK) ("(1) The provisions of this Part apply where conditions A and B are met in relation to a company. (2) Condition A is that the company has encountered, or is likely to encounter, financial difficulties that are affecting, or will or may affect, its ability to carry on business as a going concern.").

333 *E.g.*, *In re* LTL Mgmt., LLC, 58 F.4th 738, 755–57, 761 (3d Cir. 2023), *amended and superseded by* 64 F.4th 84 (3d Cir. 2023). Mokal notes that even the formalist must concede that insolvency is only one ground for a corporate winding up petition under UK law, yet few would doubt a corporate liquidation is an "insolvency proceeding." Mokal, *supra* note 8, at 424. This is a touchy issue in the international sphere. The Singapore Court of Appeal (its court of last instance) recently reversed its High Court to hold that an insolvency proceeding, under its enactment of the MLCBI, need not be based upon the debtor's actual insolvency or even financial distress, because the Singapore gloss of a "law related to insolvency" intends a broader reach. The opinion's canvasing of other jurisdictions is studious but may understate the role of good faith (discussed *infra* at notes 335–38) in U.S. law. Ascentra Holdings, Inc. v. SPGK Pte Ltd. [2023] SGCA 32 (Sing.).

Moreover, simply because a debtor initiating a car scheme is oversecured in the car does not mean that the debtor lacks financial distress (or is even solvent for that matter).

Plank, for his part, worries about going beyond insolvency as a gatekeeping requirement, not so much for rigid categorization but to combat cases that have arisen in the bad faith jurisprudence under the Code (although he does ultimately settle on rigid categorization).[334] The absence of a strict insolvency requirement under U.S. law has been justified in part on the bad faith screen picking up much of the work that an insolvency screen would, which it tends to do.[335] These are cases where, to generalize broadly, a debtor who otherwise does not have financial distress seeks access to the bankruptcy courts to exploit a substantive provision of the Bankruptcy Code to the detriment of a specific creditor (e.g., a commercial tenant with no other financial problems who wants to engage the Code's cap on landlord damages claims to browbeat a landlord—or more recently, mass tort litigation advantage).[336] As such, it is not insolvency for the sake of insolvency, but insolvency as a proxy for *bona fide (i.e., good faith) financial distress*. Car debtors in default on their loans, especially if facing imminent repossession, surely would be seen as nonexploitative users of debtor relief law.

Relatedly, though, many of the bad faith cases in the consumer context involve debtors who have only a two-party dispute and are not in generalized financial distress, essentially crossing over into collectivity concerns and finding its absence an indication of bad faith.[337] But even these cases often involve an element of sneakiness or naughtiness that is absent from a genuine situation of a car borrower experiencing a liquidity

334 Plank, *supra* note 266, at 547–48.

335 *See, e.g.*, *In re* Bandini, 165 B.R. 317 (Bankr. S.D. Fla. 1994) (holding that debtor with liquid assets worth triple his ex-wife's alimony claim could not use Chapter 13 to drag out payments over five years without interest); *cf. LTL Mgmt.*, 58 F.4th at 754–58 (finding bad faith in lack of genuine financial distress when corporate affiliate underwrote debtor's liabilities).

336 Solow v. PPE Enters. (U.S.), Inc. (*In re* PPI Enters. (U.S.), Inc.), 324 F.3d 197, 211–12 (3d Cir. 2003); *see also* Blumenberg v. Yihye (*In re* Blumenberg), 263 B.R. 704, 715 (Bankr. E.D.N.Y. 2001) (finding bad faith filing of Chapter 11 petition in absence of any attempt to reorganize as debtor's true intent was to launch collateral attack on breach of contract defeat while staying collection).

337 *See, e.g.*, *In re* Brown, 88 B.R. 280 (Bankr. D. Haw. 1988) (finding bad faith where ophthalmologist-debtor filed Chapter 7 bankruptcy petition to avoid payment after losing a medical malpractice claim). Of course, bad faith is a totality of circumstances analysis, sometimes called a "smell test," Morgan Fiduciary, Ltd. v. Citizens & S. Int'l Bank, 95 B.R. 232, 234 (S.D. Fla. 1988), and so having one creditor will not, on its own, suffice to show bad faith, Janvey v. Romero, 883 F.3d 406, 414–15 (4th Cir. 2018). For example, in *In re Keobapha*, the debtor was found liable for the wrongful death of two motorists and filed a bankruptcy petition in response. Deglin v. Keobapha (*In re* Keobapha), 279 B.R. 49 (Bankr. D. Conn. 2002). The court found a lack of bad faith given the debtor's meager financial condition. *Id.* at 52–53.

crisis.[338] Thus, if "insolvency" is recast, as it has in the corporate context, as "good faith financial distress," there should not be resistance to embracing debtors in genuine financial struggle, even if that distress is restricted to one specific creditor.[339]

The real problem is whether the whole is greater than the sum of its parts. That is, while it may be acceptable to have "bankruptcy law" address a single-creditor dispute within a modern understanding of collectivity, and while it may be acceptable to have debtors who have equity in their cars and hence access to a "car scheme" even if they are not "car-insolvent," can we put it all together? Especially if debtors do not receive a discharge of any unsecured debt, is the combination of a "solvent-ish" debtor who only seeks to readjust a debt with one creditor simply too far afield from bankruptcy to fit even the U.S. Supreme Court's permissive approach to bankruptcy jurisdiction? Although a definitive answer cannot be offered on the scant jurisprudence and the innovative nature of the car scheme proposal, we can repair to the background principles of insolvency law: to come to the assistance of debtors who are in financial trouble.[340] Again, as discussed above, Congress could gatekeep access by requiring clear indicia of such distress (limits on car value, loan-to-value ratio, etc.). And, importantly, the oversight power of a bankruptcy court would presumably remain, complete with its discretionary authority to dismiss cases filed in bad faith by someone who looks like a truly financially capable debtor who has just gotten into a tiff with their lender and now declines to pay out of spite.[341] To be sure, were cars highly cyclical assets, we might worry about a savvy debtor stripping down their liens ("lien capping," really, not lien stripping) at a nadir in collateral value. But family cars, as consumer bankruptcy petitioners will attest, tend not to appreciate in value. Accordingly, although it would perhaps require challenging our conventional understandings of laws "on the subject of Bankruptcies," a consumer scheme, even a car scheme regarding an oversecured car, does seem plausibly within the normative ambit of U.S. bankruptcy power.

338 *See, e.g.*, Piazza v. Nueterra Healthcare Physical Therapy, LLC (*In re* Piazza), 719 F.3d 1253 (11th Cir. 2013) (affirming as bad faith petition filed in response to losing state court litigation when debtor had been transferring thousands each month to his wife and paying off his great-aunt's mortgage instead of trying to pay the victorious plaintiff).

339 *LTL Mgmt.*, 58 F.4th at 754–57 (describing financial distress as a touchstone of "insolvency"); *see also* Preventative Restructuring Directive, *supra* note 18, recital 2, at 18 (listing benefits of restructuring for debtors facing financial difficulties rather than insolvency).

340 *See* Preventative Restructuring Directive, *supra* note 18.

341 *See, e.g.*, Indus. Ins. Servs., Inc. v. Zick (*In re* Zick), 931 F.2d 1124, 1126–27 (6th Cir. 1991).

4. Summary

It is a fair challenge to ask whether a one-creditor proceeding to restructure a car loan with a debtor that has equity in the car (and hence is "car-solvent") even fits within the paradigm of bankruptcy law. There is no supermajority vote, as with a scheme of arrangement. Normatively, if there is no buy-in analogous to the Chapter 7 asset forfeiture or the Chapter 13 income tithe, is there sufficient moral hazard protection to safeguard the benefits of, in the strong case, a discharge, or, in the weaker case, a cramdown? Doctrinally, constitutionally, and perhaps even ontologically, is it even a "bankruptcy" proceeding absent insolvency of the debtor (as Plank would require) or collectivity of creditors (as would Eidenmüller)? Indeed, the answer to one of these questions—that we might combat normative theory's moral hazard concerns by withholding the discharge—seems to run smack into other questions of scope (if the proceeding leads to no discharge, is it even a bankruptcy?).

The answer to these concerns lies in a progressive approach to these seeming cores of modern consumer bankruptcy law. Informed by other aspects of corporate law, such as developments in the cross-border realm, we can see that the concept of collectivity is undergoing profound change and moving away from a rigid fixation on numerosity. And insolvency has long been interpreted flexibly to mean, functionally, genuine financial distress. The scheme of arrangement has shown that a stay or even an estate is not truly essential. As such, these issues with a consumer scheme of arrangement, while important and discussion worthy, can be overcome.

A modular consumer bankruptcy proceeding structured around an asset class, exemplified by a "car scheme," would work largely as a limited Chapter 13 proceeding, perhaps borrowing the Chapter 7 power for asset redemption. There would be no need for a trustee (other than general public oversight by a U.S. trustee and bankruptcy court), and no need for complex asset scheduling and hearings. Calmed by a stay, the debtor and creditor would either agree to a voluntary restructuring of the debt or, as with Chapter 13, a plan could be crammed down over the creditor's objection provided that the full value of the allowed secured claim were paid off within the lifespan of the plan (leaving the creditor no worse off). As for the unsecured claim of deficiency, it could either be discharged, survive, or (more experimentally) subjected to some formula for pro rata discharge. An oversecured car loan could have any surplus equity remain with the debtor. Such a system would comport with the normative theories of consumer debt discharge canvassed at the outset of this Article because abuse concerns would be substantially attenuated and still, in their attenuated form, be adequately policed.

It is true that such a system might push the boundaries of the scope of bankruptcy law. It would sacrifice collectivity and, in some cases, even literal insolvency. It might even forego the presumed central telos of consumer bankruptcy law: discharge. But modern, flexible approaches toward both collectivity (in the cross-border realm) and insolvency (in the good faith realm) can situate such modular proceedings comfortably in bankruptcy law's wheelhouse. The scheme of arrangement has already shown us the way. More importantly, the system could provide meaningful debtor relief from financial distress at a fraction of the cost.

CONCLUSION: LOOKING FORWARD

Discussing current data that tend to suggest meaningful consumer demand for noncomprehensive bankruptcy relief, this Article has argued for modular consumer bankruptcy proceedings. It proposed, as an example, a "car scheme," premised upon the British scheme of arrangement so popular in the corporate restructuring world. It grounded this proposal in an analysis of the normative foundations of consumer bankruptcy law and its essential attributes. It has argued that the car scheme would not violate these fundamental understandings of bankruptcy law, although it might require rethinking of bankruptcy's boundaries and even of its most fundamental core, the consumer discharge. Importantly, it also maintained that the grand bargain that polices the moral hazard regarding discharge of traditional consumer bankruptcy would either be inapposite to or find outlet through acceptable alternative means. A final word, however, is in order—one that looks to the future and considers what some members of the U.S. Congress have proposed as a radical (and, some would say, long overdue) overhaul of the consumer bankruptcy system.

In 2022, Senators Elizabeth Warren and Sheldon Whitehouse introduced Senate Bill 4980, the Consumer Bankruptcy Reform Act.[342] It cites in its introductory section of congressional findings that the purpose is to "streamlin[e] the process of filing for bankruptcy . . . and lower[] the cost of bankruptcy for both consumers and creditors."[343] Would this modernization comport with the recommendations of this Article? Perhaps surprisingly, the answer is yes.

The primary thrust of the bill is to eliminate the Chapter 7/13 distinction and replace it with one omnibus consumer Chapter 10. The proposal effectively combines the asset forfeiture and income tithe

342 Consumer Bankruptcy Reform Act of 2022, S. 4980, 117th Cong. (2022); *see also* Consumer Bankruptcy Reform Act of 2020, S. 4991, 116th Cong. (prior version).

343 S. 4980, § 101(b)(1).

requirements of those chapters by setting a "repayment amount" that must be turned over to creditors over a "repayment plan," and allows for turnover of nonexempt assets to fulfill this obligation in the new chapter.[344] The reform is intentionally progressive, pegging the repayment amount at zero for many debtors with incomes near or below the median.[345] Of particular interest for this Article, the bill also proposes "Property Plans," under which the debtor could refinance an individual piece of property—indeed, there are some special rules for motor vehicles—at market interest rates and valuations over a five-year payment period.[346]

So far, this just sounds like Chapter 13 regarding secured debt. But what is especially relevant for this Article is that the bill proposes, for the first time, and explicitly, modularity. Newly proposed sections 1051 to 1053 of the Bankruptcy Code would also allow so-called "Limited Proceedings," under which debtors could open bankruptcy petitions *limited to the specific asset on which they intend to file a Property Plan*.[347] This is exactly what this Article has argued for as a car scheme of arrangement. The Limited Proceeding would have strict time limits (e.g., seven days to file the Property Plan, thirty days to commence payments),[348] but would otherwise adopt many of the suggestions of this Article, such as minimizing the paperwork requirements to accelerate and simplify the bankruptcy process.[349] Importantly, the suggested legislation also recognizes some of the technical requirements discussed in this analysis, such as the noncreation of an estate (or, in its take, the creation of a mini-estate limited to the asset in question), the absence of a trustee, and even the need to regulate cross-default clauses.[350]

But most significantly, the bill demonstrates some legislative appetite for a bankruptcy proceeding that does not culminate in discharge.[351] A Limited Proceeding, while enjoining the limited creditor from pursuing the debtor after confirmation of the plan regarding the adjusted debt, would not discharge the debtor from any unsecured

344 *Id.* § 102; Press Release, Sen. Elizabeth Warren, Senator Warren and Representative Nadler Reintroduce the Consumer Bankruptcy Reform Act (Sept. 28, 2022), https://www.warren.senate.gov/newsroom/press-releases/senator-warren-and-representative-nadler-reintroduce-the-consumer-bankruptcy-reform-act [https://perma.cc/2W75-5CXP].

345 *See, e.g.*, S. 4980, sec. 102(a), § 1024(b)(2).

346 *Id.* § 1022(c). There are also special plans for residential mortgages ("Residence Plans"). *Id.* § 1022(b).

347 *Id.* §§ 1051–1053.

348 *Id.* § 1051(a).

349 *Id.* § 1052(7).

350 *Id.* §§ 1052(2)–(3), 1028(k).

351 Indeed, the bill clarifies it would leave all other rights of the secured creditor upon refinancing (and arrearage cure) "unaltered." *Id.* § 1028(h), (j).

deficiency (perhaps making its proponents "weak" in this Article's taxonomy); such relief would require a repayment plan plenary Chapter 10.[352] The moral hazard concerns of the grand bargain, thus, would not be engaged given the absence of a discharge. While there is no evidence the bill's sponsors turned their attention to the constitutional issues explored in some depth in this Article, presumably that is a job for the courts (and academics), not legislators. Moreover, abuse remains policed discretionarily, with importation of the Chapter 13 good faith requirements, albeit slightly retinkered as an absence of bad faith, and explicit provisions to allow dismissal of plans that would constitute a "manifestly improper use of the bankruptcy system."[353] So, too, do some of the progressive screens to target abuse through wealth proxies suggested in this Article find outlets in the bill's various terms, such as, for example, limiting car plans to cars "reasonably necessary for the support or maintenance of the debtor or a dependent of the debtor."[354]

Accordingly, the propitiously timed bill just introduced to Congress aligns strongly with the normative proposal of this Article. To be sure, there is not complete concordance,[355] and it is beyond the scope of this Article—well beyond, really—to opine on the political viability of the desired overhaul. (Certainly many a proposed bill to revise the bankruptcy system has withered on the congressional vine.)[356] But from a normative standpoint, the proposal would accurately implement the crux of this Article and, if adopted, allow for the first time modular ("limited") U.S. proceedings. And that is as it should be. Corporate debtors have had such cost-saving opportunities in the United Kingdom under the scheme of arrangement for centuries. Consumer debtors here deserve no less.

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352 *Id.* §§ 1028(d), 1031(a). Given the robustly progressive revisions to unsecured debt repayment obligations, it may actually be more accurate to characterize the integrated effect of the proposal as "strong" or even "Herculean"—even stronger than this Article's suggestions.

353 *Id.* § 1005(c).

354 *Id.* § 1024(d)(3)(A); *see also, e.g.*, *id.* § 1024(d)(1)(G) (restricting purchase money security interests on cars acquired within the past ninety days).

355 For example, the bill still struggles to preserve a role for voidable preferences. *Id.* § 1002(b)(1).

356 *See, e.g.*, Medical Bankruptcy Fairness Act of 2014, S. 2471, 113th Cong. (2014); Medical Bankruptcy Fairness Act of 2016, S. 3385, 114th Cong. (2016); Medical Bankruptcy Fairness Act of 2020, S. 4305, 116th Cong. (2020); Medical Bankruptcy Fairness Act of 2021, S. 146, 117th Cong. (2021).