UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NORTH CAROLINA

In Re:	Case No. C-B-89-31301
	Chapter 13
WILLIE HUGHES, JR., and ELLA LOUISE HUGHES,	
Debtors.	JUDGMENT ENTERED ON JAN 26 1990

ORDER SUSTAINING CHAPTER 13 TRUSTEE'S OBJECTION TO CONFIRMATION

This matter is before the court on the objection by the Chapter 13 Trustee to confirmation of the debtor's Chapter 13 plan and the debtor's response to that objection. The court has concluded that the Trustee's objection should be sustained based on the fact that the debtors' plan, as now proposed, would distribute less to unsecured creditors than those same creditors would receive if this case had been brought under Chapter 7, thereby failing to satisfy the provisions of 11 U.S.C. § 1325(a)(4).

Facts and Contentions

Willie Hughes, Jr., and Ella L. Hughes, the debtors in this proceeding, filed a joint Chapter 13 bankruptcy petition on October 4, 1989. The schedules accompanying the debtors' petition listed $2,384.32 of secured debt and $9,372.90 of unsecured debt outstanding. The debtors proposed to pay these debts by making plan payments of $101.00 per month for thirty-six months. These payments were to be distributed in a manner which would pay in full all secured claims and all claims to which the debtors were jointly liable. However, the remaining unsecured creditors

--were to be paid only a small percentage of their claims. The debtors' schedules also indicated that they possessed $51,000.00 of equity in their residence, owned as a tenancy by the entirety. By completing their Chapter 13 plan as proposed, the debtors sought to protect this equity.

At the hearing, the Trustee objected to the confirmation of the debtors' plan. The Trustee asserted that such a low payout to non-joint, unsecured creditors was unwarranted in light of the debtors' substantial equity in their residence. Expert testimony was offered which indicated that had the debtors filed their petition under Chapter 7, their residence would have been sold, and all creditors, including those possessing non-joint, unsecured claims, would have been paid in full. The Trustee argued that because such a Chapter 7 distribution would provide the non-joint, unsecured creditors with more than the payments under the debtors' proposed Chapter 13 plan, the plan would be improper under the provisions of § 1325(a)(4).

The debtors argued in favor of confirmation. It was conceded that all of the debtors' secured and joint debts had to be paid in full. The debtors maintained the view, however, that the non-joint, unsecured claims could be paid a lesser amount. A joint bankruptcy filing, the debtors asserted, did not create a joint estate. Instead, both individuals continued to possess separate estates, except for the purpose of administrative convenience. Therefore, the residential entireties property could not be used to satisfy the individual creditors of either debtor.

The debtors further argued that because non-joint creditors would not be allowed to reach entireties property under state law, those creditors should also not be allowed to reach entireties property in a Chapter 7 bankruptcy, even if it is sold to pay joint creditors. Simply put, the fact that two debtors file a joint bankruptcy petition should not work to expand the rights a creditor possesses under state law.

Discussion

Section 1325(a)(4) of the Bankruptcy Code provides:

> [T]he court shall confirm a plan if -
> * * * *
> (4) the value, as of the effective date of the plan, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under Chapter 7 of this title on such date;....

This requirement is mandatory. See H.R. Rep. No. 95-595, 95th Cong., 1st Sess. 430, reprinted in Appendix 2, Collier on Bankruptcy (15th ed. 1989). The court has concluded that the confirmation requirement of § 1325(a)(4) is not met in the present case because a Chapter 7 distribution would result in a higher payment to unsecured creditors.

The debtors correctly point out that the filing of a joint bankruptcy petition does not automatically create a joint estate. In re Ageton, 14 B.R. 833 (Bankr. App. Panel 9th Cir. 1981). Joint filing serves primarily an administrative purpose, and both debtors continue to maintain two separate bankruptcy estates. Id.; H.R. Rep. No. 95-595, 95th Cong., 1st Sess. 321 reprinted in Appendix 2, Collier on Bankruptcy (15th ed. 1989). However, Code

§ 302(b) and Bankruptcy Rule 1015 allow substantive consolidation of debtors' estates, in the discretion of the court. Such consolidation creates one pool of assets for the benefit of the creditors of both debtors. Courts have recognized an exception to consolidation where it would prejudice the rights of creditors of either debtor. In re Birch, 72 B.R. 103 (Bkrtcy. N.H. 1987).

Such prejudice does not exist in this case. Had the debtors filed their joint petition in Chapter 7, the expert testimony offered by the Trustee indicated that the debtors' estates would have been consolidated and the residence sold. In Matter of Steury, 94 B.R. 553 (Bkrtcy. N.D. Ind. 1989), the court allowed a similar result. The debtors in that case contested the consolidation of their separate Chapter 7 petitions attempting to preserve substantial equity in their residence owned as tenants by the entirety. The court rejected the debtors' contentions of prejudice and allowed consolidation. The consolidation was limited, however, to allow for payment of only the debtors' joint liabilities because these debts alone exceeded the equity in the debtors' home. In the present case there would be no need to limit consolidation in this manner. The total of the debtors' joint liabilities is far less than the $51,000.00 of equity in their residence. Even after all joint debts are paid, there would be substantial funds remaining with which to pay the non-joint claims. Thus, anything less than a one hundred percent payout to all creditors in Chapter 13 would prevent confirmation in this case.

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Finally, the court rejects the debtors' argument that allowing non-joint creditors to reach entireties property in bankruptcy results in an expansion of the rights those creditors would have under state law. Under North Carolina law, the debtors' joint creditors could force a sale of the residence and dissolve the tenancy by the entirety to satisfy their claims. The entireties estate does not extend to the surplus funds of this sale. McClure v. McClure, 64 N.C. App. 318, 307 S.E.2d 212 (1983). The surplus funds are viewed as property of tenants in common, and they are then subject to the claims of any creditor. United States v. Mauney, 642 F.Supp. 1097 (W.D.N.C. 1986); In re Foreclosure of Deed of Trust Recorded in Book 911, Page 512, Catawba County Registry, 303 N.C. 514, 279 S.E.2d 566 (1981). Therefore, even under state law, the debtors' non-joint creditors could reach the entireties property, and the Bankruptcy Code affords those creditors no greater rights.

Conclusion

The debtors cannot propose a Chapter 13 plan which will meet the requirements § 1325(a)(4) unless they make full payment to all creditors. Had this been a Chapter 7 case, consolidation would appear to have been warranted, and one pool of assets would have been created. This would have resulted in the sale of the residential property and payment of all creditors in full. Such a result is very similar to the distribution of proceeds which

would occur under state law following a forced sale by the debtors' joint creditors. Thus, the bankruptcy process cannot be viewed as providing any greater rights to non-joint creditors than they would possess under state law.

It is therefore **ORDERED** that:

1. The Chapter 13 Trustee's objection to confirmation is sustained; and

2. The debtors are given 30 days from the date of this Order to modify their plan, convert the case, or take other appropriate action. If no such action has been taken at the end of 30 days, this case will be dismissed.

This the 26th day of January, 1990.

George R. Hodges
United States Bankruptcy Judge