

TITLE 11 - BANKRUPTCY

CHAPTER 7 - LIQUIDATION

SUBCHAPTER II - COLLECTION, LIQUIDATION, AND DISTRIBUTION OF THE ESTATE

§ 726. Distribution of property of the estate

- (a) Except as provided in section 510 of this title, property of the estate shall be distributed—
- (1) first, in payment of claims of the kind specified in, and in the order specified in, section 507 of this title, proof of which is timely filed under section 501 of this title or tardily filed on or before the earlier of—
 - (A) the date that is 10 days after the mailing to creditors of the summary of the trustee’s final report; or
 - (B) the date on which the trustee commences final distribution under this section;
 - (2) second, in payment of any allowed unsecured claim, other than a claim of a kind specified in paragraph (1), (3), or (4) of this subsection, proof of which is—
 - (A) timely filed under section 501 (a) of this title;
 - (B) timely filed under section 501 (b) or 501 (c) of this title; or
 - (C) tardily filed under section 501 (a) of this title, if—
 - (i) the creditor that holds such claim did not have notice or actual knowledge of the case in time for timely filing of a proof of such claim under section 501 (a) of this title; and
 - (ii) proof of such claim is filed in time to permit payment of such claim;
 - (3) third, in payment of any allowed unsecured claim proof of which is tardily filed under section 501 (a) of this title, other than a claim of the kind specified in paragraph (2)(C) of this subsection;
 - (4) fourth, in payment of any allowed claim, whether secured or unsecured, for any fine, penalty, or forfeiture, or for multiple, exemplary, or punitive damages, arising before the earlier of the order for relief or the appointment of a trustee, to the extent that such fine, penalty, forfeiture, or damages are not compensation for actual pecuniary loss suffered by the holder of such claim;
 - (5) fifth, in payment of interest at the legal rate from the date of the filing of the petition, on any claim paid under paragraph (1), (2), (3), or (4) of this subsection; and
 - (6) sixth, to the debtor.
- (b) Payment on claims of a kind specified in paragraph (1), (2), (3), (4), (5), (6), (7), or (8) of section 507 (a) of this title, or in paragraph (2), (3), (4), or (5) of subsection (a) of this section, shall be made pro rata among claims of the kind specified in each such particular paragraph, except that in a case that has been converted to this chapter under section 1112, 1208, or 1307 of this title, a claim allowed under section 503 (b) of this title incurred under this chapter after such conversion has priority over a claim allowed under section 503 (b) of this title incurred under any other chapter of this title or under this chapter before such conversion and over any expenses of a custodian superseded under section 543 of this title.
- (c) Notwithstanding subsections (a) and (b) of this section, if there is property of the kind specified in section 541 (a)(2) of this title, or proceeds of such property, in the estate, such property or proceeds shall be segregated from other property of the estate, and such property or proceeds and other property of the estate shall be distributed as follows:
- (1) Claims allowed under section 503 of this title shall be paid either from property of the kind specified in section 541 (a)(2) of this title, or from other property of the estate, as the interest of justice requires.
 - (2) Allowed claims, other than claims allowed under section 503 of this title, shall be paid in the order specified in subsection (a) of this section, and, with respect to claims of a kind specified in a particular paragraph of section 507 of this title or subsection (a) of this section, in the following order and manner:

(A) First, community claims against the debtor or the debtor's spouse shall be paid from property of the kind specified in section 541 (a)(2) of this title, except to the extent that such property is solely liable for debts of the debtor.

(B) Second, to the extent that community claims against the debtor are not paid under subparagraph (A) of this paragraph, such community claims shall be paid from property of the kind specified in section 541 (a)(2) of this title that is solely liable for debts of the debtor.

(C) Third, to the extent that all claims against the debtor including community claims against the debtor are not paid under subparagraph (A) or (B) of this paragraph such claims shall be paid from property of the estate other than property of the kind specified in section 541 (a)(2) of this title.

(D) Fourth, to the extent that community claims against the debtor or the debtor's spouse are not paid under subparagraph (A), (B), or (C) of this paragraph, such claims shall be paid from all remaining property of the estate.

(Pub. L. 95–598, Nov. 6, 1978, 92 Stat. 2608; Pub. L. 98–353, title III, § 479, July 10, 1984, 98 Stat. 381; Pub. L. 99–554, title II, §§ 257(r), 283 (s), Oct. 27, 1986, 100 Stat. 3115, 3118; Pub. L. 103–394, title II, § 213(b), title III, § 304(h)(5), title V, § 501(d)(24), Oct. 22, 1994, 108 Stat. 4126, 4134, 4146; Pub. L. 109–8, title VII, § 713, title XII, § 1215, Apr. 20, 2005, 119 Stat. 128, 195.)

Historical and Revision Notes

legislative statements

Section 726 (a)(4) adopts a provision contained in the Senate amendment subordinating prepetition penalties and penalties arising in the involuntary gap period to the extent the penalties are not compensation for actual pecuniary laws.

The House amendment deletes a provision following section 726(a)(6) of the Senate amendment providing that the term “claim” includes interest due owed before the date of the filing of the petition as unnecessary since a right to payment for interest due is a right to payment which is within the definition of “claim” in section 101(4) of the House amendment.

senate report no. 95–989

This section is the general distribution section for liquidation cases. It dictates the order in which distribution of property of the estate, which has usually been reduced to money by the trustee under the requirements of section 704 (1).

First, property is distributed among priority claimants, as determined by section 507, and in the order prescribed by section 507. Second, distribution is to general unsecured creditors. This class excludes priority creditors and the two classes of subordinated creditors specified below. The provision is written to permit distribution to creditors that tardily file claims if their tardiness was due to lack of notice or knowledge of the case. Though it is in the interest of the estate to encourage timely filing, when tardy filing is not the result of a failure to act by the creditor, the normal subordination penalty should not apply. Third distribution is to general unsecured creditors who tardily file. Fourth distribution is to holders of fine, penalty, forfeiture, or multiple, punitive, or exemplary damage claims. More of these claims are disallowed entirely under present law. They are simply subordinated here.

Paragraph (4) provides that punitive penalties, including prepetition tax penalties, are subordinated to the payment of all other classes of claims, except claims for interest accruing during the case. In effect, these penalties are payable out of the estate's assets only if and to the extent that a surplus of assets would otherwise remain at the close of the case for distribution back to the debtor.

Paragraph (5) provides that postpetition interest on prepetition claims is also to be paid to the creditor in a subordinated position. Like prepetition penalties, such interest will be paid from the estate only if and to the extent that a surplus of assets would otherwise remain for return to the debtor at the close of the case.

This section also specifies that interest accrued on all claims (including priority and nonpriority tax claims) which accrued before the date of the filing of the title 11 petition is to be paid in the same order of distribution of the estate's assets as the principal amount of the related claims.

Any surplus is paid to the debtor under paragraph (6).

NB: This unofficial compilation of the U.S. Code is current as of Jan. 5, 2009 (see <http://www.law.cornell.edu/uscode/uscpri.html>).

Subsection (b) follows current law. It specifies that claims within a particular class are to be paid pro rata. This provision will apply, of course, only when there are inadequate funds to pay the holders of claims of a particular class in full. The exception found in the section, which also follows current law, specifies that liquidation administrative expenses are to be paid ahead of reorganization administrative expenses if the case has been converted from a reorganization case to a liquidation case, or from an individual repayment plan case to a liquidation case.

Subsection (c) governs distributions in cases in which there is community property and other property of the estate. The section requires the two kinds of property to be segregated. The distribution is as follows: First, administrative expenses are to be paid, as the court determines on any reasonable equitable basis, from both kinds of property. The court will divide administrative expenses according to such factors as the amount of each kind of property in the estate, the cost of preservation and liquidation of each kind of property, and whether any particular administrative expenses are attributable to one kind of property or the other. Second, claims are to be paid as provided under subsection (a) (the normal liquidation case distribution rules) in the following order and manner: First, community claims against the debtor or the debtor's spouse are paid from community property, except such as is liable solely for the debts of the debtor.

Second, community claims against the debtor, to the extent not paid under the first provision, are paid from community property that is solely liable for the debts of the debtor. Third, community claims, to the extent they remain unpaid, and all other claims against the debtor, are paid from noncommunity property. Fourth, if any community claims against the debtor or the debtor's spouse remain unpaid, they are paid from whatever property remains in the estate. This would occur if community claims against the debtor's spouse are large in amount and most of the estate's property is property solely liable, under nonbankruptcy law, for debts of the debtor.

The marshalling rules in this section apply only to property of the estate. However, they will provide a guide to the courts in the interpretation of proposed 11 U.S.C. 725, relating to distribution of collateral, in cases in which there is community property. If a secured creditor has a lien on both community and noncommunity property, the marshalling rules here—by analogy would dictate that the creditor be satisfied first out of community property, and then out of separate property.

Amendments

2005—Subsec. (a)(1). Pub. L. 109–8, § 713, substituted “on or before the earlier of—” and subpars. (A) and (B) for “before the date on which the trustee commences distribution under this section;”.

Subsec. (b). Pub. L. 109–8, § 1215, struck out “1009,” before “1112”.

1994—Subsec. (a)(1). Pub. L. 103–394, § 213(b), inserted before semicolon at end “, proof of which is timely filed under section 501 of this title or tardily filed before the date on which the trustee commences distribution under this section”.

Subsec. (b). Pub. L. 103–394, §§ 304(h)(5), 501 (d)(24), substituted “, (7), or (8)” for “or (7)” and “chapter under section 1009, 1112,” for “chapter under section 1112”.

1986—Subsec. (b). Pub. L. 99–554, § 283(s), inserted reference to par. (7) of section 507 (a) of this title.

Pub. L. 99–554, § 257(r), inserted reference to section 1208 of this title.

1984—Subsec. (b). Pub. L. 98–353, § 479(a), substituted “each such particular paragraph” for “a particular paragraph”, “a claim allowed under section 503 (b) of this title” for “administrative expenses” in two places, and “has priority over” for “have priority over”.

Subsec. (c)(1). Pub. L. 98–353, § 479(b)(1), substituted “Claims allowed under section 503 of this title” for “Administrative expenses”.

Subsec. (c)(2). Pub. L. 98–353, § 479(b)(2), substituted “Allowed claims, other than claims allowed under section 503 of this title,” for “Claims other than for administrative expenses”.

Effective Date of 2005 Amendment

Amendment by Pub. L. 109–8 effective 180 days after Apr. 20, 2005, and not applicable with respect to cases commenced under this title before such effective date, except as otherwise provided, see section 1501 of Pub. L. 109–8, set out as a note under section 101 of this title.

Effective Date of 1994 Amendment

Amendment by Pub. L. 103–394 effective Oct. 22, 1994, and not applicable with respect to cases commenced under this title before Oct. 22, 1994, see section 702 of Pub. L. 103–394, set out as a note under section 101 of this title.

NB: This unofficial compilation of the U.S. Code is current as of Jan. 5, 2009 (see <http://www.law.cornell.edu/uscode/uscpri.html>).

Effective Date of 1986 Amendment

Amendment by section 257 of Pub. L. 99-554 effective 30 days after Oct. 27, 1986, but not applicable to cases commenced under this title before that date, see section 302(a), (c)(1) of Pub. L. 99-554, set out as a note under section 581 of Title 28, Judiciary and Judicial Procedure.

Amendment by section 283 of Pub. L. 99-554 effective 30 days after Oct. 27, 1986, see section 302(a) of Pub. L. 99-554.

Effective Date of 1984 Amendment

Amendment by Pub. L. 98-353 effective with respect to cases filed 90 days after July 10, 1984, see section 552(a) of Pub. L. 98-353, set out as a note under section 101 of this title.