A brief explanation of consumer bankruptcy and aspects of the bankruptcy estate in the United States of America

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Abstract

The American bankruptcy law system is considerably different from most other bankruptcy regimes. In place of the policy of advantage to creditors, which is the system prevailing in most western countries, and also in South Africa, the American system places considerable emphasis on the fresh start policy. While this policy assists debtors to build up a new estate by allowing them to keep a considerable number of their assets, the creditors are also looked after because of the further policy of the preservation of the bankruptcy estate, thereby possibly swelling the bankruptcy estate of the debtor. The exclusion of the debtor's assets from his or her bankrupt estate is known as exemption law. But whatever the policy, bankruptcy (insolvency in some jurisdictions) is, however, really a hopeless situation for all the parties involved, such as the creditors, the debtor, the state, and society in general. For this reason, some commentators submit that the debtor should be forgiven. This may be a sensible idea because if the fresh start policy is ignored in a bankruptcy system, a debtor may become a debt slave who is never able to escape from debt. He or she may then have to depend on social hand-outs, thereby ultimately placing a burden on the country's social system.

Introduction

The American bankruptcy regime is unique. Its policies and principles are liberal and debtor friendly, unlike the South African insolvency law system, which is essentially creditor friendly. Skeel puts it this way:

> Bankruptcy law in the United States is unique in the world. Perhaps most startling to outsiders is that individuals and business in the United States do not seem to view bankruptcy as the absolute last resort, as an outcome to be avoided at all costs. No one wants to wind up in bankruptcy, of course, but many US debtors treat it as a means to another, healthier end, not as the

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end.[1]

As with most bankruptcy systems, American law regulates the position of the bankrupt person in relation to his creditors and the position among those creditors inter se'. This also applies in the South African system when a debtor's estate is sequestrated in terms of the Insolvency Act 24 of 1936.[2] But from here on, the basis of the different international systems is very different from American law. 'Advantage to creditors'[3] is the policy followed by most countries, including South Africa, where the prevailing policy is that of advantage to the creditors as a group. The debtor is, however, dealt with rather harshly. But under consumer bankruptcy law[4] in America, the policy is one of a 'fresh start' for the unfortunate debtor. American law is sympathetic to the debtor as that system includes generous exclusions or exemptions of estate property which is then out of reach of the creditors.[5] In South African insolvency law, it has never really been considered whether there is a distinction between excluded and exempt property, and if there is, what the difference could be. As regards excluded and included assets, the United Kingdom has also made sweeping progressive changes', thereby adding some sense of humanity to a field of law that traditionally has been known for its inhumanity.[6]

The American bankruptcy system is regulated by the Bankruptcy Reform Act of 1978, which came into effect on 1 October 1979.[7] Referred to as the 'Bankruptcy Code', it is federal legislation embodied in Title 11 of the United States Code. Apart from the code, bankruptcy is also influenced by state law and a variety of non-bankruptcy legislation. The code was the first radical reassessment of bankruptcy legislation in America in almost a century. Before this the Bankruptcy Act of 1898 regulated American bankruptcy as the first comprehensive bankruptcy legislation in America.[8] The United States Constitution is the foundation of American bankruptcy law. It empowered Congress to establish uniform bankruptcy law throughout

1 DA Skeel *Debts dominion: a history of bankruptcy law in America* (2001) at 1.
2 Hereafter the Act.
3 E Bertelsmann *et al Mars the law of insolvency in South Africa* (9ed 2008) at 52, 108; CH Smith *The law of insolvency* (3ed 1988) at 26, 50.
4 The words bankruptcy and insolvency will be used interchangeably.
5 Generally 'excluded' property never forms part of an insolvent estate, while 'exempt' property is part of an insolvent estate but may be released to·the debtor if the trustee or the creditors agree to this. However, a distinction between the two is not always made, therefore this property is often just referred to as exempt property.
6 See Evans n * above at respectively at 83 and further and at 135 further See also J Calitz 'Developments in the United States' consumer bankruptcy law: a South African perspective' (2007) *Obiter* at 397.
7 Public Law No 95–598, 92 Stat 2459 as amended (1978).
8 LE Woodard *The practitioner's guide to consumer bankruptcy* (1996).

the United States.[9] The code applies to both juristic persons and natural persons, and it offers different methods of debt alleviation.[10]

The 1898 Act was complex. The 1978 amending legislation was intended to simplify the 1898 Act, but failed to do so. The code was in fact a complex statute that was amended several times in an attempt to cure its pitfalls.[11] However, for the purpose of the bankruptcy estate, the 1978 amendments were important because they introduced a small degree of clarity in respect of included and excluded property. Further amendments were embodied in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA)[12] Domiciliary and dollar limits on certain categories of exempt property were introduced by this Act. This development is part of a steady movement to steer bankruptcy policy in America away from the debtor-friendly approach, towards a creditor-friendly policy, thereby making it more difficult for debtors and insolvency practitioners to enter into bankruptcy proceedings.[13] In the present article, however, only aspects of individual consumer bankruptcy are considered,[14] particularly, in respect of the estate property in the code's chapters 7 and 13 proceedings.

A short description of the Bankruptcy Code

General

As described above, the United States' bankruptcy laws today address two different kinds of bankruptcy, namely individual debtor bankruptcy (also referred to as consumer bankruptcy) and the financial distress of corporations.[15] Although these two fields overlap to some extent, they do raise different policy issues. This paper concentrates primarily on aspects of the bankruptcy of individuals in America. The central concept in personal bankruptcy in the American framework is the discharge.[16] When a debtor receives a discharge, his existing obligations end, and creditors can no longer

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9 Article I, s VIII of the United States Constitution.

10 See chapters 7, 11, 12 and 13 of the Code.

11 The most notable problems related to the jurisdiction of the Bankruptcy Court and to the Bankruptcy Court judge. These problems were alleviated by amendments in 1984. The recession of the late 1980s and early 1990s affected the values of assets, and debtors' liabilities rose dramatically, prompting further amendments to the Code in 1994. See Woodard n 8 at 6.

12 Hereafter also referred to as BAPCPA.

13 See the paragraph on BAPCPA below.

14 See *The paths to personal bankruptcy* below.

15 See generally, K Gross *Failure and forgiveness: rebalancing the bankruptcy system* (1997) ; E Warren & JL Westbrook *The law of debtors and creditors: text, cases and problems* (3ed 1996) at 207; WC Whitford 'The ideal of individualized justice: consumer bankruptcy as consumer protection and consumer protection in consumer bankruptcy' 1994 *Am Bankr LJ* at 397.

16 Skeel n 1 above at 6; DJ Whaley & JW Morris *Problems and materials on debtor and creditor law* (1998) at 4.

look to the debtor to collect the discharged obligation.[17]

Before further discussion, it may, at this point, be appropriate to give a brief overview of the structure of the Bankruptcy Code in order to place the position of consumer bankruptcy in perspective.

The structure of the Bankruptcy Code

The Code,[18] in Title 11 of the United States Code, is divided into chapters, designated as such in Arabic numerals (for example chapter 11) to distinguish it from the 1898 Act which used Roman numerals (for example chapter XI). The Code is numbered in uneven numbers, for example, chapters 1, 3, 5, 7 and so on. The even numerals have been reserved for additions to the code, with chapter 12, included in 1986 for family farmers, currently taking up the only even number.[19]

The sections in the first three chapters of the Code are of general application to the chapters that follow. Chapter 1, for example, is devoted to definitions, rules of construction, general powers of the bankruptcy court, and the qualification of debtors who are eligible for each of the types of proceedings available. Chapter 3 governs the most important administrative and procedural sections in the Code. Sub-chapter I of chapter 3 governs the commencement of a case, describing how a voluntary and an involuntary proceeding commences. Officers are dealt with in sub-chapter II, which provides, among other things, who may serve as trustees. Sub-chapter III deals with a variety of procedural rules. Sub-chapter IV is one of the more significant provisions of the Code, containing provisions on adequate protection, the automatic stay, executory contracts, and unexpired leases.

Chapter 5, entitled 'Creditors, the Debtor, and the Estate', contains provisions relating to creditors, their claims and administrative expenses. Section 522, dealing with property excluded from the estate, establishes a set of (United States) federal exemptions which a debtor may choose in lieu of any (United Sates) state exemptions available. This is a radical departure from the American tradition and from the Bankruptcy Act of 1898 under which a debtor was limited to state exemptions and no federal set of exemptions existed. These federal exemptions are considerably more generous than the exemptions accorded a debtor under the laws of many

17 Skeel n 1 above at 6.

18 Bankruptcy Reform Act of 1978.

19 See, generally, MD Scott & LP King *2002 Collier pamphlet edition: part 1 bankruptcy code* (2001); LP King *2002 Collier portable pamphlet: full text of the bankruptcy code and rules* (2001); Warren & Westbrook n 15 above at 215; Gross n 15 above at 25.

states.[20] Discharge is dealt with in sections 523 and 524, and includes issues in respect of the reaffirmation of a particular debt and whether it can or should be exempted from the discharge. Section 541 defines the property of the estate, and the trustee's avoiding powers are also provided for in chapter 5. Chapter 7 is entitled 'Liquidation' and is the first chapter to provide for a specific form of bankruptcy, previously known as a 'straight' bankruptcy. In a nutshell, the trustee simply collects the debtor's assets, sells them, and distributes the proceeds to creditors.[21] Chapter 7 can be distinguished from a chapter 11 plan of reorganisation, which may keep a business in operation, and from a chapter 13 wage earners' plan, whereby an individual can propose certain periodic payments. Most bankruptcy proceedings in the United States are commenced under chapter 7, and many of the chapter 11 and 13 proceedings end up as chapter 7 proceedings.[22] Read together with sections 523 and 524, section 727 sets out the rules denying a debtor any right to a discharge under certain circumstances.

Chapter 9 makes special provision for the bankruptcy of a municipality and other governmental units.

Chapter 11 is central to reorganisation in business bankruptcies, making provision for 'a plan' for failing businesses which attempt to remain in operation and work out their difficulties.

Chapter 12 was enacted by Congress in 1986 and is a specialised version of chapter 13, modelled exclusively for farmers. Chapter 12 developed because most farmers had too large a debt to be eligible for a chapter 13 relief, while they were often adversely affected by chapter 11 proceedings.[23] Chapter 12 enables a farmer to keep his farm after reorganisation under circumstances where he probably could not keep it under a chapter 11 proceeding.

Chapter 13 is a new development in the Code which provides for the adjustment of debts of an individual with regular income. It is used by most consumers wishing to keep their non-exempt property and try to pay back some part of their debts over time.[24]

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20 Scott & King n 19 above at 434–462; King n 19 s 112–121; Warren & Westbrook n 15 above at 215; JJ White & TR Nimmer *Cases and materials on bankruptcy* (3ed 1996) at 58. Exemptions in other non-bankruptcy federal laws also exist, such as social security payments to the ill or elderly, but these will not be considered any further at this point.

21 White n 20 above at 59. Gross n 15 at 25.

22 *Ibid.* See, generally, Gross n 13 at 25 and further.

23 White n 20 above at 60.

24 Warren & Westbrook n 15 above at 216. For a comprehensive discussion of the impact of BAPCPA on chapter 13 cases, see HE Hildebrand III 'Impact of the Bankruptcy Abuse prevention and Consumer Protection Act of 2005 on chapter 13 Trustees' 2005 *The Am Bankr LJ* 373.

Chapter 15 deals with ancillary and other cross-border bankruptcy. It was inserted by BAPCPA.

The jurisdictional and procedural provisions governing bankruptcy are dealt with in Title 28 of the United States Code, while Title 18 defines and establishes criminal sanctions and offences in bankruptcy.

The paths of personal bankruptcy

It has already been noted that the central concept in personal bankruptcy in the American framework is the discharge. From the above exposition of the structure of the Code, it can be seen that debtors may follow one of two paths to obtain a discharge. The first path is the straight liquidation envisaged in chapter 7 of the Code. In summary, the debtor's assets are handed over to a bankruptcy court, the assets are then sold by the trustee and the proceeds distributed first amongst the debtor's secured creditors. If assets remain, they are distributed pro rata among the unsecured creditors. In practice, these individual debtors filing for bankruptcy under chapter 7, in fact, have no non-exempt assets, leaving no need to conduct a sale and the debtor receives a discharge very quickly.[25]

The second path that the debtor may follow is the proposal of a rehabilitation plan under chapter 13. Here the debtor retains his assets and proposes the repayment of a portion of his debts over a period of three to five years. This is an attractive option for a debtor who has property that he wishes to retain.[26]

The core of personal bankruptcy in the United States therefore lies in three concepts, namely, the straight liquidation, the rehabilitation plan (and the discharge offered under both), and the third, an important concept, exemptions of property. The exempt property of the debtor is not available to creditors. Exemptions are intended to protect enough of the debtor's assets to allow him to recover from his financial woes and to achieve a 'fresh start'. Exemptions have been and still are, the cause of contention between state and federal legislators.[27] As mentioned earlier,[28] Congress simply incorporated exemptions into bankruptcy under the old Bankruptcy Act, thereby allowing different states to provide for their own specific exemptions (opting out). The Code currently allows a debtor to choose between his state exemptions and a set of federal exemptions, unless the debtor's state requires

25 Skeel n 1 above at 5–6. Gross n 15 above at 25 and further.
26 See the discussion below regarding the amendments to the Code by BAPCPA.
27 Skeel n 1 above at 6.
28 See above *The structure of the Bankruptcy Code.*

all debtors to use the state alternative (opting out).[29] Exempt property will be discussed in greater detail below.[30]

Under the Code either a debtor or his creditors may invoke the bankruptcy laws, but BAPCPA has introduced certain limitations or obstacles to the pathways into bankruptcy.[31] In the past most debtors filed for bankruptcy voluntarily as creditors had little incentive to file for an involuntary proceeding as the law was rather generous to debtors. Creditors therefore rather tried to collect their debts outside of bankruptcy.[32] BAPCPA has attempted to alter this situation.

Bankruptcy Abuse Prevention and Consumer Protection Act of 2005

This Act brought about fundamental changes to the bankruptcy law affecting consumers. It was signed by the then President, George Bush, on 20 April 2005, but it generally applies to cases filed on or after 17 October 2005, because most of the BAPCPA amendments take effect only in respect of cases filed 180 days after enactment.[33] With respect to consumer debtors, Congress apparently intended to force debtors to make substantial lifestyle changes in cases where their income exceeded state median income, before they could receive the benefits of bankruptcy.[34] BAPCPA's consumer provisions restrict methods of asset protection and state by state shopping for advantageous exemptions.[35] This has made it difficult to establish domicile for pre-bankruptcy exemption planning unless it is long-term planning, particularly in respect of homestead exemptions.[36] But this Act has been criticised by many. For example, Sommer[37] said the following shortly before its enactment:

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29 The majority of states appear to have opted out. V Countryman 'Bankruptcy and the individual debtor B and a modest proposal to return to the seventeenth century' 1983 *Catholic University Law Revue* 809 at 819; Skeel n 1 above at 7.

30 See the next para below.

31 See the paragraph on BAPCPA below.

32 Skeel n 1 above at 7.

33 USC s 101.

34 See CJ Tabb 'The death of consumer bankruptcy in the United States?' 2001 *Bankruptcy Developments Journal* at 1.

35 LR Ahern III 'Homestead and other exemptions under the Bankruptcy Abuse Prevention and Consumer Protection Act: observations on asset protection after 2005' 2005 *Am Bankr Inst L Rev* 585 at 586; See also Hildebrand III n 24 at 373 at 373. '

36 Ahern III n 35 at 586.

37 HJ Sommer 'Trying to make sense out of nonsense: representing consumers under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005' 2005 *Am Bankr LJ* at 191. See generally also MB Jacoby 'Ripple or revolution? The indeterminacy of statutory bankruptcy reform' 2005 *Am Bankr LJ* 169 at 169; CE Vance 'Nine traps and one slap: attorney liability under the new bankruptcy law' 2005 *Am Bankr LJ* at 283; M Howard 'Exemptions under the 2005 bankruptcy amendments: a tale of opportunity lost' (2005) *Am Bankr LJ* at 397. '

> From its Orwellian title, an example of deceptive advertising if ever there was one, to the last of its 512 pages, the bankruptcy bill recently passed by Congress presents numerous challenges to attorneys who represent consumer debtors. How such terrible legislation came to be passed by Congress is a story of money, political mean-spiritedness, and intellectual dishonesty, but that is a story for another article.

However, this Act came about because of the long-held perception that the integrity of the bankruptcy process in the United States was being tarnished by shrewd and unscrupulous debtors who were exploiting the system.

Policies of American bankruptcy law

General

Essentially, all insolvency law systems involve the opposing positions of debtors and creditors. Problems arise when transactions that the debtors and creditors have entered into with each other fail to result in the intended consequences, leaving the debtor unable to service his debts.[38] Insolvency legislation should balance the needs of all the stakeholders, who include the insolvent debtor, the creditors, insolvency practitioners, the government, and the commercial community in general.[39] On this point Jackson states:[40]

> It is likewise fashionable to see bankruptcy law as embodying substantive goals of its own that need to be 'balanced' with (among others) labor law, with environmental law, or with the rights of secured creditors or other property claimants.

In the United States the traditional theory of insolvency law was the equal treatment of creditors and the rehabilitation of the debtor. The latter is also known as a 'fresh start' policy.[41] Lately, however, different economic and social theories have been formulated to serve as the basis or purpose of an insolvency law system in the United States.[42] These policies then create the basis of the substantive law governing, among other issues, estate assets.[43] American bankruptcy policy, however, stems largely from the ideals of bankruptcy law expressed by Congress, legislative history, and court opinion. Academic debate is often divided in assessing what bankruptcy

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38 TH Jackson *The logic and limits of bankruptcy law* (1986) at 1 (hereafter Jackson). '

39 South African Law Commission *Review of the law of insolvency* Project 63 (2000) Report, Vol 1. Explanatory Memorandum, and vol 2 Draft Bill at 10. See also Jackson n 41 above at 1.

40 Jackson n 38 above at 1. See also, generally, J Ferriell & EJ Janger *Understanding bankruptcy* (2007) at 7 and further.

41 TH Jackson and RE Scott 'On the nature of bankruptcy: an essay on bankruptcy sharing and the creditors' bargain' 1989 *Virginia Law Review* at 155; BA Blum *Bankruptcy and debtor/creditor-examples and explanations* (3 ed 2004) at par 5.1. '

42 Jackson & Scott n 41 above at 155; see also Ferriell n 40 above at 1.

43 Blum n 41 above at 5.5.1.

policy is or ought to be.[44] But the policy espoused by Congress and the courts has been more 'traditionalist' in nature.[45] Thus American bankruptcy policy concerns itself both with a system that efficiently protects creditor's rights under non-bankruptcy law, and with a striving for social goals that account for vulnerable debtors, workers and the community in general.[46]

In general this has resulted in a complex interaction of the policies.[47] A particularly apt example of this has been the introduction of exempt property in the Code in 1978, a tug of war that had to be reconciled and prioritised.[48] Lobby groups further complicated this issue by constantly lobbying Congress in an attempt to influence legislation, or amending legislation, from faithfully achieving the intended policy goals.[49] The perceived policy of bankruptcy law, probably in any system, would therefore rather reflect its ideals and possibly not the realities of bankruptcy law.[50] Also very important to consider is the fact that bankruptcy law does not exist in a vacuum. It exists and clashes with many other legal and socio-political disciplines and problems, thereby being influenced by public policy issues and legal policies of a much broader nature. Thus policies upon which common law rules or other statutes have been founded may have to be weighed up against and reconciled with bankruptcy law.[51]

From the above, it can be deduced that, generally, American bankruptcy policy today is essentially founded on bankruptcy as a remedial tool, the protection of debtors and creditors interests, the equal treatment of creditors, the preservation of the estate, and the policy of a fresh start for the debtor. However, only the policy of the preservation of the estate and the fresh start policy will be considered here.

Preserving the estate

Bankruptcy law must also preserve what is left of the debtor's estate by preventing him/her from further diminishing it. This policy is linked to all the other policies of bankruptcy law. Bankruptcy is meant to be advantageous to creditors not only because it protects their interests *inter se*, but also because it provides otherwise unavailable tools for the preservation

44 *Ibid.*
45 *Ibid.*
46 *Ibid.*
47 *Ibid.*
48 WH Brown 'Political and ethical considerations of exemption limitations: the "opt-out" as child of the first and parent of the second' 1997 *Am Bankr LJ* at 149; WM Engledow 'Cleaning up the pigsty: approaching a consensus on exemption laws' 2000 *Am Bankr LJ* 275 at 276–78; L Ponoroff 'Exemption limitations: a tale of two solutions' 1997 *Am Bankr LJ* at 221.
49 Blum n 41 above at 5.5.1.
50 *Ibid.*
51 *Ibid.*

and possible enhancement of the estate.[52]

However, the preservation of the estate also assists the debtor. In both chapter 7 liquidation cases and chapter 13 rehabilitation cases, the preservation of the estate possibly increases, or at least provides a pool of excluded assets, exempt assets, and assets that the debtor may keep under a reorganisation.[53] These assets are then the foundation upon which the fresh start policy in American bankruptcy is based.[54]

Fresh start

One of the fundamental principles upon which American bankruptcy law rests is the policy of providing the honest debtor with an opportunity to shed his debts thereby allowing him a fresh start.[55] Inextricably linked to the fresh start principle are the policies to preserve the estate, and to exclude and exempt part of the debtor's property from the bankruptcy estate so as to assist him in achieving the fresh start.[56] In the often cited case of *Local Loan Co v Hunt*[57] the court stated that

> 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'.

Various commentators have different ideas regarding the rationale behind the fresh start policy. For example, Jackson approaches it as a form of limited liability of individuals, with the creditors being in a dominant position when transacting with debtors, thus placing the risk of non-payment upon the creditors.[58] This encourages better monitoring of credit granting by creditors.[59] He says the discharge system thus contains a built-in checking system.[60] However, he also states that a discharge should always be available at some cost so as to avoid its abuse in a credit-orientated society. Obtaining a discharge should entail some sacrifice on the debtor's part, such as the

52 *Ibid.*

53 *Ibid.*

54 *Ibid* – preservation of the estate also serves a social purpose where the estate of a business is preserved and that business is rescued, thereby helping employees, customers and the general community. Also in respect of individuals, by allowing the debtor to keep some assets the state is released of social responsibilities towards the debtor and his dependants.

55 NW Waxman *Gilbert law summaries – bankruptcy* (4ed 2001) at 1; Woodard n 8 at 184; Gross n 15 at 91.

56 See the *The chapter 7 and chapter 13 estates* below.

57 292 US 234, 244 (1934).

58 Jackson n 38 above at 229.

59 *Id* at 231.

60 *Ibid.*

forfeiture of assets in favour of creditors, and possible negative consequences regarding credit-worthiness in the future.[61] Gross, however, is of the opinion that the fresh start principle is based on the idea of society's willingness, by way of bankruptcy procedure, to forgive non-paying debtors and thereby allow for their rehabilitation.[62] However, Gross's reasoning is questionable. Perhaps she is losing sight of the fact that society has no other choice than to use bankruptcy as the only possible workable debt collection procedure, bar taking the law into one's own hands, a practice that is perhaps not all that uncommon. It is doubtful whether forgiveness is on the mind of the creditor or society in respect of debt collection. If the rationale were forgiveness, then why go through the laborious bankruptcy procedure at all? Is one forgiving if one continues to question or curtail the debtor's credit-worthiness in the future? The rationale behind the fresh start policy is linked, it appears, rather to the policy of considering bankruptcy as remedial, the aim being to manage the debtor's financial distress in the interest of all the role-players. This, of course, is aside from the idea that the debtor who has a fresh start is less of a burden on society.

Of course, the fresh start policy may also have unfortunate consequences, such as creditors increasing the cost of lending to cover the risk of bankruptcy consequences, while creditors actually carry the burden of the fresh start policy when the exempt assets in fact diminish the debtor's estate.[63] But, it would appear that the fresh start policy, with its advantages and disadvantages, is saved by the over-riding policy in bankruptcy law of finding a suitable balance that protects or satisfies the interests of not only debtors and creditors, but also society in general and the government.

The bankruptcy estate

General

In the United States the filing of a bankruptcy petition by a debtor establishes an estate,[64] a separate legal entity, which holds and controls all assets owned by the debtor.[65] Simultaneously with the creation of the bankruptcy estate, a chapter 7 individual debtor starts accumulating a new estate.[66] If an individual debtor wants to file a single petition together with his spouse, he may file a joint case.[67] For a joint case, debtors must be legally married, as

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61 *Id* at 249.

62 Gross n 15 above at 93.

63 Blum n 41 above at 5.5.1.

64 A case is commenced under section 301, 302, or 303, being a voluntary case, joint cases and an involuntary case respectively. '

65 See s 541(a) '[T]he commencement of a case … creates an estate'; see generally Ferriell n 40 above at 223 and further. See also Dickerson 'From jeans to genes: the evolving nature of property of the estate' 1999 *Bankr Dev J* at 285; Blum n 41 above at 12.1. '

66 Blum n 41 above at 12.1. '

67 S 302(a). See Ferriell n 40 above at 224 and 228.

mere cohabitation does not qualify,[68] and a joint petition may be used only in a voluntary case.[69] The debtors' estates in a joint case may be consolidated by the court. This entails the pooling of their assets and liabilities, particularly if their assets and liabilities are held together.[70] Here the court will consider whether there is a substantial identity between the property and debts, and dealing of financial affairs between the debtor and spouses, and whether consolidation, or the denial thereof, will have harmful consequences.[71]

Section 541 in sub-chapter III of the Code, provides for the property that is *included* in the bankruptcy estate. It is a broad and all-encompassing provision that includes 'all legal and equitable interests of the debtor in property as of the commencement of the case' including 'property, wherever located and by whomever held'.[72] The Code, however, does not *define* what constitutes property, but the courts construe property broadly to encompass everything of value, even if the property, or the debtor's interest in the property is 'novel'.[73]

For the purpose of consumer bankruptcy, the content of the bankruptcy estate may differ, depending on whether it is a chapter 7 estate, or a chapter 13 estate.

The chapter 7 and chapter 13 estates

A chapter 7 estate is comprised of all legal or equitable interests of the debtor in property as of the commencement of the case.[74] This includes the proceeds, product, offspring, rentals, or profits of, or from, property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.[75] Also included is every interest of the debtor and the debtor's spouse in community property as of the commencement of the case that is under the sole, equal, or joint management and control of the debtor.[76]Any interest in property that the trustee recovers

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68 *In re Malone* 50 BR 2 (Bankr ED Mich 1985).

69 *In re Benny* 842 F 2d 1147 (9th Cir 1988).

70 S 302(b); see Waxman n 55 above at par 149.

71 *In re Reider* 31 F 3d 1102 (11th Cir 1994).

72 Section 541(a)(1). See, generally, Gross n 15 above at 44.

73 See Dickerson n 64 above at 293. It must be noted that determining the bankruptcy estate may be affected by the interplay between federal bankruptcy law (the Code), and non-bankruptcy law. *Eg*, entitlements granted to a party under non-bankruptcy law may exclude an asset from an estate, or the Code may disallow such exclusion, depending on the correct and relevant analysis. However, this aspect will not be considered in further detail See in this respect Jackson n 38 above at 93.

74 Section 541(a)(6). See Dickerson n 65 above at 285 and further.

75 *Ibid.*

76 Section 541(a)(2). Community property is defined under applicable state law.

under the trustee's avoidance power[77] is also included.[78] Also included is any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date by bequest, device or inheritance, or as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree, or as a beneficiary of a life insurance policy or of a death benefit plan.[79]

All the property included in a chapter 7 estate under section 541 is also part of a chapter 13 estate.[80] Here too, bankruptcy filing creates a bankruptcy estate as a legal entity distinct from the debtor. However, chapter 13 also includes all property of the kind specified in section 541 that the debtor acquires after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapters 7, 11, or 12 of this title, whichever occurs first.[81] Here rehabilitation is aimed at the preservation of the estate for the debtor. Its liquidation is not the goal as in the chapter 7 estate, and the break between the debtor's bankruptcy estate and his fresh start estate is not as final.[82] Earnings from services performed by the debtor after the commencement of the case, but before the case is closed, dismissed, or converted to a case under chapters 7, 11, or 12 of this title, whichever occurs first, are therefore also included in the chapter 13 estate.[83] The debtor is able to re-acquire pre-petition property from the estate by committing post-petition acquisitions, for example, future earnings, to the payment of claims.[84] Thus, the debtor in chapter 13 effectively uses property or post-petition income that would have been excluded or exempt from a chapter 7 estate, and thereby saves property that would have been liquidated under chapter 7.[85] Pending the confirmation of a chapter 13 plan, the debtor can usually keep and use estate property. Once the plan has been confirmed, the debtor is re-vested with all property that has not been disposed of in the plan.[86] Should the plan ultimately succeed, this becomes the property of the debtor's new estate. But if the plan fails and is converted to chapter 7, the property is surrendered to the trustee for liquidation.[87]

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77 See ss 329(b) , 363(n) , 543 , 550 , 553 or 723. '
78 Section 541(a)(3).
79 Section 541(a)(5).
80 Chapters 11, 12 and 13 are referred to as 'rehabilitation' chapters, whereas chapter 7 is entitled 'liquidation'. Section 541 applies to all the rehabilitation chapters as well.
81 Section 1306(a)(1).
82 Blum n 41 above at 12.1. '
83 Section 1306(a)(2).
84 Blum n 39 above at 12.1. '
85 *Ibid.*
86 Section 1306(b).
87 Blum n 41 above at 12.1.

Conclusion

The Bankruptcy Act of 1898 was the first comprehensive formulation of American bankruptcy legislation, which remained in force until the promulgation of the Bankruptcy Code in 1978. The 1898 Act provided for a broad definition of property of the bankruptcy estate and extensive reform in favour of debtors regarding exempt property.[88] The courts also construed this legislation to favour certain exemptions for debtors, all with the intention of removing unnecessary obstacles in the way of the debtor's fresh start.[89]

The Bankruptcy Code of 1978 was the first thorough *revision* of bankruptcy law since the 1898 Act, generally continuing the policy of a debtor-friendly approach to bankruptcy. It substantially expanded, among other things, the rights of the consumer debtor, making chapter 13 thereof a more desirable option for debtors, and expanding the number and variety of assets exempt from the creditors' reach. Because the incorporation of state exemption laws into the federal bankruptcy case had always been criticised,[90] it was eventually amended by including federal exemptions in the new Code. South African insolvency law also has its more substantial foundations in various Ordinances dating back essentially to the nineteenth century. However, that legislation provided a minimum of attention to the idea of excluded property in insolvent estates. Only recently, being one hundred years on, has a serious attempt been made to reform the law of insolvency in South Africa. But this attempt pays little attention to the provisions regarding assets in insolvent estates, and less so to excluded assets and the policy of a fresh start for the debtor.[91]

After the enactment of the Code, there was a sharp increase in the number of business and bankruptcy filings, particularly under chapter 7. Whether the increase in filing has resulted from the generosity of the Code, or from the change in society's notions about the morality of avoiding one's debts, or from the wider availability of lawyers, is uncertain and much disputed.[92] 'On this point, the rationale behind the American bankruptcy system is presently debated, and will continue to be debated in the future, possibly resulting in fundamental policy changes in American bankruptcy legislation. Whether it should be considered a relief for the honest debtor or the forgiving of the debtor, is perhaps unimportant. What is important in the American law is the

88 Countryman n 29 809 above at 817.

89 Dickerson n 69 above at 292–293.

90 See, *eg*, LB Bartell 'The peripatetic debtor: choice of law and choice of exemptions 2006 *Emory Bankruptcy Developments Journal* at 405 note 28 and WT Vukowich 'The bankruptcy commission's proposals regarding bankrupts' exemption rights' 1975 *Cal L Rev* 1439 at 1441–1446.

91 See generally the *Review of the law of insolvency* (Project 63) of the South African Law Commission (as it then was) in the above text.

92 White n 20 above at 56.

fresh start policy. Be that as it may, several amendments to the Code inevitably followed, perhaps the most substantial being the Bankruptcy Abuse Prevention Consumer Protection Act of 2005. However, none of these amendments has drastically changed the provisions existing basically since the 1898 Act, regarding estate property and excluded or exempt property. Although access to bankruptcy has been made more laborious, once the debtor has gained access to the system, he gains access to certain property to assist him in making a fresh start and this is a fundamental policy in American bankruptcy law that has remained constant.