Behind the Bench

NCBJ In collaboration with American Bankruptcy Institute

Chapter 13 Plan Issues:

The Good, The Bad, and The Ugly

January 23, 2024

Cases and Statutes

In re Elassal, 654 B.R. 434 (Bankr. E.D. Mich. 2023)

In re Marsh, 647 B.R. 725 (Bankr. W.D. Mo. 2023)

In re Adams, No 21-80425, 2023 WL 7320858 (Bankr. M.D.N.C. Nov. 3, 2023)

Bassel v. Durand-Day, 2023 WL 5320775 (N.D.Tex.)

In re Eisenberger, 654 B.R. 762 (Bankr. W.D.N.Y. October 23, 2023)

In re Materne, 640 B.R. 781 (Bankr. D. Mass. 2022)

Bledsoe v. Cook, 70 F.4th 746 (4th Cir. June 14, 2023)

In re Moreno, 22-10886 (Bankr. D.N.M. Dec. 7, 2023)

Cal. Civ. Proc. Code § 703.140(c):

In a case under Title 11 of the United States Code, the value of the property claimed as exempt and the debtor's exemptions provided by this chapter with respect to such property shall be determined as of the date the bankruptcy petition is filed. In a case where the debtor's equity in a residence is less than or equal to the amount of the debtor's allowed homestead exemption as of the date the bankruptcy petition is filed, any appreciation in the value of the debtor's interest in the property during the pendency of the case is exempt.

654 B.R. 434
United States Bankruptcy Court,
E.D. Michigan, Southern Division.

IN RE: Wendy ELASSAL, Debtor.

Case Number 21-42801
|
Signed August 28, 2023

Synopsis

Background: Chapter 13 debtor sought court approval to use proceeds from post-confirmation sale of home, which had significantly appreciated in value post-confirmation, to purchase a new residence for cash, while making her promised dividend to unsecured creditors over the remainder of her plan. Trustee objected and filed proposed plan modification whereby debtor would keep what remained of proceeds after unsecured claimants received full payment.

Holdings: The Bankruptcy Court, Mark A. Randon, J., held that:

[1] debtor's prepetition home vested in her at confirmation;

[2] proceeds from post-confirmation sale of home were property of debtor and did not "refill" bankruptcy estate; and

[3] proceeds from post-confirmation sale of home were not "disposable income," of kind that debtor could be required to devote to payments under plan.

Objection overruled; plan modification denied.

Procedural Posture(s): Other.

West Headnotes (6)

[1] Statutes Superfluousness

Canon against surplusage is strongest when an interpretation would render superfluous another part of the same statutory scheme.

[2] Bankruptcy After-acquired property; proceeds; wages and earnings

Bankruptcy Property of estate

Under "estate replenishment" approach for determining property of the estate in a Chapter 13 case after confirmation, debtor's prepetition home vested in her at confirmation, and estate continued to exist and would "refill" with any property acquired post-confirmation. 11 U.S.C.A. §§ 541, 1306, 1327.

2 Cases that cite this headnote

[3] Bankruptcy After-acquired property; proceeds; wages and earnings

Bankruptcy Property of estate

Proceeds from post-confirmation sale of Chapter 13 debtor's prepetition home, which had significantly appreciated in value post-confirmation, were property of debtor and did not "refill" bankruptcy estate under "estate replenishment" approach for determining property of the estate in a Chapter 13 case after confirmation; sale proceeds could not be separated from the underlying real estate. 11 U.S.C.A. §§ 541, 1306, 1327.

2 Cases that cite this headnote

[4] Bankruptcy Claims and assets; propriety and feasibility in general

Proceeds from post-confirmation sale of Chapter 13 debtor's prepetition home, which had significantly appreciated in value post-confirmation, that debtor proposed to use solely to purchase a new residence were not "disposable income," of kind that debtor could be required to devote to payments under plan; sale generated a lump sum rather than a stream of payments, and the sale proceeds were not anticipated. 11 U.S.C.A. § 1325(b).

1 Case that cites this headnote

[5] Bankruptcy Claims and assets; propriety and feasibility in general

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

"Disposable income," of kind that Chapter 13 debtor could be required to devote to payments under plan, does not include prepetition property or its proceeds. 11 U.S.C.A. § 1325(b).

[6] **Bankruptcy** Claims and assets; propriety and feasibility in general

Test for determining "disposable income," of kind that Chapter 13 debtor could be required to devote to payments under plan, is whether the asset in question is an anticipated stream of payments; if it is a stream of payments, the payments must be included in projected income, but if the asset is not a stream of payments, it is not included. 11 U.S.C.A. § 1325(b).

Attorneys and Law Firms

***435** Heather D. McGivern, Charissa Potts, Freedom Law PC, Harper Woods, MI, for Debtor.

OPINION AND ORDER OVERRULING TRUSTEE'S OBJECTION AND DENYING PLAN MODIFICATION

Mark A. Randon, United States Bankruptcy Judge

I. INTRODUCTION

Housing prices fluctuate over time, as do the relative financial risks and benefits of home ownership. Ideally, home values appreciate. Yet history cautions, there are no guarantees. Reliably predicting the real estate market's ebbs and flows ranges from difficult to a fool's errand.

In 2021, Wendy Elassal ("Debtor") filed chapter 13 bankruptcy, committing three years of disposable income to keep her assets—including a $250,000 home—with $228,000 of liens. Although unsecured creditors would have received nothing in a hypothetical Chapter 7 liquidation (Debtor could have exempted the remaining home equity), Debtor's Second Amended Plan proposed to pay a minimum of $1,277.16 towards $93,805.83 in general unsecured claims. This plan was confirmed without objection.

Who could have predicted, in less than two years, Debtor's home would sell for $435,000, netting $177,695.13 in proceeds after full payment of the liens? Not the Trustee, who consented to confirmation; nor the unsecured creditors, who could reasonably have decided something was better than nothing at the time. Likely not even Debtor, who agreed to the modest payment to unsecured creditors, whether her home appreciated or *depreciated*.

Through either her uncanny real estate market expertise or good fortune, Debtor's decision to file and remain in Chapter 13 has "paid off."[1] But for whom? Debtor wants to keep the money: Having now paid her secured creditors, she seeks Court approval to use all of the sale proceeds to buy a new home—for cash—while making her promised dividend to unsecured creditors over the remainder of her plan. The Trustee's objection and proposed plan modification urge a different outcome: Debtor may only keep what remains *after* unsecured claimants receive full payment—anything ***436** less would be inconsistent with the code and evidence Debtor's lack of good faith. The Court disagrees. Superior discernment or luck is neither gamesmanship nor an absence of good faith. Because the Court determines: (1) the estate replenishment theory best harmonizes 11 U.S.C. §§ 1306 and 1327, Debtor's home vested in her at confirmation; (2) the sale proceeds, derived from post-confirmation appreciation of Debtor's pre-petition real property, cannot be untethered from the real property itself, and do not refill the estate; and (3) the sale proceeds, particularly when escrowed for direct rollover into a new home purchase, are not "disposable income"—Debtor may use the sale proceeds to buy a new residence. The Trustee's objection is **OVERRULED**, and her plan modification is **DENIED**.

II. JURISDICTION

The Court has jurisdiction over this matter under 28 U.S.C. §§ 1334(b) and 157(a) and (b), and is authorized, by standing reference from the United States District Court, to resolve the contested matter as a core proceeding under 28 U.S.C. § 157(b)(2)(A) and (O).

III. PROCEDURAL AND FACTUAL BACKGROUND

Debtor filed Chapter 13 bankruptcy on March 31, 2021. A Judgment of Divorce provided Debtor's former spouse an interest in the marital home in Van Buren Township, Michigan (the "Van Buren Property"). Debtor listed her interest on Schedule A/B and valued the Van Buren Property at $250,000, which was unchallenged. She also disclosed three outstanding liens in favor of: (1) Independent Mortgage in the amount of $180,000; (2) Debtor's divorce attorney

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

for $3,597.40; and (3) her former spouse in the amount of $48,000. Debtor listed the remaining $22,000 equity as subject to her federal homestead exemption.

The Judgment of Divorce awarded Debtor the Van Buren Property with three conditions: (1) Debtor's former spouse would make 24 monthly mortgage payments in lieu of child and spousal support; (2) Debtor would sell or refinance the Van Buren Property by December 31, 2022, to pay the former spouse's equity position; and (3) Debtor would be responsible for any mortgage payments after January 1, 2023.

On July 31, 2021, the Court entered an Order Confirming Debtor's Plan. On February 2, 2023, after the deadline to sell or refinance, Debtor filed a motion to sell the Van Buren Property. The Trustee objected to the proposed sale to Debtor's friend for $275,000; Debtor filed an amended motion to sell the Van Buren Property. This time, she sought approval to sell it for $435,000 through an arms length transaction and to use all of the proceeds from the sale, $173,655.93 (the "Sale Proceeds"), to purchase a new residence. The Trustee objected. She argued Debtor was first required to use $94,000 of the Sale Proceeds to pay her unsecured creditors in full. Debtor and Trustee stipulated to the entry of an order approving the sale, requiring Debtor's attorney to retain the Sale Proceeds in attorney's client trust ("IOLTA") account until further order of the Court. On May 8, 2023, Debtor filed a motion to use the Sale Proceeds to purchase a new residence. The Trustee objected and filed a plan modification, again proposing Debtor use $94,000 of the Sale Proceeds to pay unsecured creditors in full.

After hearing the motions, the Court ordered supplemental briefing. On July 21, 2023, Debtor filed her Post-Hearing Response Brief ("Debtor's Brief"), and the Trustee filed her Supplemental Brief in Support of Trustee's Proposed Post-Confirmation Plan Modification ("Trustee's Brief" and collectively, the "Briefs").

*437 IV. APPLICABLE LAW AND ANALYSIS

The Court recognizes that the Briefs cite to competing persuasive–but not controlling–authority to support their respective positions. The Court first adopts a common position that appears in both Briefs—implementation of the Estate Replenishment approach to harmonize 11 U.S.C. §§ 1306 and 1327. *See In re Marsh*, 647 B.R. 725 (Bankr. W.D. Mo. 2023) (relied upon in Trustee's Brief); *see also In re Larzelere*, 633 B.R. 677 (Bankr. D. N.J. 2021) (relied upon in Debtor's Brief). The Court then leans into Debtor's argument, finding the post-confirmation Sale Proceeds belong to Debtor. *See e.g., McDonald v. Burgie (In re Burgie)*, 239 B.R. 406 (B.A.P. 9th Cir. 1999); *In re Euler*, 251 B.R. 740 (Bankr. M.D. Fla. 2000); *In re Larzelere*, 633 B.R. 677 (Bankr. D. N.J. 2021); *In re Mobley*, No. 11-49079, 2011 WL 6812551 (Bankr. E.D. Mich. Dec. 1, 2011); *In re Ash'shadi*, No. 04-55924, 2005 WL 1105039 (Bankr. E.D. Mich. May 6, 2005).

A. Reconciliation of 11 U.S.C. §§ 1306 and 1327 is Best Accomplished Though the Estate Replenishment Approach

This Court is not the first to grapple with fashioning an approach which harmonizes the competing statutory directives of sections 1306 and 1327. *See e.g., In re Tarby*, 2012 WL 1390201 (Bankr. D. N.J. Apr. 20, 2012); *In re Scholl*, 605 B.R. 163 (Bankr. S.D. Ohio 2019); *In re Baker*, 620 B.R. 655 (Bankr. D. Colo. 2020); *In re Clouse*, 446 B.R. 690 (Bankr. E.D. Pa. 2010).[2] This Court finds the Estate Replenishment approach best reconciles these code sections.

Sections 541 and 1306 primarily govern property of the chapter 13 bankruptcy estate. 11 U.S.C. §§ 541 and 1306. Section 541 defines estate property as "all legal or equitable interests of the debtor in property as of the commencement of the case" and "[p]roceeds, product, offspring, rents, or profits of or from property of the estate[.]" 11 U.S.C. § 541(a)(1), (6). Section 1306 incorporates section 541 and captures additional property in chapter 13 cases:

> (a) Property of the estate includes, in addition to the property specified in section 541 of this title—
>
> (1) all property of the kind specified in such section that the debtor acquires after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7, 11, or 12 of this title, whichever occurs first; and
>
> *438 (2) 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 chapter 7, 11, or 12 of this title, whichever occurs first.

Read together, sections 541 and 1306 appear to encompass all property of the estate that a debtor owns as of the petition date and any property acquired during the pendency of a chapter 13 case before closure or conversion. In contrast to sections

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

541 and 1306, section 1327 vests all estate property in the debtor at confirmation and creates the crux of the issue here.

Section 1327, in pertinent part, states:

> (b) Except as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor.
>
> (c) Except as otherwise provided in the plan or in the order confirming the plan, the property vesting in the debtor under subsection (b) of this section is free and clear of any claim or interest of any creditor provided for by the plan. [3]

But given these competing code sections, what if any, property remains part of the bankruptcy estate post-confirmation? According to section 1327, "confirmation of a plan vests *all of the property of the estate in the debtor*" and "property vesting in the debtor under [section 1327] is free and clear of any claim or interest of any creditor provided for by the plan." 11 U.S.C. § 1327(b), (c) (emphasis added). However, section 1306 seemingly stands in direct conflict with section 1327 posing "estate property includes ... property of the kind specified in section 541 [and] *all property of the kind specified in such section that the debtor acquires after the commencement of the case* but before the case is closed, dismissed, or converted to a case under chapter 7, 11, or 12 of this title, whichever occurs first." 11 U.S.C. § 1306(a) (emphasis added).

[1] A reading of the plain language of section 1306(a) appears to render all property until "the case is closed, dismissed, or converted," property of the estate. On the other hand, a reading of the plain language of section 1327(b) appears to vest all property with the debtor post-confirmation. Moreover, section 1327(c) provides that this property is free and clear of any claims. Harmonizing the inharmonious is a tall order. And courts must do so in light of a Supreme Court's recent reminder that " '[t]he canon against surplusage is strongest when an interpretation would render superfluous another part of the same statutory scheme.' " *City of Chicago v. Fulton*, —— U.S. ——, 141 S. Ct. 585, 591, 208 L.Ed.2d 384 (2021) (citing *Yates v. United States*, 574 U.S. 528, 543, 135 S.Ct. 1074, 191 L.Ed.2d 64 (2015)). Faced with this task, "several courts [ ] suggest [sections 1306 and 1327] ... may even be 'impossible to reconcile." ' *In re Scholl*, 605 B.R. at 173 (citing *In re Rangel*, 233 B.R. 191, 194 (Bankr. D. Mass. 1999); *see also In re Barbosa*, 236 B.R. 540, 545 (Bankr. D. Mass. 1999)). The Court believes reconciliation, while difficult, is not impossible, and will add another opinion to the growing discord.

Courts have utilized at least five different theories or "approaches" in their attempts to reconcile sections 1306 and ***439** 1327: the Estate Termination approach; [4] the Estate Transformation approach; [5] the Conditional Vesting approach; [6] the Estate Preservation approach; [7] and the Estate Replenishment approach. [8] *In re Marsh*, 647 B.R. at 730–34; *In re Baker*, 620 B.R. at 663–64 (listing all five approaches).

Many courts have determined—and this Court agrees—that both the Estate Termination and Estate Preservation approaches "render another part of the statutory scheme superfluous." *City of Chicago*, 141 S. Ct. at 591. The Estate Termination approach draws a sharp line at confirmation, vesting all property with debtor, and the "estate ceases to exist." *In re Baker*, 620 B.R. at 663 (citing KEITH M. LUNDIN, LUNDIN ON CHAPTER 13 § 120.3, ¶ [9] (citations omitted); *see also In re Rangel*, 233 B.R. 191 (Bankr. D. Mass. 1999). This approach allows section 1327 to swallow up section 1306. The Estate Preservation approach proposes the opposite–section 1306 engulfing 1327.

> The vesting of property in the debtor under § 1327(b) does not remove any property from the chapter 13 estate, whether acquired before or after confirmation; property remains in the estate until the case is closed, dismissed, or converted. The debtor's rights and responsibilities with respect to property of the estate may change somewhat at confirmation, but the existence and composition of the estate are not disturbed by § 1327(b).
>
> *In re Baker*, 620 B.R. at 663–64 (citing LUNDIN at § 120.3¶ [9]).

Because the Estate Termination and Preservation approaches effectively render the competing code section superfluous, this Court adopts a moderate approach, recently favored by other courts faced with this issue–the Estate Replenishment approach. *See e.g., City of Chicago v. Fisher (In re Fisher)*, 203 B.R. 958, 962–63 (N.D. Ill. 1997); *Fritz Fire Protect. Co.*

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

v. Wei-Fung Chang (In re Chang), 438 B.R. 77, 83 (Bankr. M.D. Pa. 2010); *see also In re Marsh*, 647 B.R. 725 (Bankr. W.D. Mo. 2023); *In re Larzelere*, 633 B.R. 677 (Bankr. D. N.J. 2021; *In re Willard*, 2023 WL 2601769 (S.D.N.Y. Mar. 22, 2023)).

The Estate Replenishment approach provides "[a]t confirmation, all property of the estate becomes property of the debtor; the Chapter 13 estate continues to exist and 'refills' with property defined in § 1306 that is acquired by the debtor after confirmation, ***440** without regard to whether that property is necessary to performance of the plan." *In re Baker*, 620 B.R. at 663 (citing LUNDIN).

[2] These facts are undisputed. Debtor listed the Van Buren Property on her Schedule A/B at $250,000. Her plan was confirmed on July 31, 2021; following confirmation, the Van Buren Property significantly appreciated in value—selling for $435,000. With the Trustee's consent, the Court approved the sale, Debtor sold the Van Buren Property, and the Sale Proceeds are being held in the Debtor's attorney's IOLTA account. Application of the Estate Replenishment approach vests the Van Buren Property in the Debtor at confirmation.

The Court finds the Van Buren Property was property of the estate until it confirmed Debtor's Plan. Following confirmation, the Van Buren Property vested in Debtor. The estate continues to exist and will "refill" with any property acquired post-confirmation. The Court now pivots to whether the Sale Proceeds are newly acquired post-confirmation property that refill the estate.

B. Post-Confirmation Sale Proceeds Cannot Be Separated from the Debtor's Pre-Confirmation Property from Which They Were Derived

Sale Proceeds must fall into either one of two categories to be considered post-confirmation estate property: (1) under the Estate Replenishment approach, the Sale Proceeds refill the bankruptcy estate post-confirmation because they are newly acquired property of the Debtor; or (2) the Sale Proceeds are disposable income encompassed by 11 U.S.C. § 1325. Neither categorization is persuasive.

1. The Sale Proceeds do not refill the estate

Several courts have addressed whether proceeds from the sale of prepetition property derived from post-confirmation appreciation are newly acquired property of a debtor. Unsurprisingly, courts have come down on both sides of the issue. The Court adopts what it believes is the better-reasoned line of cases and holds the Sale Proceeds cannot be untethered from the underlying Van Buren Property and therefore, are not a newly acquired asset of Debtor.

Courts have determined chapter 7 bankruptcy estates capture appreciation of prepetition property as property of the estate, despite proceeds being attributable to post-petition appreciation. *See e.g., Coslow v. Reisz,* 811 Fed. App'x 980 (6th Cir. 2020); *In re Lents*, 644 B.R. 479 (Bankr. D. S.C. 2022). The Court finds it unnecessary to look to Code provisions governing chapter 7 estate property when Debtor received the protections of the chapter 13 bargain. The Court looks to sections 1306, 1335, and 1327, and the chapter 13 case law relying on these sections, to guide its decision.

Even when a chapter 13 case is converted to a chapter 7, courts have found appreciation of prepetition property is property of the estate. *See In re Adams,* 641 B.R. 147 (Bankr. W.D. Mich. 2022).[9] The Trustee's Brief relies on the *Adams* holding to suggest a chapter 13 debtor's post-confirmation ***441** sale proceeds from prepetition real estate are property of the bankruptcy estate. *See id.* But the *Adams* holding does not extend to the circumstances here because, unlike in *Adams*, Debtor did not convert to a chapter 7.

In *Adams*, the debtors converted their chapter 13 case to a chapter 7 and attempted to retain post-confirmation appreciation of real property, post-conversion. *In re Adams*, 641 B.R. 147 (Bankr. W.D. Mich. 2022). The court never contemplated sections 1306 and 1327, but relied mainly on 11 U.S.C. § 348(f) to determine whether property belonged to the debtor or to the estate. *Id.* Section 348—Effect of Conversion—is not applicable here as Debtor did not convert to a chapter 7. However, a chapter 13 debtor who converts to a 7, does lose the benefit of the bargain given to a chapter 13 debtor. The *Adams* court drove this point home, stating "chapter 13 still presents the best avenue for debtors to retain property in bankruptcy, and the unqualified right to dismiss their chapter 13 proceedings protects them from any adverse consequences of conversion to chapter 7." *In re Adams*, 641 B.R. at 156. Debtor retains the benefit of her bargain struck at confirmation.

Moreover, a debtor's chapter 13 protections are distinguished from that of a debtor's chapter 7 protections. The Supreme Court framed this distinction clearly in *Hamilton v. Lanning*:

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

> Chapter 13 of the Bankruptcy Code provides bankruptcy protection to "individual[s] with regular income" whose debts fall within statutory limits. 11 U.S.C. §§ 101(30), 109(e). Unlike debtors who file under Chapter 7 and must liquidate their nonexempt assets in order to pay creditors, see §§ 704(a)(1), 726, Chapter 13 debtors *are permitted to keep their property*, but they must agree to a court-approved plan under which they pay creditors out of their future income.

Hamilton v. Lanning, 560 U.S. 505, 508, 130 S.Ct. 2464, 177 L.Ed.2d 23 (2010) (emphasis added).

The Supreme Court in *Bullard v. Blue Hills Bank*, clarified its stance with respect to section 1327's vesting language stating "[s]ubject to certain exceptions, confirmation 'vests all of the property of the [bankruptcy] estate in the debtor' and renders that property 'free and clear of any claim or interest of any creditor provided for by the plan." ' 575 U.S. 496, 502, 135 S.Ct. 1686, 191 L.Ed.2d 621 (2015) (citing 11 U.S.C. § 1327(b), (c)).

Many decisions, nationwide, align with this Court's finding. *See e.g., In re Euler*, 251 B.R. 740, 747–48 (Bankr. M.D. Fla. 2000) ("As stated by Judge Jennemann in *In re Meeks,* 237 B.R. 856, 861 [(Bankr. M.D.Fla. 1999)], 'A debtor who decides to retain collateral at a confirmation hearing is entitled to any later appreciation in value but also must suffer any resulting depreciation or loss.' " (citations omitted)); *In re Burgie*, 239 B.R. at 410 ("The chapter 13 deal permits a debtor to retain all prepetition property, including earnings, assets, money in the bank and real estate."); *In re Mobley*, 2011 WL 6812551, at *2 (" 'Under a chapter 13 plan, the debtor is entitled to keep all of the debtor's prepetition property' and includes prepetition proceeds..." (quoting *In re Burgie*, 239 B.R. at 410–11)); *In re Ash'shadi*, 2005 WL 1105039, at *3 ("As explained above, the proceeds from the sale of a prepetition asset do not become property of the chapter 13 estate...").

The court in *Burgie* laid the framework for a line of cases, which have followed the *Burgie* court's analysis of chapter 13's protections—including two cases decided in the Eastern District of Michigan. *See e.g.,* ***442** *In re Burgie*, 239 B.R. 406 (B.A.P. 9th Cir. 1999); *In re Euler*, 251 B.R. 740 (Bankr. M.D. Fla. 2000); *Black v. Leavitt (In re Black)*, 609 B.R. 518 (B.A.P. 9th Cir. 2019); *Willard v. Preuss (In re Willard)*, No. 21 Civ 10220, 2023 WL 2601769 (S.D.N.Y. March 22, 2023); *see also In re Ash'shadi*, No. 04-55924, 2005 WL 1105039 (Bankr. E.D. Mich. May 6, 2005) and *In re Mobley*, No. 11-49079, 2011 WL 6812551 (Bankr. E.D. Mich. Dec. 1, 2011).

In *Burgie*, chapter 13 debtors sold their prepetition homestead five days post-confirmation. *In re Burgie*, 239 B.R. at 408. The debtors proposed to use the $63,000 in sale proceeds to purchase a new residence. *Id.* The trustee did not object to debtors' original proposal to dedicate *all* of the post-confirmation sale proceeds to the purchase of a new residence. *Id.* The trustee only objected to debtors' subsequent proposal to use $43,000 of the sale proceeds as a down payment on a new residence, and retain $20,000 "to support themselves and help complete their plan." *Id.* The trustee moved to modify the debtors' plan to require any sale proceeds *not* utilized in the purchase of a new residence to be turned over to the trustee to "provide 100% distribution" to unsecured creditors. *Id.*

The Bankruptcy Appellate Panel for the Ninth Circuit affirmed the bankruptcy court's decision denying the trustee's motion. *Id.* at 412. The court held "debtors cannot be compelled to use the proceeds from the sale of prepetition real estate to pay creditors under a confirmed chapter 13 plan." *Id.* at 410. And despite debtors retaining $20,000 of the sale proceeds, the court further stated "[w]hile a debtor may voluntarily use such proceeds to make payments to creditors under a chapter 13 plan, a debtor cannot be compelled to use the proceeds for this purpose." *Id.* at 409. The Court finds this reasoning persuasive, but does not expand its finding to the extent of the *Burgie* court.

The circumstances here are well within the scope of what the *Burgie* court saw fit for a chapter 13 debtor's post-confirmation sale proceeds. Debtor sold her homestead not five days, but over 20 months after confirmation.[10] Furthermore, the trustee in *Burgie* did not object to the debtors' use of the sale proceeds to purchase a new residence. Only when debtors proposed to retain $20,000 of the proceeds did the trustee object. Therefore, the Court limits its holding to Debtor's specific request: she may use the Sale Proceeds solely to purchase a new residence.[11] The Sale Proceeds must remain in the IOLTA account until transferred directly

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

to close on a new residence. And Debtor must close on said residence *on or before December 31, 2023*—unless the Court extends this deadline, for cause.

Widening the scope on chapter 13 protections, the Southern District Court of New York recently addressed the sale proceeds issue on appeal from the Bankruptcy Court stating " '[a]n examination of the basic structure of chapter 13 makes it clear that the debtors cannot be compelled to' turn over their prepetition property, whether post-confirmation as in *Burgie*, or pre-confirmation, as here." *In re Willard*, 2023 WL 2601769, at *3 (citing *In re Burgie*, 239 B.R. at 410). The chapter 13 debtor in *Willard* sought to retain sale proceeds of his prepetition property in the amount of $354,333.77, and the trustee objected. *In re Willard*, 2023 WL 2601769. ***443** The sale of the debtor's property occurred pre-confirmation and the trustee argued that the sale proceeds were property of the estate, not the debtor's property. *Id.* The district court disagreed with the trustee and Bankruptcy Court, finding the bankruptcy court had abused its discretion in requiring the debtor to turn over the sale proceeds to the trustee. *Id.* at *3.

[3] The court explained that "[c]ompelling a debtor to submit a pre-petition asset to the trustee, and thereby exposing such pre-petition asset to the creditors, runs counter to the congressional design evidenced by Chapter 13's language and structure." *In re Willard*, 2023 WL 2601769, at *3. The Debtor's Sale Proceeds here, arise from a post-confirmation sale and are derived from post-confirmation appreciation. If a debtor cannot be compelled to turnover pre-confirmation sale proceeds derived from pre-confirmation appreciation because "chapter 13 makes it clear that debtors cannot be compelled to turn over their prepetition property," then certainly the protections of chapter 13 further fortified with the post-confirmation protections of section 1327 shield the Debtor's Sale Proceeds here.

The Sale Proceeds are the Debtor's property pursuant to 1327, cannot be separated from the underlying real estate, and according to the Supreme Court "[c]hapter 13 debtors are permitted to keep their property." *Hamilton*, 560 U.S. at 508, 130 S.Ct. 2464. Not only does Debtor receive the benefit the bargain struck with her creditors—without the benefit of foresight—but she also receives the fortified protections of section 1327 because the appreciation generating the Sale Proceeds arose post-confirmation. Consequently, the Sale Proceeds will not refill the bankruptcy estate.

2. The Sale Proceeds are not Disposable Income within the Purview of 11 U.S.C. § 1325

[4] Alternatively, the Sale Proceeds could be categorized as disposable income. If the Sale Proceeds were considered disposable income under 11 U.S.C. § 1325(b), Debtor could be compelled to contribute them to the plan. Because the Court finds the Sale Proceeds are not disposable income, Debtor cannot be compelled to turn them over to her creditors. The Trustee's proposed plan modification is denied as moot.

Section 1325(b)(1) states:

> If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the court may not approve the plan unless, as of the effective date of the plan—
>
> (A) the value of the property to be distributed under the plan on account of such claim is not less than the amount of such claim; or
>
> (B) the plan provides that all of the debtor's projected disposable income to be received in the three-year period beginning on the date that the first payment is due under the plan will be applied to make payments under the plan.

Section 1325(b)(2) defines "disposable income" for the purpose of section 1325(b)(1) and provides in pertinent part:

> For the purposes of this subsection, "disposable income" means current monthly income which is received by the debtor and which is not reasonably necessary to be expended—
>
> (A) for the maintenance or support of the debtor or a dependent of the debtor....

11 U.S.C. § 1325(b)(2).

The Trustee suggests that Debtor must propose a post-confirmation plan modification as required by 11 U.S.C. § 1329, because ***444** the Sale Proceeds are disposable income not accounted for in her plan. Further, the Trustee asserts that because Debtor failed to propose a modification, the Trustee, pursuant to 11 U.S.C. § 1329(b)(1), proposed a post-confirmation plan modification to account for the Sale Proceeds. *Id.* The Court disagrees that (1) Debtor is required to propose a modification; and (2) that—under the particular circumstances here—the Trustee may propose a modification,

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

as the Sale Proceeds are not disposable income. Debtor cannot be compelled to turn over any property that vested in her at confirmation.

a. Trustee's Reliance on Sixth Circuit Cases Misses the Mark

The Trustee presents two Sixth Circuit Court of Appeals cases in attempt to drive home her argument that the Sale Proceeds are disposable income. These decisions would be binding if on point, however, their holdings do not apply here. *In re Freeman* involved a post-confirmation plan modification where the court required the debtor to turn over an unexpected surplus in a tax refund derived from prepetition wages. *Freeman v. Schulman (In re Freeman)*, 86 F.3d 478 (6th Cir. 1996). The tax refunds were for prepetition wages, and the Trustee purports that the *Freeman* decision reaches the circumstances in here—but it does not.

The debtor in *Freeman*, upon the realization her tax refund would be in excess of what the plan projected, attempted to exempt the excess under state law. *In re Freeman*, 86 F.3d at 479. In addition, the debtor "specifically identified that tax refunds should go to the plan and made no argument that the funds were needed for 'maintenance and support' of the debtor or her dependents." *Id.* at 481. The court held that the tax refund qualified as disposable income under section 1325. *Id.* However, the court also stated that "[s]ituations may arise where a debtor did not specifically list tax refunds for inclusion in the plan and those situations would need to be examined on a case-by-case basis to decide whether a tax refund arising from pre-petition income qualified as 'projected disposable income." ' *Id.*

Debtor neither seeks to exempt the Sale Proceeds under state law nor purports use of projected proceeds from the sale of the Van Buren Property for "maintenance and support" of herself and her children. In fact, at confirmation, the projected sale of the Van Buren Property would have yielded nothing to unsecured creditors after paying secured creditors and Debtor's exemption. And although the Court does not need to look to *Freeman*, it does agree with the recognition that circumstances require "a case-by-case" analysis to determine what constitutes disposable income.

The Trustee also cited *In re Harchar*, which relied on *Freeman* to reach its decision also surrounding tax refunds. *Harchar v. United States (In re Harchar)*, 694 F.3d 639 (6th Cir. 2012). There, the Sixth Circuit held that the IRS was permitted to seek modification of debtor's plan to compel turnover of a post-confirmation tax refund for prepetition wages. *See id.* Appreciation of prepetition real estate that arose post-confirmation, generated the Sale Proceeds here —not prepetition wages. Real property sale proceeds are categorically different than tax refunds. While this Court agrees with the holdings in both *Freeman* and *Harchar*, neither applies under the facts of this case.

b. Anticipated Stream of Payments

[5] **[6]** Instead of relying on *Freeman* and *Harchar*, this Court adopts the position that "disposable income does not include prepetition property or its proceeds." *In re Burgie*, 239 B.R. at 410. The test in *Burgie* is "whether the asset in question is an anticipated stream of payments. ***445** If it is a stream of payments, the payments must be included in projected income. If the asset is not a stream of payments, it is not included." *Id.* (internal citations omitted).

The court goes on to distinguish a debtor's primary residence from income:

> The sale of a capital asset does not create "disposable income" pursuant to § 1325. Disposable income under § 1325 is postpetition income received by the debtor that is not reasonably necessary for the maintenance or support of the debtor or a dependant of the debtor. *See* § 1325(b)(2). A debtor's prepetition homestead is a capital asset, not postpetition income.

Id.

The court further states "[t]he proceeds of the sale of a debtors real estate in a chapter 13 case never become disposable income for the purposes of chapter 13." *Id.* at 409. The sale of a "capital asset" or a debtor's primary residence generates only a lump-sum payment; it is not an anticipated stream of payments. Although Debtor here planned from the outset to sell her property, not only would the sale generate a lump sum rather than a stream of payments, but the Sale Proceeds were certainly not anticipated. Again, the projected sale—based

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

on the liquidation analysis—was expected to generate only $22,000 in proceeds. Therefore, the Sale Proceeds are not in the anticipated stream of payments for the "maintenance and support" of Debtor's family.

Moreover, as discussed above, the debtors in *Burgie* were not only allowed to use their sale proceeds as a down payment on a new residence, but were permitted to keep $20,000 "to support themselves." *In re Burgie*, 239 B.R. at 408. Despite the debtors actually realizing some of the sale proceeds rather than rolling over all them into a new residence, the court stated "a debtor's homestead is a capital asset" and "[t]he sale of a capital asset does not create disposable income pursuant to § 1325." *Id.* at 410. Debtor proposes to use the Sale Proceeds, in their entirety, to purchase a new residence. The Debtor does not realize any income as defined in section 1325, but is merely rolling over the Sale Proceeds directly into a new (replacement) homestead. The Court holds that the Sale Proceeds are not disposable income insofar they are used solely to purchase Debtor's new homestead. The Court does not make a determination as to the fate of any excess Sale Proceeds above and beyond the new-residence purchase price.

The Court also acknowledges, as the Trustee points out, that the facts of *Mobley* and *Ash'shadi* are different from those here. However, the Court looks to cases in this district not for factual identity but for its application of the stream of income test in a chapter 13 case. Both *Mobley* and *Ash'shadi* apply the stream of income test in a chapter 13 case, and this Court does the same. *See In re Mobley*, 2011 WL 6812551, at *2 ("Chapter 13 contemplates making available an ongoing stream of regularly anticipated income out of which plan payments are to be calculated and made."); *see also In re Ash'shadi*, 2005 WL 1105039, at *3 ("The cases cited by the Trustee in his brief do not control the disposition of the instant case because they all involve a stream of income, or a payment which replaces income, rather than the post-confirmation sale of a pre-petition asset. Specifically, *In re Freeman,* 86 F.3d 478 (6th Cir.1996) involved a post-petition tax refund related to pre-petition income."). The *Ash'shadi* court offered the same argument this Court presented above distinguishing *Freeman*: post-petition tax refunds derived from prepetition income are drastically different from proceeds from the sale of a chapter 13 debtor's ***446** primary residence. *See id.* The Court finds that the Sale Proceeds are not disposable income.

C. The Trustee's Proposed Post-Confirmation Plan Modification

The Court does not reach this issue as Debtor cannot be compelled to turn over the Sale Proceeds to the be distributed to general unsecured creditors. The Plan Modification is denied as moot.

V. CONCLUSION

More than 20 years ago, the Sixth Circuit determined it would be an "unlikely congressional intent" to give Chapter 13 debtors–post-confirmation—"the option to shift the burden of depreciation to a secured creditor by reclassifying the claim and surrendering the collateral when the debtor no longer has any use for the devalued asset." *Chrysler Fin. Corp. v. Nolan (In re Nolan)*, 232 F.3d 528, 533 (6th Cir. 2000). In other words, Chapter 13 debtors assume the risk of depreciation in their revested assets. It stands to reason they should also enjoy the benefit of any post-confirmation appreciation of revested property when sold.

The Court finds the Estate Replenishment approach best reconciles the disparities between 11 U.S.C.§§ 1306 and 1327, and that—at confirmation—all property of Debtor's chapter 13 bankruptcy estate vested in her. The bankruptcy estate continues to exist and can be refilled with a debtor's newly acquired post-confirmation property.

The Sale Proceeds are not newly acquired property as they cannot be untethered from the underlying Van Buren Property. The appreciation of the Van Buren Property occurred post-confirmation, which vested with the Debtor at confirmation. *See* 11 U.S.C. § 1327. Thus, the Debtor "cannot be compelled to turn over prepetition property." Furthermore, the Sale Proceeds are not disposable income as they are not in the anticipated steam of payments. Accordingly, Debtor may use all of the Sale Proceeds to purchase a new residence *on or before December 31, 2023*, unless the Court extends this deadline, for cause. The Trustee's Objection is **OVERRULED**, and her Plan Modification is **DENIED** as moot.

IT IS ORDERED.

All Citations

654 B.R. 434

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

Footnotes

1 Many chapter 13 cases end unsuccessfully: without a discharge, debtors face the resumption of accumulated interest on their debts, which has compounded during their bankruptcies and, having paid a fee to their attorneys and trustees, often find themselves in worse financial shape than before they filed. *See* *Harris v. Viegelahn*, 575 U.S. 510, 514, 135 S. Ct. 1829, 191 L.Ed.2d 783 (citing Porter, *The Pretend Solution: An Empirical Study of Bankruptcy Outcomes*, 90 TEXAS L. REV., 103, 107–11 (2011)).

2 *In re Larzelere*, 633 B.R. at 681-82 (Bankr. D. N.J. 2021) ("The Circuit Courts of Appeals that have addressed the issue are not in agreement. *See* *In re Jones*, 420 B.R. 506, 515 (B.A.P. 9th Cir. 2009) *aff'd on other grounds*, 657 F.3d 921 (9th Cir. 2011) (following estate termination approach); *Telfair v. First Union Mortg. Corp.*, 216 F.3d 1333, 1339-40 (11th Cir. 2000) (estate transformation); *In re Barbosa*, 236 B.R. 540, 550 (Bankr. D. Mass. 1999) *aff'd sub nom*, *Barbosa v. Solomon*, 243 B.R. 562 (D. Mass. 2000) *aff'd*, 235 F.3d 31 (1st Cir. 2000) (following estate replenishment approach); *In re Talbot*, 124 F.3d 1201, 1208 (10th Cir. 1997) (stating without discussion that house revested in debtors at confirmation pursuant to section 1327(b)); *Black v. United States. Postal Serv. (In re Heath)*, 115 F.3d 521, 524 (7th Cir. 1997) (estate transformation). *See also* *In re Goldston,* 627 B.R. 841, 864 (Bankr. D.S.C. 2021) (stating that 'The Fourth Circuit has expressly avoided reconciling the interplay between §§ 1306(a) and 1327(b).'); *Sec. Bank of Marshalltown v. Neiman*, 1 F.3d 687, 690 (8th Cir. 1993) (holding that estate exists after confirmation even if it holds no property")).

3 Under section 1327(b), the Plan or Order Confirming the Plan could have included a provision excluding any property appreciation from revesting in Debtor. *See e.g.,* *In re Euler*, 251 B.R. 740, 747 (Bankr. M.D. Fla 2000).

4 *In re Baker*, 620 B.R. 655, 663 (Bankr. D. Colo. 2020) ("At confirmation, the estate ceases to exist and all property of the estate, whether acquired before or after confirmation, becomes property of the debtor.").

5 *Id.* ("At confirmation, all property of the estate becomes property of the debtor except property essential to the debtor's performance of the plan; the Chapter 13 estate continues to exist, but it contains only property necessary to performance of the plan, whether acquired before or after confirmation.").

6 *Id.* at 664 ("At confirmation, vesting gives the debtor an immediate and fixed right to use estate property, but that right is not final until the debtor completes the plan and obtains a discharge.").

7 *Id.* at 663–64 ("The vesting of property in the debtor under § 1327(b) does not remove any property from the chapter 13 estate, whether acquired before or after confirmation; property remains in the estate until the case is closed, dismissed, or converted. The debtor's rights and responsibilities with respect to property of the estate may change somewhat at confirmation, but the existence and composition of the estate are not disturbed by § 1327(b).").

8 *Id.* at 663 ("At confirmation, all property of the estate becomes property of the debtor; the Chapter 13 estate continues to exist and 'refills' with property defined in § 1306 that is acquired by the debtor after confirmation, without regard to whether that property is necessary to performance of the plan.").

9 The *Adams* court relied on the Sixth Circuit's reasoning in *Coslow v. Reisz*, where a chapter 7 debtor brought an adversary proceeding to compel the trustee to abandon his residential property. The debtor in *Coslow* filed under chapter 7, and the Sixth Circuit's reasoning as to property of the chapter 7 estate is not binding when resolving estate property issues in a chapter 13 case. *See* *Coslow v. Reisz,* 811 Fed. App'x 980 (6th Cir. 2020).

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

10 The Court entered an Order Confirming Plan on July 31, 2021 [Docket # 35] and the Order Approving Sale of Debtor's Real Property was entered on March 30, 2023 [Docket # 49].

11 If the cost of the Debtor's new residence is less than the value of the Sale Proceeds, the fate of the excess Sale Proceeds can be addressed by the Trustee at that time. The Court does not contemplate the possibility herein.

End of Document

© 2024 Thomson Reuters. No claim to original U.S. Government Works.

647 B.R. 725
United States Bankruptcy Court, W.D. Missouri.

IN RE: Christopher Charles MARSH
and Nicole Diane Marsh, Debtors.

Case No. 18-42471
|
Signed January 17, 2023

Synopsis

Background: Chapter 13 debtors moved to retain proceeds from post-confirmation sale of their residence.

Holdings: The Bankruptcy Court, Brian T. Fenimore, Chief Judge, held that:

[1] property of bankruptcy estate that vested in debtors at confirmation lost its status as property of estate;

[2] on issue of first impression, proceeds from post-confirmation sale of debtors' residence were property of estate;

[3] statute governing contents of Chapter 13 plan did not exclude proceeds from sale of debtors' residence from replenished estate; and

[4] debtors had to clarify nature and effect of their proposed modification before bankruptcy court could rule on debtors' motion to retain those proceeds.

Ordered accordingly.

Procedural Posture(s): Other.

West Headnotes (17)

[1] **Bankruptcy** Property of estate

Chapter 13 debtors, as movants, bore burden of proof on motion to retain proceeds from post-confirmation sale of their residence. 11 U.S.C.A. §§ 541, 1306, 1327.

[2] **Bankruptcy** Creation of estate; time

Bankruptcy After-acquired property; proceeds; wages and earnings

Property of the Chapter 13 bankruptcy estate includes all property the debtor (1) owns on the petition date and (2) acquires while the Chapter 13 case is pending. 11 U.S.C.A. §§ 541, 1306.

2 Cases that cite this headnote

[3] **Bankruptcy** Property of estate

Under the "estate replenishment approach," pre-confirmation property of the estate becomes property of the debtor at confirmation, but post-confirmation property becomes property of the estate, i.e., "replenishes" the estate. 11 U.S.C.A. §§ 1306, 1327.

2 Cases that cite this headnote

[4] **Bankruptcy** Property of estate

Estate replenishment approach for determining the scope of a Chapter 13 debtor's entitlement to retain post-confirmation property includes in the estate, at least temporarily, all property debtor acquires after petition date but before case is closed, dismissed, or converted, but it honors the vesting of property free and clear of creditors' claims; by making a clear demarcation between pre-confirmation property, which vests in the debtor, and post-confirmation property, which becomes property of the estate, the estate replenishment approach more predictably differentiates between property of the debtor and property of the estate. 11 U.S.C.A. §§ 1306, 1327.

4 Cases that cite this headnote

[5] **Bankruptcy** Property of estate

Under estate replenishment approach, absent contrary provisions in plan or confirmation order, property debtor acquires before confirmation first becomes property of estate, then vests in debtor at confirmation. 11 U.S.C.A. §§ 1306, 1327.

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

1 Case that cites this headnote

[6] **Bankruptcy** Property of estate

Under the estate replenishment approach for determining the scope of a Chapter 13 debtor's entitlement to retain post-confirmation property, all property that the debtor acquires after confirmation and before the case is closed, dismissed, or converted becomes property of the replenished bankruptcy estate. 11 U.S.C.A. §§ 541, 1306, 1327.

1 Case that cites this headnote

[7] **Bankruptcy** Property of estate

Property of Chapter 13 estate that vested in debtors at confirmation lost its status as property of estate. 11 U.S.C.A. §§ 541, 1306, 1327.

[8] **Bankruptcy** After-acquired property; proceeds; wages and earnings

Unlike appreciation, proceeds in form of cash or cash equivalents are entirely separate from underlying property after property is sold, with attributes and uses distinct from property sold, and therefore the Bankruptcy Code recognizes treats proceeds separately from the property that generates them. 11 U.S.C.A. § 541(a)(6).

[9] **Bankruptcy** After-acquired property; proceeds; wages and earnings

Proceeds from vested property may not be captured as property of the Chapter 13 bankruptcy estate, since vested property is no longer property of the estate. 11 U.S.C.A. § 541(a)(6).

1 Case that cites this headnote

[10] **Bankruptcy** Property of estate

Proceeds from post-confirmation sale of debtors' residence were distinct property "of a kind," i.e., from pre-sale unrealized appreciation in residence, that debtors "acquired" after confirmation and before end of their Chapter 13 case, and consequently proceeds were property of bankruptcy estate under estate replenishment approach for determining scope of debtor's entitlement to retain post-confirmation property. 11 U.S.C.A. §§ 541, 1306(a)(1), 1327.

[11] **Bankruptcy** Property of estate

Statute governing contents of Chapter 13 plan did not exclude proceeds from post-confirmation sale of debtors' residence from replenished estate, under estate replenishment approach for determining scope of debtor's entitlement to retain post-confirmation property, since debtors were not seeking initial confirmation and neither trustee nor holder of allowed secured claim had objected to confirmation. 11 U.S.C.A. §§ 1322, 1325.

1 Case that cites this headnote

[12] **Bankruptcy** Time for completion; extension or modification

Period of time to which debtors committed to make payments under Chapter 13 plan did not apply to plan modifications even if debtors' motion to retain proceeds from post-confirmation sale of residence could be construed as proposed plan modification. 11 U.S.C.A. § 1325(b).

[13] **Bankruptcy** Time for completion; extension or modification

The applicable payment commitment period is a temporal requirement and not a monetary requirement, and so the 36-month applicable commitment period that applies to below-median Chapter 13 debtors acts solely to set the minimum term of a Chapter 13 plan that below-median debtors may be compelled to propose; if a below-median debtor elects to propose a longer term than three years, and the court for cause approves such longer term, the requirements for payment of disposable income in years four and five of the plan remain the same as those in

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

the first three years of the plan. 11 U.S.C.A. § 1325(b)(1).

[14] **Bankruptcy** Time for completion; extension or modification

Chapter 13 debtors sought to modify their confirmed plan without filing modified plan or otherwise specifying terms of their proposed modification through post-confirmation sale of their residence and proposal to retain proceeds from that sale, requiring debtors to clarify nature and effect of their proposed modification before bankruptcy court could rule on debtors' motion to retain those proceeds, since confirmed plan required ongoing payments on their mortgage but sale contravened terms of their confirmed plan. 11 U.S.C.A. § 1329.

[15] **Bankruptcy** After-acquired property; proceeds; wages and earnings

Bankruptcy Time for completion; extension or modification

Debtors could retain portion of proceeds from sale of their residence under modified Chapter 13 plan, although proceeds were property of estate. 11 U.S.C.A. § 1329.

[16] **Bankruptcy** Time for completion; extension or modification

Bankruptcy statute governing plan modification does not necessarily require that debtors pay value of all postconfirmation assets to estate. 11 U.S.C.A. § 1329.

[17] **Bankruptcy** Time for completion; extension or modification

Whether debtors' proposed modification of Chapter 13 bankruptcy plan through sale of their residence satisfied prerequisites for modification, such as by providing for submission of future income as necessary to execute plan and being proposed in good faith, was mixed question of law and fact. 11 U.S.C.A. §§ 1322(a), 1323(c), 1325(a), 1329.

Attorneys and Law Firms

***727** Joseph C. Jeppson, VI, Jeppson Law Office, LLC, Gladstone, MO, for Debtors Christopher Charles Marsh, Nicole Diane Marsh.

MEMORANDUM OPINION AND ORDER

Brian T. Fenimore, United States Chief Bankruptcy Judge

The question before the court is straightforward. If, after the court confirms their chapter 13 plan, debtors sell property they owned on the petition date, do the debtors get to keep the proceeds from the sale or do those proceeds become property of the estate? The answer to that question has proven somewhat elusive. For the reasons explained below, the court determines (1) property of the estate that vests in the debtors at confirmation loses its status as property of the estate, but (2) proceeds from the sale of vested property are new property that replenish—and, therefore, become property of —the chapter 13 estate.

In this case, debtors Christopher and Nicole Marsh seek to retain proceeds from the post-confirmation sale of their residence. The court determines that because the proceeds arose after confirmation and are distinct from the pre-sale unrealized appreciation in the residence, the proceeds are property of the Marshes' chapter 13 estate. That determination, however, is only the first step in the court's adjudication of the Marshes' motion to retain. Because the court requires additional evidence, it does not presently rule on the motion to retain but instead sets this matter for further proceedings consistent with the court's analysis in this case.

JURISDICTION

The court has jurisdiction over this matter under 28 U.S.C. §§ 1334(b) and 157(a) and (b). This matter is a statutorily core proceeding under 28 U.S.C. § 157(b)(2)(A) and (O) and is constitutionally core. No party has contested the court's jurisdiction or its authority to make a final determination. The

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

court, therefore, has authority to hear this matter and make a final determination.

BURDEN OF PROOF

[1] As movants, the Marshes bear the burden of proof in this case. *See* ***728** *Joseph A. Bass Co. v. United States*, 340 F.2d 842, 844 (8th Cir. 1965) ("It is fundamental that the burden of proof in any cause rests upon the party who, as determined by the pleadings or the nature of the case, asserts the affirmative of an issue and remains there until the termination of the action.").

BACKGROUND

The parties do not dispute the relevant facts.

The Marshes commenced this case by filing a chapter 13 voluntary petition in September 2018.[1] On their schedule A/B, they listed a $140,000 ownership interest in their residence.[2] Freedom Mortgage Corporation asserted a $124,842.71 lien against the residence as of the petition date.[3] The Marshes claimed a $15,000 homestead exemption.[4]

The Marshes' chapter 13 plan provided that the trustee would make payments on Freedom Mortgage's secured claim during the Marshes' chapter 13 case and further provided that non-priority unsecured creditors would receive nothing.[5] The Marshes' proposed plan would take a total of five years to complete. Though the Marshes later modified their plan, the modification did not alter these key provisions.[6] The court confirmed the Marshes' original plan in November 2018[7] and approved the plan modifications in May 2021.[8] No party objected to confirmation of the original plan or approval of the May 2021 modification.

In April 2022, the Marshes filed a motion to sell their residence.[9] The sale motion stated that the Marshes had "received an offer to purchase their home for $210,000," that the sale was scheduled to close on May 19, 2022, and that the sale would "result in net proceeds of approximately $78,000."[10] The trustee filed a notice stating he had "reviewed the related motion and ha[d] no objection."[11] No other party objected to the sale. The court entered an order granting the motion to sell the residence on April 26, 2022.[12]

In July 2022, the Marshes filed the present motion to retain proceeds from the sale of their former residence.[13] The Marshes report that the sale produced $73,252 net proceeds and ask the court to enter an order permitting them to retain all proceeds "to be used for obtaining a ***729** new residence and other expenses."[14] The chapter 13 trustee objected to the motion to retain, requesting that the Marshes remit to the trustee an amount sufficient to pay 100% of the filed and allowed non-priority unsecured claims against the Marshes' chapter 13 estate.[15]

The parties submitted briefs in support of their respective positions,[16] and the court held oral argument on the Marshes' motion.[17] At oral argument and in his brief, the trustee argued that the proceeds from the sale of the Marshes' residence are property of the estate. The Marshes argued the proceeds are not property of the estate and are otherwise unavailable to the trustee because the applicable commitment period that applied to the Marshes' chapter 13 case expired before the Marshes acquired the proceeds.

Having explained the relevant background information, the court next analyzes the issues the Marshes raise in their motion.

DISCUSSION

I. Post-Confirmation Property Replenishes the Chapter 13 Estate

The dispute in this case arises from a conflict between the provisions of the Bankruptcy Code that define property of the estate in a chapter 13 case and the provision that vests all property of the estate in the debtor at plan confirmation.

[2] Sections 541 and 1306 govern property of the estate in a chapter 13 case. 11 U.S.C. §§ 541, 1306. Section 541 broadly defines property of the estate to include, "all legal or equitable interests of the debtor in property as of the commencement of the case" and "[p]roceeds, product, offspring, rents, or profits of or from property of the estate."[18] 11 U.S.C. § 541(a)(1), (6). In chapter 13 cases, § 1306 clarifies that "in addition to the property specified in § 541," the estate includes all property "of the kind" specified in § 541 "that the debtor acquires after

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

the commencement of the case but before the case is closed, dismissed, or converted ... whichever occurs first." 11 U.S.C. § 1306(a). Thus, together, §§ 541 and 1306 make property of the estate all property the debtor (1) owns on the petition date and (2) acquires while the chapter 13 case is pending. 11 U.S.C. §§ 541, 1306.

Though §§ 541 and 1306 appear to capture for the estate both property the debtor acquires before plan confirmation and property the debtor acquires after confirmation, § 1327 arguably alters the estate's interest in property at the moment the court confirms the debtor's chapter 13 plan. *Compare* 11 U.S.C. § 541, *and* 11 U.S.C. § 1306, *with* 11 U.S.C. § 1327. Section 1327 states, "[e]xcept as otherwise ***730** provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor ... free and clear of any claim or interest of any creditor provided for by the plan." 11 U.S.C. § 1327(b)–(c). Courts have interpreted this language to move property "out of the estate and into the possession and control of the debtor upon confirmation of the plan." *Fritz Fire Prot. Co., Inc. v. Chang (In re Chang)*, 438 B.R. 77, 81 (Bankr. M.D. Pa. 2010) (quoting 3 Keith M. Lundin, *Chapter 13 Bankruptcy* § 230.1, at 231–1 (3d ed. 2000 and 2004 Supp.)).

The apparent removal of property from the estate at confirmation under § 1327 is somewhat difficult to reconcile with § 1306's inclusion in the estate of all property the debtor acquires between the petition date and the date "the case is closed, dismissed, or converted." *In re Clouse*, 446 B.R. 690, 699 (Bankr. E.D. Pa. 2010). Nonetheless, the reconciliation of these statutes may determine several outcomes in a chapter 13 case. For example, determining the scope of post-confirmation property of the estate may control whether expenses incurred to preserve property are entitled to administrative priority as "actual, necessary costs of preserving the estate" under § 503(b)(1)(A). *See, e.g.*, *Sec. Bank of Marshalltown v. Neiman*, 1 F.3d 687, 691 (8th Cir. 1993) ("the bankruptcy court was correct in finding the Chapter 13 estate continued post-confirmation and in classifying the post-petition debts [incurred to preserve debtor's principal asset] as administrative expenses"). The postconfirmation characterization of property also may determine whether subsections (2), (3), and (4) of § 362(a) automatically stay certain actions as against "property of the estate." *See, e.g.*, *City of Chicago v. Fisher (In re Fisher)*, 203 B.R. 958, 964 (N.D. Ill. 1997) (determining city's post-confirmation actions to immobilize, tow, and destroy a vehicle that had previously vested in the debtor at confirmation did not violate § 362(a)(3) because the actions were not "to exercise control over property of the estate"). And in circumstances like those in the present case, reconciliation of § 1306 and § 1327 may determine the scope of a debtor's entitlement to retain post-confirmation property. *See, e.g.*, *Barbosa v. Solomon*, 235 F.3d 31 (1st Cir. 2000) (affirming the bankruptcy court's decision to require an increased dividend to unsecured creditors).

Five approaches to reconciling § 1306 and § 1327 have emerged. *See In re Baker*, 620 B.R. 655, 663–64 (Bankr. D. Colo. 2020) (listing approaches). In selecting among the competing approaches, the court endeavors to give effect to all relevant statutes; it may not give effect to one statute while ignoring others. *See Epic Sys. Corp. v. Lewis*, —— U.S. ——, 138 S. Ct. 1612, 1624, 200 L.Ed.2d 889 (2018) (explaining approach to reconciling Federal Arbitration Act, Fair Labor Standards Act, and National Labor Relations Act). The court will analyze each approach in turn.

Estate Termination Approach

Courts adopting the "estate termination approach," conclude that, because § 1327 vests all property in the debtor at confirmation, the chapter 13 estate terminates at confirmation except as provided in the debtor's plan. *See Cal. Franchise Tax Bd. v. Jones (In re Jones)*, 420 B.R. 506, 512–13, 515 (B.A.P. 9th Cir. 2009) (describing then adopting the estate termination approach). As a result, "all property of the estate, whether acquired before or after confirmation, becomes property of the debtor"—and may become vulnerable to post-petition creditors—unless the plan designates it property of the estate. *See* ***731** *In re Baker*, 620 B.R. 655, 663, 667–68 (Bankr. D. Colo. 2020) (adopting estate termination approach but concluding that § 362(a)(5)–(7) protected vested property); *In re Jones*, 420 B.R. at 515–16 (discussing creditor's ability to collect against property under the estate termination approach and debtor's access to credit and use of property after confirmation). Proponents of this approach reason that it "effectuates the important choice [§] 1327(b) gives to the debtor ... to vest in itself all, none, or some combination of estate property." *In re Jones*, 420 B.R. at 515.

Eighth Circuit precedent eliminates the estate termination approach as an available method of reconciling § 1306 and § 1327. *See Sec. Bank of Marshalltown v. Neiman*, 1 F.3d 687, 690 (8th Cir. 1993) (concluding that the estate continues to exist after confirmation). [19] Specifically, the Eighth Circuit

expressly rejected the estate termination approach in *Neiman*, reasoning that the trustee's post-confirmation authority to administer the estate and "[s]everal sections of the bankruptcy code support [the] view that the estate continues to exist after confirmation." *Id.* at 690–91 (analyzing implication of 11 U.S.C. §§ 345, 347, 349(b)(3), 704, 1302(b)(1), and 1327 and determining estate continues after confirmation); *see also In re Rangel*, 233 B.R. 191, 195–96 (Bankr. D. Mass. 1999) (explaining that the estate termination approach would render several provisions of the Bankruptcy Code "meaningless or superfluous"). As the Eighth Circuit concluded in *Neiman*, the structure and operation of the Bankruptcy Code demonstrate that the estate continues to exist after confirmation. *See Neiman*, 1 F.3d at 690–91 (discussing Code provisions that undermine the estate termination approach). Consequently, the court rejects the estate termination approach.

Estate Preservation Approach

The approach differing most from the estate termination approach is the "estate preservation approach." *See In re Clouse*, 446 B.R. 690, 700 (Bankr. E.D. Pa. 2010) ("At one extreme is estate preservation; at the other extreme is estate termination."). Under the estate preservation approach, the estate continues after confirmation, retains all pre-confirmation property, and also includes any property the debtor acquires after confirmation. *See e.g.*, *Annese v. Kolenda (In re Kolenda)*, 212 B.R. 851, 853 (W.D. Mich. 1997) (determining that "vesting" under § 1327 removes no property from the estate). Courts adopting this approach reason that § 1327 is not relevant to the scope of property of the estate because § 1327's vesting provision merely "fix[es] the debtor's right to possess and deal with estate property after confirmation." *Id.* at 853–54 (quoting *In re Fisher*, 198 B.R. 721, 733 (Bankr. N.D. Ill. 1996)). As a result, property of the debtor and property of the estate are "one and the ***732** same" both before and after confirmation, and the automatic stay continues to protect all property after confirmation. *See id.* at 853–55 (discussing estate preservation approach and need to preserve assets for creditors and protect priority).

The court determines the estate preservation approach does not adequately reconcile § 1306 and § 1327. Though this approach comports with § 1306, it significantly undermines § 1327 by construing § 1327 as giving the debtor something less than an immediate, absolute interest in vested property. *See Fritz Fire Prot. Co., Inc. v Chang (In re Chang)*, 438 B.R. 77, 80–81 (Bankr. M.D. Pa. 2010) (rejecting the estate preservation approach because, among other reasons, vesting must mean more than giving debtors the right to possession). This construction is at odds with the mandate in § 1327(c) that "the property vesting in the debtor under subsection (b) of this section is free and clear of any claim or interest of any creditor provided for by the plan." *See City of Chicago v. Fisher (In re Fisher)*, 203 B.R. 958, 962 (N.D. Ill. 1997) (emphasizing the effect of § 1327(c)). The court rejects the estate preservation approach as not recognizing the import of § 1327.

Conditional Vesting Approach

Like the estate preservation approach, the "conditional vesting approach" interprets § 1306 and § 1327 to make property simultaneously property of the debtor and property of the estate. Under the conditional vesting approach, § 1327 gives the debtor "an immediate and fixed right to the future enjoyment of the bankruptcy estate," but that right is not final until the debtor "has faithfully completed his obligations under the plan and is entitled to a discharge." *Woodard v. Taco Bueno Rests., Inc.*, No. 4:05-CV-804-Y, 2006 WL 3542693, at *9 (N.D. Tex. Dec. 8, 2006). The result is that "assets that the debtor acquire[s] after confirmation must be included in the bankruptcy estate," and are subject to the trustee's administration. *Id.* at *10. Courts adopting this approach reason that it results in "a legitimate *quid pro quo*": in exchange for a discharge of debts and the ability to retain all assets under the protection of the automatic stay, the debtors have a continuing obligation to disclose all pre- and post-confirmation assets and account for them under the plan when appropriate. *Id.* at *9–10.

The conditional vesting approach suffers from the same flaws that made the court reject the estate preservation approach. The conditional vesting approach disregards § 1327's mandate that property vests in the debtor "free and clear" of creditors' claims at confirmation. *See City of Chicago v. Fisher (In re Fisher)*, 203 B.R. 958, 961 (N.D. Ill. 1997) (critiquing the estate preservation approach). In addition, because this approach makes parties' respective property rights conditional until those rights "vest" at plan completion, it creates uncertainty about the extent of each parties' interests in property during the life of the chapter 13 plan. The court declines to adopt an approach that creates such uncertainty.

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

Estate Transformation Approach

Under the "estate transformation approach," the "estate consists of the property and future earnings of the debtor dedicated to fulfillment of the Chapter 13 plan," regardless of whether the debtor acquires that property before or after confirmation. *In re Root*, 61 B.R. 984, 985 (Bankr. D. Colo. 1986). Courts adopting the estate transformation approach reason that the post-confirmation estate must include property necessary to fulfill the plan because §§ 1322 and 1327(b) imply that the plan and confirmation order control the extent of vesting under § 1327. *See, e.g.*, ***733** *In re Adams*, 12 B.R. 540, 541–42 (Bankr. D. Utah 1981) (discussing exceptions under §§ 1322 and 1327 and adopting the estate transformation approach); 11 U.S.C. § 1322(b) (authorizing plan to provide for vesting after confirmation or in an entity other than the debtor); 11 U.S.C. § 1327(b) (vesting property in the debtor "[e]xcept as otherwise provided in the plan or order confirming the plan"). Courts developed this approach as "[a] compromise between the[ ] two extremes" of the estate termination and the estate preservation approaches. *Telfair v. First Union Mortg. Corp.*, 216 F.3d 1333, 1340 (11th Cir. 2000). It "attempts to honor, in part, the vesting provision of Section 1327(b), while acknowledging the inclusive language of Section 1306(a)." *In re Clouse*, 446 B.R. 690, 701 (Bankr. E.D. Pa. 2010).

Though "attractive in concept," neither the Bankruptcy Code's plain language nor the practicalities of chapter 13 support the estate transformation approach. *Fritz Fire Prot. Co., Inc. v. Chang (In re Chang)*, 438 B.R. 77, 82 (Bankr. M.D. Pa. 2010). Specifically, "no textual basis exists for distinguishing between post-confirmation property that is 'necessary' and that which is 'not necessary' " to fulfill the chapter 13 plan. *Annese v. Kolenda (In re Kolenda)*, 212 B.R. 851, 855 (W.D. Mich. 1997). Sections 1322 and 1327 are not so broad as to make property of the estate all property necessary to the plan; those provisions instead require that the plan or confirmation order designate property that does not vest in the debtor at confirmation. *See* 11 U.S.C. § 1322(b)(9) ("the plan may ... provide for the vesting of property of the estate, on confirmation of the plan or at a later time, in the debtor or in any other entity"); 11 U.S.C. § 1327(b) ("Except as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor."). Moreover, "this approach is difficult to apply in practice" because reasonable parties may disagree about what property is "necessary" to fulfill the plan at any given time, and the necessity of property may change throughout the chapter 13 case. *In re Chang*, 438 B.R. at 82. The Bankruptcy Code and chapter 13 practice, therefore, do not support this approach.

Estate Replenishment Approach

[3] Finally, under the "estate replenishment approach," pre-confirmation property of the estate becomes property of the debtor at confirmation, but post-confirmation property becomes property of (*i.e.,* "replenishes") the estate. *City of Chicago v. Fisher (In re Fisher)*, 203 B.R. 958, 962–63 (N.D. Ill. 1997); *In re Chang*, 438 B.R. at 83–84 (adopting what it dubbed the "reconciliation approach"). This approach reconciles § 1306 and § 1327 by construing vesting under § 1327 as an event that occurs only at confirmation. *See In re Fisher*, 203 B.R. at 964 (summarizing sequence of events under §§ 541, 1306(a), and 1327). Specifically, on the petition date, "§ 541 generally sweeps the debtor's property into the estate." *Id.* Between the petition date and the date of confirmation, § 1306 operates to augment the estate with any additional property "of the kind specified in [§ 541] that the debtor acquires." *See id.* (summarizing holding). Each time the plan or modified plan is confirmed, § 1327 vests all then-existing property of the estate in the debtor, unless the plan or confirmation order provides otherwise. *See id.* (analyzing § 1327). But any property the debtor acquires after confirmation "is not subject to § 1327(b) because it was not in existence at confirmation." *Fritz Fire Prot. Co., Inc. v. Chang (In re Chang)*, 438 B.R. 77, 83 (Bankr. M.D. Pa. 2010). "After confirmation, § 1306(a) once again operates to deem property acquired by the debtor after confirmation as property of the estate." *In re Fisher*, 203 B.R. at 964.

***734** Critics of the estate replenishment approach typically reject it as giving insufficient weight to either § 1306 or § 1327. *See, e.g.*, *In re Baker*, 620 B.R. 655, 669 (Bankr. D. Colo. 2020) (disagreeing with the estate replenishment approach); *Woodard v. Taco Bueno Rests.*, No. 4:05-CV-804-Y, 2006 WL 3542693, *8 (N.D. Tex. Dec. 8, 2006) (explaining importance of §§ 541 and 1306). Some courts conclude that, by including post-confirmation property in the estate, the estate replenishment approach "reads § 1306 too broadly and gives insufficient weight to § 1327(b)," undermining "the chapter 13 bargain a debtor makes when trading his future income [devoted to the plan] for his assets." *In re Baker*, 620 B.R. at 669 (analyzing the benefits of the estate termination approach); *see also In re Chang*, 438

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

B.R. at 83 n.7 (noting commentator's concern with estate replenishment approach's broad inclusion in the estate of post-confirmation proceeds from vested assets). Others, however, conclude that the estate replenishment approach reads § 1306 too narrowly and exaggerates the effect of § 1327 by pretending the debtor enjoys absolute entitlement to vested property and ignoring that the Bankruptcy Code inherently conditions the debtor's entitlement to vested property on the faithful fulfillment of the plan. *Woodard*, 2006 WL 3542693, at *7. All are valid critiques.

[4] Despite these flaws, the court determines the estate replenishment approach best reconciles § 1306 and § 1327. *See In re Chang*, 438 B.R. at 84 (adopting estate replenishment approach but noting "[r]emedial legislative drafting would more appropriately solve the conundrum") (quoting *In re Ziegler*, 136 B.R. 497, 502 (Bankr. N.D. Ill. 1992)). The estate replenishment approach gives effect to § 1306 by including in the estate, at least temporarily, all property the debtor acquires after the petition date but before the case is closed, dismissed, or converted. *See City of Chicago v. Fisher (In re Fisher)*, 203 B.R. 958, 962 (N.D. Ill. 1997) (discussing effect of § 1306(a)). It also gives effect to § 1327 by honoring the vesting of property free and clear of creditors' claims. *In re Larzelere*, 633 B.R. 677, 682 (Bankr. D.N.J. 2021). Moreover, by making "a clear demarcation" between pre-confirmation property (which vests in the debtor) and post-confirmation property (which becomes property of the estate), the estate replenishment approach differentiates between property of the debtor and property of the estate more predictably than other approaches. *In re Chang*, 438 B.R. at 83; *see also Barbosa v. Solomon*, 235 F.3d 31, 37 (1st Cir. 2000) (explaining that this approach "gives meaning to both sections 1306 and 1327, without the subjective analysis required by the [estate transformation] approach"). Finally, this approach "avoids creating a distinction among types of post-confirmation estate property where there exists no textual basis to do so." *In re Fisher*, 203 B.R. at 962–63. Consequently, the court adopts the estate replenishment approach in this case.

The court's conclusion that the estate replenishment approach governs the scope of post-confirmation property of the estate, however, is only the first step in its analysis. The court must next apply that approach to the sale proceeds in this case to determine whether the proceeds are property vested in the debtors or property of the chapter 13 estate.

II. The Proceeds from the Sale of Vested Property are Property of the Estate Under the Estate Replenishment Approach

[5] **[6]** As the court explained above, under the estate replenishment approach, absent contrary provisions in the plan or ***735** confirmation order, property the debtor acquires before confirmation first becomes property of the estate, then vests in the debtor at confirmation. *See e.g.*, *In re Fisher*, 203 B.R. at 964 (summarizing estate replenishment approach). But "all property of the kind specified in [§ 541] that the debtor acquires" after confirmation and "before the case is closed, dismissed, or converted" becomes property of the replenished chapter 13 estate. *Id.*

[7] In this case, the Marshes seek to retain proceeds from the post-confirmation sale of their residence, arguing their interest in the proceeds vested at confirmation along with their residence. The trustee disagrees, arguing the proceeds are distinct from the vested residence and § 1306 brings them into the estate as property "of the kind" specified in § 541 that the debtors "acquire[d]" after the petition date. For the reasons explained below, the court determines (1) proceeds are distinct from the property sold to produce them, (2) proceeds are property "of the kind" specified in § 541, and (3) the Marshes "acquired" the proceeds after the confirmation date. Consequently, the proceeds are property of the estate in this case.

Courts disagree about whether proceeds from the sale of vested property are distinct from the property sold. *Compare Barbosa*, 235 F.3d at 35, 41–42 (affirming district court's decision that § 1327 "vested title to the realty in the Debtors at confirmation, but not the proceeds of the sale"), *with In re Larzelere*, 633 B.R. 677, 683 (Bankr. D.N.J. 2021) (equating proceeds with appreciation and "respectfully disagree[ing] with the holding in *Barbosa* that [proceeds are] ... separate from the originally-valued real property in a confirmed chapter 13 case"). Some courts hold that proceeds are distinct, reasoning that proceeds differ materially from the property that generated them. *See, e.g.*, *Rodriguez v. Barrera (In re Barrera)*, 22 F.4th 1217, 1223, 1223 n.3 (10th Cir. 2022) (excluding sale proceeds from the converted estate because proceeds are "a property interest distinct from the physical house from which they were derived" and recognizing that this result potentially creates a conflict with § 1306); *In re Hawk*, 871 F.3d 287, 293–95 (5th Cir. 2017) (construing prior Fifth Circuit determination that proceeds from the sale of exempt property were new property and therefore not entitled to exemption in chapter 13 case) (analyzing *In re Frost*, 744

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

F.3d 384 (5th Cir. 2014)). Others conclude that, because the debtor owns vested property outright, the proceeds from the later sale of that property cannot become property of the estate. *In re Larzelere*, 633 B.R. at 683.

The court agrees with the decisions distinguishing sale proceeds from the property sold. *E.g.*, *In re Barrera*, 22 F.4th at 1223.

Courts that have reached the opposite conclusion have done so by equating proceeds with unrealized appreciation. *See In re Larzelere*, 633 B.R. at 683 (using the terms "proceeds" and "appreciation" interchangeably). Concededly, *unrealized appreciation* "cannot be separated from the underlying [property]" and, therefore, remains vested in the debtor so long as the debtor retains the property. *See id.* (equating proceeds with appreciation). Because unrealized appreciation is not separate property, those courts that equate proceeds with unrealized appreciation might find it illogical to treat sale proceeds as separate property. *See id.* ("because the [ ] Property ceased to be property of the estate, the proceeds of its later sale could not become property of the chapter 13 estate").

[8] But treating proceeds as separate property logically results from the differences between sale proceeds and unrealized ***736** appreciation. *Compare In re Barrera*, 22 F.4th at 1219 (determining proceeds that arose before conversion inured to the debtors), *with In re Goetz*, Case No. 20-41493, 647 B.R. 412, 413-14 (Bankr. W.D. Mo. Nov. 10, 2022) (determining unrealized appreciation that arose before conversion inured to the estate). Unlike appreciation, *proceeds* in the form of cash or cash equivalents are entirely separate from the underlying property after the property is sold, with attributes and uses distinct from the property sold. *See In re Barrera*, 22 F.4th at 1223 (analyzing "whether ... proceeds from the post-petition sale of property are identical to the underlying property that the debtor possessed on the Chapter 13 petition date" and concluding "they are not."); *c.f. In re Larzelere*, 633 B.R. at 683 ("One cannot separately pledge, mortgage, hypothecate or liquidate *appreciation*." (emphasis added)). The Bankruptcy Code recognizes this distinction by treating proceeds separately from the property that generates them. *See, e.g.*, 11 U.S.C. § 541(a)(6) (separately including proceeds in the estate); *Id.* § 552(b)(1) (requiring separate pledge of proceeds). Proceeds are, therefore, a separate, distinct form of property. [20]

In this case, because the proceeds are distinct from the Marshes' former residence and because the proceeds were not property of the estate at confirmation, the proceeds could not have vested in the Marshes at confirmation under § 1327. *See* 11 U.S.C. § 1327(b) ("the confirmation of a plan vests all of the property of the estate in the debtor"). Consequently, under the estate replenishment approach, § 1306 makes the proceeds property of the replenished chapter 13 estate if they are "property of the kind specified in [§ 541]" that the Marshes "acquire[d]" after confirmation.

[9] The proceeds are "property of the kind specified in [§ 541]." Section 1306(a) captures for the post-petition estate "in addition to the property specified in section 541" the "kind[s]" of property specified in that section "that the debtor acquires after the commencement of the case but before the case is closed, dismissed, or converted." 11 U.S.C. § 1306(a)(1). Section 541(a) specifies several kinds of property that become property of the estate, including "all legal or equitable interests of the debtor in property as of the commencement of the case." [21] 11 U.S.C. § 541(a)(1). And though § 541(a)(1) only captures for the estate property the debtor owned "as of the commencement of the case," § 1306(a)(1) expands that temporal restriction ***737** by imposing its own distinct, post-petition time period to the *kinds* of property § 541 specifies. *See Carroll v. Logan*, 735 F.3d 147, 150–51 (4th Cir. 2013) (concluding § 1306 captured for the estate an inheritance acquired more than 180 days after the petition date despite the 180-day temporal restriction under § 541(a)(5)). In this case, the Marshes' interest in the proceeds certainly is "a legal or equitable interest of the debtor[s] in property" within the meaning of the first part of § 541(a)(1). And though the Marshes did not have an interest in the proceeds "as of the commencement of the case," under § 1306(a)(1)'s expanded temporal framework, the Marshes' interest in the proceeds are nonetheless "legal or equitable interests of a debtor in property" "of the kind specified in [§ 541(a)(1)]."

[10] Finally, the court determines the Marshes "acquire[d]" the proceeds within the relevant period under § 1306(a)(1). Black's Law Dictionary broadly defines the term "acquire" to mean "1. To gain possession or control of; to obtain," or "2. To gain as an attribute of form <the statute acquired judicial gloss>." *Acquire*, Black's Law Dictionary (11th ed. 2019). Merriam Webster similarly defines the term "acquire," in relevant part, as "to get as one's own," meaning either "a: to come into possession or control of often by unspecified means," or "b: to come to have as a new or added characteristic, trait or ability (as sustained by effort or natural ability)." *Acquire*, merriam-webster.com, https://www.merriam-webster.com/dictionary/acquire (last visited

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

Dec. 8, 2022). In this case, the Marshes "gain[ed] possession or control of" or "c[a]me into possession or control of" the proceeds when they sold the property after confirmation. Likewise, though the proceeds arose from the residence, they, at a minimum, became proceeds "as an attribute of form" or as "a new or added characteristic" after confirmation and before the end of the Marshes' chapter 13 case. Thus, the Marshes "acquired" the proceeds during the relevant period under § 1306(a)(1).

In summary, the court determines the proceeds are distinct property "of a kind" specified in § 541 that the Marshes "acquired" during the relevant period. Consequently, § 1306(a)(1) makes them property of the chapter 13 estate under the estate replenishment approach. [22]

III. Section 1322 Does Not Exclude the Proceeds from the Replenished Estate

[11] In addition to their arguments concerning the scope of the post-confirmation chapter 13 estate, the Marshes argue alternatively that the court must permit them to retain the proceeds in this case because their thirty-six-month applicable ***738** commitment period "suggests that the debtors are not required to commit disposable income received after that applicable commitment period to pay unsecured creditors." [23] Brief in Supp. of Mot. to Retain, ECF No. 93 (Sept. 28, 2022). The court disagrees.

The Marshes' argument relies on a temporal limitation set forth in 11 U.S.C. § 1325. Subsection (b)(1) of that section states,

> If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the court may not approve the plan unless, as of the effective date of the plan--
>
> ...
>
> (B) the plan provides that all of the debtor's projected disposable income to be received in the applicable commitment period beginning on the date that the first payment is due under the plan will be applied to make payments to unsecured creditors under the plan.

Id.

The court rejects the Marshes' proposal to apply § 1325(b)(1)'s applicable commitment period outside the context of initial plan confirmation. Section 1325(b) applies only to the confirmation of a debtor's initial plan. *Compare* 11 U.S.C. § 1325 ("Confirmation of plan"), *with* 11 U.S.C. § 1329 ("Modification of plan after confirmation"). And § 1325(b)(1) applies only "[i]f the trustee or a holder of an allowed secured claim objects to the confirmation of the plan." 11 U.S.C. § 1325(b). In this case, the Marshes are not seeking initial confirmation, and neither the trustee nor a holder of an allowed secured claim has objected to confirmation. Nothing in the Bankruptcy Code would otherwise make § 1325(b)(1) apply to the Marshes' motion to retain proceeds. *See* 11 U.S.C. § 1325(b)(1). Consequently, the court declines to apply § 1325(b)(1) to the Marshes' motion to retain.

[12] Moreover, even if the court construes the present motion as a proposed modification to the Marshes' confirmed plan, the applicable commitment period under § 1325(b) would not govern the proposed modification because the applicable commitment period does not apply to plan modifications. *See Forbes v. Forbes (In re Forbes)*, 215 B.R. 183, 191–93 (B.A.P. 8th Cir. 1997) (analyzing § 1329 and concluding the so called "best efforts test" under § 1325(b)(1) "is not a factor to be considered by a court in approving postconfirmation modifications"). After the initial confirmation, § 1329—not § 1325—governs approval of plan modifications. *Id.* at 191. Though § 1329 incorporates some provisions of § 1325, it does not incorporate the applicable commitment period under § 1325(b). *See id.* (quoting 11 U.S.C. § 1329(b)(1)). Instead, § 1329(c) authorizes the court to approve a post-confirmation plan modification that provides for payments over a period longer than thirty-six months in below median cases, so long as the modified plan does not expire more than five years after the first payment under the original plan came due. 11 U.S.C. § 1329(c). Thus, even if the court construes the Marshes' motion to retain proceeds as a proposed plan modification, the applicable commitment period under § 1325(b)(1) does not apply.

[13] Finally, even if the applicable commitment period in § 1325(b)(1) applied, it would not prevent the Marshes from making payments after the thirty-sixth ***739** month of their plan. The court agrees with the Marshes' assertion that "the applicable commitment period is a temporal requirement and not a monetary requirement" under *Coop v. Frederickson (In re Frederickson)*, 545 F.3d 652, 660 (8th Cir. 2008). Brief in Supp. of Mot. to Retain, ECF No. 93 (Sept. 28, 2022). But the thirty-six-month applicable commitment period that applies to below median debtors "acts solely to set the minimum term of a chapter 13 plan that [below-median] debtors may

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

be compelled to propose." *In re Rodger*, 423 B.R. 591, 595 (Bankr. D.N.H. 2010); *see also In re Frederickson*, 545 F.3d at 660 (quoting authority stating that the applicable commitment period creates a temporal minimum). "If a below median debtor elects to propose a longer term than three years, and the Court for cause approves such longer term, the requirements for payment of disposable income in years four and five of the plan remain the same as those in the first three years of the plan." *In re Rodger*, 423 B.R. at 595. In this case, the Marshes obtained confirmation of a sixty-month plan. Order Confirming the Chapter 13 Plan, ECF No. 22 (Nov. 15, 2018). Section 1325(b)(1), therefore, does not prevent the court from enforcing the Marshes' plan after the thirty-sixth month. Thus, § 1325(b)(1) does not undermine the court's determination that the proceeds are property of the estate in this case.

IV. The Court's Analysis Does Not Resolve the Marshes' Motion to Retain

[14] The court's determination that the proceeds are property of the Marshes' estate, however, does not resolve the Marshes' motion to retain. Because the Marshes' confirmed plan requires ongoing payments on their mortgage, the Marshes' sale of their residence and proposal to retain the proceeds from that sale contravene the terms of their confirmed plan. *See* Chapter 13 Plan, ECF No. 2 (Sept. 19, 2018). Thus, the Marshes, in effect, seek to modify their confirmed plan without filing a modified plan or otherwise specifying the terms of their proposed modification. The court will not rule on the Marshes' motion to retain until the Marshes clarify the nature and effect of their proposed modification.

[15] **[16]** **[17]** Moreover, the court's determination that the proceeds are property of the estate does not necessarily prevent the Marshes from retaining at least a portion of the proceeds under a modified plan. Section 1329, which governs plan modification, does not necessarily require that debtors pay the value of all post-confirmation assets to the estate. 11 U.S.C. § 1329. Instead, § 1329(b)(1) requires that modified plans comply with §§ 1322(a), 1322(b), 1323(c), and 1325(a), by, among other prerequisites, providing for submission of future income as necessary to execute the plan, being proposed in good faith, and satisfying § 1325(a)(4)'s liquidation-analysis requirement "as of the effective date of the plan"—which, in the Eighth Circuit, is a date that precedes plan modification. 11 U.S.C. § 1329(b)(1); *Forbes v. Forbes (In re Forbes)*, 215 B.R. 183, 189 (B.A.P. 8th Cir. 1997) ("Regarding the effective date of the plan, there is only one plan. The effective date is not altered by modification of the plan, for the modified plan remains, ever constant, the plan."). Whether the Marshes' proposed modification satisfies these prerequisites is a mixed question of law and fact, requiring evidence not before the court. Consequently, the court does not presently rule on the Marshes' motion to retain proceeds and instead sets this matter for further proceedings consistent with the court's analysis in this case.

CONCLUSION

For the reasons set forth in this memorandum opinion, the court determines the ***740** proceeds from the sale of the Marshes' residence are property of the chapter 13 estate. The court will enter a separate notice and order on the docket setting this matter for further proceedings consistent with this memorandum opinion.

IT IS SO ORDERED.

All Citations

647 B.R. 725, 72 Bankr.Ct.Dec. 58

Footnotes

1 Chapter 13 Voluntary Pet., ECF No. 1 (Sept. 19, 2018).

2 Schedule A/B, ECF No. 1, at 18 (Sept. 19, 2018).

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

3 Freedom Mortg. Corp. Proof of Claim, Claim No. 25-1 (Nov. 21, 2018). Though Freedom Mortgage amended its proof of claim in January 2019, the amended proof of claim did not alter the claim amount or secured status. Freedom Mortg. Corp. Am. Proof of Claim, Claim No. 25-1 (Nov. 21, 2018).

4 Chapter 13 Voluntary Pet. 26, ECF No. 1 (Sept. 19, 2018).

5 Chapter 13 Plan, ECF No. 2 (Sept. 19, 2018).

6 First Am. Plan, ECF No. 47 (Apr. 15, 2021).

7 Initial Confirmation: Order Confirming the Chapter 13 Plan as Filed, ECF No. 22 (Nov. 15, 2018).

8 Order Confirming Chapter 13 Plan as Filed or Am. on or About 4/16/21, ECF No. 53 (May 7, 2021).

9 Mot. to Sell Real Estate, ECF No. 64 (Apr. 25, 2022).

10 *Id.*

11 Trustee text entry, ECF No. 66 (Apr. 26, 2022).

12 Order Granting Mot. to Sell, ECF No. 67 (Apr. 26, 2022).

13 Mot. to Retain Proceeds from Sale of Home, ECF No. 74 (July 27, 2022).

14 *Id*.

15 Trustee's Obj. to Mot. to Sell Property, ECF No 78 (July 28, 2022). Though the document is titled an objection to debtors' motion to sell, the body of the document makes clear that the trustee intended the document as an objection to the Marshes' motion to retain proceeds.

16 Brief in Supp. of Tr. Obj. to Debtors' Mot. to Retain Proceeds from Sale, ECF No. 92 (Sept. 27, 2022); Brief in Supp. of Mot. to Retain, ECF No. 93 (Sept. 28, 2022).

17 Hearing Held, ECF No. 95 (Oct. 4, 2022).

18 Though § 541(a)(6) excludes post-petition earnings, § 1306(a)(2) captures post-petition earnings from services for the chapter 13 estate. Because it does not appear that the proceeds from the sale of the Marshes' residence are earnings from services, the court does not focus on the Bankruptcy Code's treatment of post-petition earnings in this memorandum opinion.

19 Although the Eighth Circuit conclusively rejected the estate termination approach in *Neiman*, the *Neiman* court did not clearly adopt any particular approach. *See Sec. Bank of Marshalltown v. Neiman*, 1 F.3d 687, 690–91 (8th Cir. 1993). In dicta, the court cited approvingly both authority adopting the estate preservation approach and authority adopting the estate transformation approach. *Id.* (first quoting *In re Root*, 61 B.R. 984, 985 (Bankr. D. Colo. 1986); then quoting *Riddle v. Aneiro (In re Aneiro)*, 72 B.R. 424, 429 (Bankr. S.D. Cal. 1987)). The Eighth Circuit did not analyze the estate replenishment approach, likely because that approach developed later. *See Neiman*, 1 F.3d at 689 (comparing the two lines of cases that existed at the time the court issued its decision). As the below explanations of the estate preservation and estate termination approaches illustrate, those approaches reach inconsistent conclusions concerning the effect of § 1327. Consequently, the court does not interpret *Neiman* to bind this court to either the estate preservation approach or the estate transformation approach in this case.

20 The court acknowledges that this interpretation may incentivize debtors to retain appreciated property during a chapter 13 case. The court views this as a tolerable outcome to a complicated issue. As other courts

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

have noted, "there is something unsavory" about permitting a debtor to "walk[ ] away with substantial cash proceeds" during the life of a chapter 13 case without amending the plan to fairly accommodate any change in circumstances or converting to chapter 7. *In re Barbosa*, 236 B.R. 540, 551–52 (Bankr. D. Mass. 1999), *aff'd*, 243 B.R. 562 (D. Mass. 2000), *aff'd*, 235 F.3d 31 (1st Cir. 2000); *see also In re Barrera*, 22 F.4th at 1219 (permitting debtors to retain proceeds in circumstance of conversion to chapter 7). But there is something equally unsavory about the court ordering the sale of an appreciated residence against the debtor's wishes to generate proceeds for the estate. The court's decision in this case attempts to deter the pursuit of either unsavory outcome.

21 Though § 541(a)(6) also includes in the estate "proceeds ... from property of the estate," it does not include in the estate proceeds from property that is no longer property of the estate. Thus, because vested property is no longer property of the estate, § 541(a)(6) does not capture proceeds from vested property as property of the estate.

22 The court notes that the proceeds would also be property of the estate under the estate preservation approach, conditional vesting approach, and the estate transformation approach. The proceeds would become property of the estate under the estate preservation and conditional vesting approaches because, as the court explained above, those approaches make property of the estate all property the debtor acquires before or after confirmation. The proceeds also would be property of the estate under the estate transformation approach as "proceeds ... from property of the estate" under §§ 541 and 1306. Specifically, under the estate transformation approach, the residence would have remained property of the estate post-confirmation because it was necessary to the completion of the Marshes' confirmed plan. As a result, the proceeds would have been "proceeds ... from property of the estate" within the meaning of § 541(a)(6) and would themselves have become property of the estate under § 1306 as "property of the kind specified in [§ 541] that the debtor acquires after the commencement of the case but before the case is closed, dismissed, or converted."

23 In making this argument, the Marshes appear to assume that the sale proceeds are disposable income. Because the court otherwise determines the Marshes' argument relies on an inaccurate interpretation of the Bankruptcy Code, the court does not further determine whether the proceeds would constitute disposable income under § 1325(b).

End of Document

© 2024 Thomson Reuters. No claim to original U.S. Government Works.

654 B.R. 703
United States Bankruptcy Court, M.D. North Carolina, Durham Division.

IN RE: Johnny Ray ADAMS, Debtor.

Case No. 21-80425
|
Signed November 3, 2023.

Synopsis

Background: In Chapter 13 case, converted from one under Chapter 7, trustee filed motion to modify plan to require turnover of funds from postconfirmation sale of real property and to increase liquidation requirement.

Holdings: The Bankruptcy Court, Benjamin A. Kahn, J., held that:

[1] debtor's funds from sale of property constituted "substantial change in circumstances," as required to permit modification;

[2] debtor's sale of property only five months after confirmation was "unanticipated," as required to permit modification;

[3] purposes of proposed modification was permitted under Bankruptcy Code subsection that allowed for payments to be increased to a class of claim;

[4] proposed modification did not violate confirmation requirements or otherwise frustrate purposes of Bankruptcy Code;

[5] proposed modification satisfied "good faith" requirement; and

[6] proposed modification satisfied "best interests of the creditors" or "liquidation value" test.

Motion granted.

Procedural Posture(s): Motion to Modify Plan.

West Headnotes (14)

[1] **Bankruptcy** Time for completion; extension or modification

Bankruptcy Conclusiveness; res judicata; collateral estoppel

Doctrine of res judicata prevents modification of confirmed Chapter 13 plan unless debtor experiences substantial and unanticipated postconfirmation change in his financial condition. 11 U.S.C.A. § 1329(a).

[2] **Bankruptcy** Time for completion; extension or modification

Party seeking modification of confirmed Chapter 13 plan bears burden of demonstrating that postconfirmation change in debtor's ability to pay was both substantial and unanticipated. 11 U.S.C.A. § 1329(a).

[3] **Bankruptcy** Time for completion; extension or modification

Bankruptcy Conclusiveness; res judicata; collateral estoppel

Once res judicata is overcome, Chapter 13 plan can be modified after confirmation if the purpose of the proposed modification is one that is identified in Bankruptcy Code provision governing modification of plan after confirmation, and if the proposed modification complies with confirmation requirements applicable to modification of plans. 11 U.S.C.A. §§ 1329(a), 1329(b)(1).

[4] **Bankruptcy** Relation to recovery in liquidation

Bankruptcy Time for completion; extension or modification

Chapter 13 debtor's funds from sale of real property only five months after confirmation constituted "substantial change in circumstances," as required to permit

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

modification of debtor's confirmed plan; funds realized from the unanticipated sale of the property substantially changed debtor's ability to pay postconfirmation, especially given the 11.2 percent appreciation in the value of debtor's petition-date interest in the property, and debtor's nonexempt equity in the property constituted a substantial portion of the liquidation value required to be paid to creditors under the plan. 11 U.S.C.A. § 1329(a).

1 Case that cites this headnote

[5] **Bankruptcy** Time for completion; extension or modification

"Substantial change in circumstances," such as will permit modification of confirmed Chapter 13 plan, can be increased income or receipt of large sum of money. 11 U.S.C.A. § 1329(a).

[6] **Bankruptcy** Time for completion; extension or modification

Chapter 13 debtor's sale of real property only five months after confirmation was "unanticipated," as required to permit modification of debtor's confirmed plan; while debtor's plan contained a liquidation requirement of $79,705.55 and the vast majority of that liquidation value was attributable to nonexempt equity of $63,744.36 in the property, the plan gave no indication that debtor intended to sell the property. 11 U.S.C.A. § 1329(a).

[7] **Bankruptcy** Time for completion; extension or modification

Where a Chapter 13 plan provides for unsecured creditors to be paid from income earned from a business and the confirmed plan gives no indication of a debtor's intention to sell the business, a postconfirmation sale could be an "unanticipated" change warranting plan modification. 11 U.S.C.A. § 1329(a).

[8] **Bankruptcy** Time for completion; extension or modification

Where liquidation value of Chapter 13 plan relies on property that will remain property of estate, liquidation of that property during case can be "unanticipated" change, as required for postconfirmation modification of plan. 11 U.S.C.A. § 1329(a).

[9] **Bankruptcy** Time for completion; extension or modification

Purpose of Chapter 13 trustee's proposed modification to debtor's confirmed plan after sale of real property, namely, to increase amount of distribution to unsecured creditors and reduce time for payment by debtor, was permitted under Bankruptcy Code subsection that allowed for payments to be increased to a class of claim. 11 U.S.C.A. § 1329(a)(1).

[10] **Bankruptcy** Time for completion; extension or modification

Confirmed Chapter 13 plan may be modified to require turnover of funds that would create windfall to debtor. 11 U.S.C.A. § 1329(a).

[11] **Bankruptcy** Relation to recovery in liquidation

Bankruptcy Time for completion; extension or modification

Chapter 13 trustee's proposed modification of confirmed plan to require turnover of funds from postconfirmation sale of real property and to increase liquidation requirement did not violate confirmation requirements or otherwise frustrate purposes of Bankruptcy Code; debtor's interest in the property remained property of the estate postconfirmation and debtor's nonexempt equity in that interest represented a significant portion of the liquidation requirement in the plan, and debtor could not use proceeds from sale of the property without court approval. 11 U.S.C.A. §§ 363, 1303, 1325(a)(1), 1329(b)(1).

[12] **Bankruptcy** Particular plans

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

Bankruptcy Relation to recovery in liquidation

Bankruptcy Time for completion; extension or modification

Chapter 13 trustee's proposed modification of confirmed plan to require turnover of funds from postconfirmation sale of real property and to increase liquidation requirement satisfied "good faith" requirement, where modification would prevent debtor from receiving a substantial and unanticipated windfall, after debtor's liquidation of substantial appreciation in property value had significantly altered debtor's ability to pay. 11 U.S.C.A. §§ 1325(a)(3), 1329(b)(1).

[13] **Bankruptcy** Relation to recovery in liquidation

Bankruptcy Time for completion; extension or modification

Chapter 13 trustee's proposed modification of confirmed plan to require turnover of funds from debtor's postconfirmation sale of real property, after 11.2 percent appreciation in value of debtor's petition-date interest in the property, and to increase liquidation requirement satisfied "best interests of the creditors" or "liquidation value" test; trustee indicated that $60,022.28 of the original $63,744.36 attributable to the liquidation value of the property remained unpaid, and she requested an additional $31,319.57 in proceeds be turned over for distribution to unsecured creditors pursuant to the increased liquidation requirement of $109,403 under proposed modification and accordingly requested turnover of a total of $91,341.85. 11 U.S.C.A. §§ 1325(a)(4), 1329(b)(1).

[14] **Bankruptcy** Relation to recovery in liquidation

Bankruptcy Time for completion; extension or modification

"Best interests of the creditors" or "liquidation value" test for modification of confirmed Chapter 13 plan is applied using values as of effective date of Chapter 13 plan as modified. 11 U.S.C.A. § 1325(a)(4).

Attorneys and Law Firms

***705** Travis Sasser, Sasser Law Firm, Cary, NC, for Debtor.

Anita Jo Kinlaw Troxler, Greensboro, NC, Trustee, Pro Se.

ORDER GRANTING MOTION TO MODIFY PLAN TO REQUIRE TURNOVER OF FUNDS AND TO INCREASE LIQUIDATION REQUIREMENT

BENJAMIN A. KAHN, UNITED STATES BANKRUPTCY JUDGE

This matter is before the Court on the Motion to Modify Plan to Require Turnover of Funds and to Increase the Liquidation Requirement (the "Motion"), ECF No. 149, filed by the chapter 13 trustee (the "Trustee"). For the reasons set forth herein, the Court will grant the Trustee's motion.

I. BACKGROUND

Debtor filed a petition under chapter 7 on November 17, 2021. ECF No. 1. On May 6, 2022, Debtor filed Amended Schedules A/B, listing the resale value of his residential real property located at 300 Plaza Dr, Garner, NC 27529 (the "Garner Property") at $260,000.00, and claiming $35,000.00 in value of his interest in the Garner Property exempt.[1] ECF No. 60. On ***706** May 12, 2022, the Court granted Debtor's motion to convert his case to chapter 13. ECF No. 64. The Court confirmed Debtor's chapter 13 plan (the "Plan") on December 14, 2022. ECF No. 121. The Plan included a liquidation requirement of $79,705.55 under 11 U.S.C. § 1325(a)(4),[2] ECF No. 98, at 2, and provided that property of the estate would remain property of the estate, notwithstanding 11 U.S.C. § 1327(b).[3] Id. at 5. On June 15, 2023, Debtor moved to sell the Garner Property for $289,000.00, ECF No. 142, and the Court approved the sale on June 30, 2023. ECF No. 144. The sale price represents an 11.2 percent increase from Debtor's valuation on the schedules of $260,000.00, which was used about six months earlier at plan confirmation as the value of the property for

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

purposes of determining whether the Plan complied with the best interests of the creditors test under § 1325(a)(4). At the hearing on the sale motion, the Trustee requested that the net proceeds of the sale be turned over to the Trustee for payment to creditors to the extent that the proceeds exceeded Debtor's exemption. ECF No. 143, at 00:49-01:14. Because Debtor's interest in the Garner Property represented a substantial portion of the liquidation value and the Plan did not contemplate the sale of property, the Court permitted the sale but required that all net proceeds above the $35,000.00 exemption amount be held in a Sasser Law Firm Trust Account, subject to the Trustee filing a motion to modify the plan within thirty days of receiving the settlement statement from the sale closing. ECF No. 144, at 1.

The Trustee timely filed the motion to modify the plan on August 8, 2023, recommending that the Plan be modified pursuant to 11 U.S.C. § 1329: (1) to require the turnover of a minimum of $60,022.38 of the net proceeds to the Trustee for distribution to unsecured creditors; (2) to increase the liquidation requirement to $109,403.00 to include the increased post-petition liquidation value realized from the sale of the ***707** Garner Property; and (3) to require the turnover of an additional $31,319.57 of the nonexempt net proceeds to the Trustee for distribution to unsecured creditors. ECF No. 149. Debtor contends that modification should be denied because the Plan is res judicata and modification is not permitted under § 1329(b)(1). ECF No. 151. Debtor further contends that he should have "the exclusive right to use and possess estate property in chapter 13 regardless of whether the property is 'subject to depletion,' " including all proceeds of the sale, and be allowed to continue to pay the liquidation value provided under the originally confirmed plan over the life of the plan. ECF No. 151, at 1-2. The Court held a hearing on the Motion on September 18, 2023. Jennifer Harris, attorney for the Trustee, and Travis Sasser, counsel for Debtor, appeared at the hearing. At the conclusion of the hearing, the Court took the matter under advisement.

II. DISCUSSION

[1] **[2]** **[3]** The doctrine of res judicata prevents modification of a confirmed plan pursuant to § 1329(a) unless the debtor experiences a "substantial and unanticipated post-confirmation change in his financial condition." In re Murphy, 474 F.3d 143, 149 (4th Cir. 2007). The party seeking modification bears the burden of demonstrating that the post-confirmation change in the debtor's ability to pay was both substantial and unanticipated. See id.; In re Arnold, 869 F.2d 240, 242 (4th Cir. 1989) (citing In re Fitak, 92 B.R. 243, 250 (Bankr. S.D. Ohio 1988) (holding that, where the plan contemplated sale of the debtor's property 57 months into a plan and the property was sold as and when contemplated by the plan, a 20 percent appreciation in value during the first 57 months of the plan was reasonably foreseeable and did not justify overcoming res judicata)). Once res judicata is overcome, the plan can be modified if the purpose of the proposed modification is one that is identified in § 1329(a), and if the proposed modification complies with § 1329(b)(1). Murphy, 474 F.3d at 150.

A. Substantial Change

1. Ability to Pay

[4] **[5]** The Plan did not contemplate selling the Garner Property. Instead, the Plan contemplated that Debtor would retain the property in the estate and pay the equity that otherwise would have been available to creditors over the life of the Plan. Instead, Debtor moved to approve a sale of the property only five months after confirmation. See In re Stinson, 302 B.R. 828, 830-31 (Bankr. D. Md. 2003) (holding that an unanticipated sale of property, when the original plan contemplated retention of the property, constituted a substantial and unanticipated change permitting modification, and observing that "Debtors have initiated a *de facto* modification of the plan by voluntarily selling the Property and seeking to pay off their Plan obligation with the proceeds ... [and] seek[ing] to bind the Trustee to the valuation of the Property at the time of confirmation, and thus obtain the benefit of the Property's appreciation"). As a result, funds realized from the unanticipated sale of the Garner Property substantially changed Debtor's ability to pay post-confirmation. "A substantial change in circumstances can be increased income ... or receipt of a large sum of money." In re Solis, 172 B.R. 530, 532 (Bankr. S.D.N.Y. 1994) (citing Arnold, 869 F.2d at 240 and Fitak, 92 B.R. at 250; and holding that a post-confirmation sale of the debtor's business that provided the debtor substantial proceeds warranted modification of the plan). In Murphy, the Fourth Circuit held that the "money received" by the debtor from a post-confirmation sale of property was "[u]nquestionably" substantial." 474 F.3d at 152. There, the debtor, who owned $34,000 of nonexempt ***708** equity in real property, sold the real property post-confirmation for $80,000 more than its valuation on his schedules.[4] Id. at 147. The Fourth

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

Circuit held that the debtor's financial condition had improved substantially and affirmed the bankruptcy court's order requiring turnover of $30,000 [5] of sale proceeds to the trustee for distribution to unsecured creditors. Id. at 152.

Although the 11.2 percent appreciation in the value of Debtor's petition-date interest in [6] the Garner Property is proportionately smaller than the 51.6 percent appreciation in Murphy, the amount of additional funds available for creditors in this case is almost identical to the amount that was required to pay creditors in full in Murphy. Further, while the proportionate appreciation of the Garner Property alone may not have resulted in a substantial and unanticipated change in this case—especially over a longer post-confirmation period—the sale resulted in a "substantial amount of readily available cash without any debt," and therefore created a substantial change in Debtor's financial condition. Id. Other courts similarly recognize that unanticipated receipt of a substantial amount of readily available cash can constitute a substantial change for purposes of § 1329. In Fitak, for example, the Bankruptcy Court for the Southern District of Ohio found that a debtor's post-confirmation withdrawal of $16,000 from her scheduled retirement account constituted a substantial change in the debtor's financial condition. See 92 B.R. at 251. [7] "When a debtor's financial fortunes improve, the creditors should share some of the wealth." Arnold, 869 F.2d at 243. As in Arnold and Solis, the sale of the Garner Property constituted a substantial change in Debtor's ability to pay post-confirmation.

2. Protection of Creditors' Entitlement to Receive Liquidation Value Under the Plan

The conversion of estate property into cash constituted a substantial change from ***709** the perspective of the creditors. The sale of the property itself materially altered the creditors' protections embodied within the Plan. Debtor's interest in the Garner Property remained property of the estate after plan confirmation, and Debtor's nonexempt equity in the property constituted a substantial portion of the liquidation value required to be paid to creditors under the Plan. In these circumstances, the estate's interest in the real property provided protection to creditors in the event of a reconversion to chapter 7. But if an unanticipated sale of estate property is permitted and the case is later reconverted, the value promised to creditors is at risk if Debtor is granted "the exclusive right to use" the sale proceeds as he requests in his response to the Trustee's Motion. See ECF No. 151 at 1-2. Even if Debtor does not expend any of the proceeds, proceeds from a sale of the property may not constitute property of the chapter 7 estate if the case is reconverted to chapter 7. See 11 U.S.C. § 348(f)(1)(A) (property of the estate in a case converted from chapter 13 to chapter 7 consists of property of the estate as of the filing of the petition that remains in the possession of the debtor on the date of conversion); see also In re Marsh, 647 B.R. 725, 736-37 (Bankr. W.D. Mo. 2023) (recognizing that proceeds of property of the estate is a different category of property than the property itself, or there would be no need for § 541(a)(6)); In re Barrera, 22 F.4th 1217, 1223 (10th Cir. 2022) (holding in a post-confirmation conversion from chapter 13 to chapter 7 that proceeds from the post-petition, pre-conversion sale of property are not identical to the underlying property the debtor possessed on the chapter 13 petition date and, absent bad faith, do not constitute property of the chapter 7 estate under § 348(f)).

For this reason, when nonexempt proceeds from an unanticipated post-confirmation sale of property are not committed to funding the plan, "conversion or dismissal after the sale could leave creditors with less than they were entitled to in the Chapter 13 case." Keith M. Lundin, Lundin on Chapter 13, § 127.6, at ¶ 3 (2023). As attorney for the Trustee argues, there would be nothing to stop a debtor after a post-confirmation sale of estate property from spending the proceeds and allowing the case to be dismissed or converted. ECF No. 155, at 20:29-21:55; see also Lundin, § 120.3, at ¶ 45 ("[A] subsequent conversion produces a Chapter 7 estate that does not include the equity dissipated by the debtor."). Therefore, under the circumstances of this case, the sale itself was a substantial and material change in the creditors' protection as contemplated in the Plan.

B. Unanticipated Change

[6] **[7]** **[8]** The change also was unanticipated as required for modification under § 1329. The Fourth Circuit has adopted the test applied in Fitak to determine whether a change in a debtor's financial condition was unanticipated. Arnold, 869 F.2d at 243. The Fitak test asks whether a debtor's "altered financial circumstances could have been *reasonably anticipated* at the time of confirmation by the parties seeking modification." 92 B.R. at 250 (emphasis in original). Debtor's Plan contains a liquidation requirement of $79,705.55. ECF No. 121. The vast majority of this liquidation value is attributable to nonexempt equity of $63,744.36 in the Garner Property. ECF No. 149, at 1. The Plan gave no indication that Debtor intended to sell the Garner Property. "[W]here a

Chapter 13 plan provides for unsecured creditors to be paid from income earned from a business and the confirmed plan gives no indication of a debtor's intention to sell the business, a post-confirmation sale could be an unanticipated change warranting ***710** plan modification." In re Suratt, No. 95-6183-HO, 1996 WL 914095, at *2 (D. Or. Jan. 10, 1996); see also Arnold, 869 F.2d at 243 (if income increase was anticipated, debtor's expectations should have been disclosed to the bankruptcy court before the plan was confirmed). Similarly, where the liquidation value of a plan relies on property that will remain property of the estate, the liquidation of that property during the case can be an unanticipated change. See Lundin, § 127.6, at ¶ 1 ("Modification under § 1329 may be required if the debtor sells property after confirmation.").

The court in Surratt rejected the debtor's argument that the plan must specifically provide for payment to creditors of any proceeds in the event of a sale of the property:

> The logical extension of the debtor's argument here is that there must be a provision in all Chapter 13 plans requiring post-confirmation sale proceeds from property originally part of the estate to be paid to creditors, in order to preclude the debtor from receiving those funds. There is no such requirement in the Bankruptcy Code, nor has any court imposed such a requirement. 11 U.S.C. § 1329(a) is intended, in part, to provide the protection the debtor claims is missing.

1996 WL 914095, at *3. Thus, at the time of confirmation, the Trustee could not have reasonably anticipated the substantial change in Debtor's ability to pay resulting from the sale of the Garner Property.

Because the change in Debtor's post-confirmation ability to pay following the sale of the Garner Property was both substantial and unanticipated, res judicata is overcome, and the Court must consider whether the purpose of the modification is consistent with § 1329(a) and whether the modification satisfies § 1329(b)(1).

C. Purpose of Modification

[9] The purpose of the proposed modification is consistent with § 1329(a). Debtor argues that the proposed modification "exceeds the bounds of 11 U.S.C. § 1329(a)(1) which only allows for payments to be increased to a class of claims," and that Trustee's proposed modification would transform a plan that provides for payments "to be cash flowed out of ongoing disposable income ... into a liquidating plan." ECF No. 151, at 2. However, this argument is inconsistent with the text of the Bankruptcy Code and relevant caselaw.

[10] Section 1329(a)(1) provides that the trustee may request modification of the plan after confirmation to "increase or reduce the amount of payments on claims of a particular class provided for by the plan." Section 1329(a)(2) provides that the plan can be modified to "extend or reduce the time for such payments." Debtor's Plan provides for payment over time. The Trustee seeks modification to (1) require immediate turnover of the unpaid balance of the liquidation value attributable to the Garner Property established by the confirmed Plan, (2) increase the liquidation requirement to include the increased post-petition liquidation value realized from the sale of the Garner Property, and (3) require the immediate turnover of the additional nonexempt net proceeds. ECF No. 149. These modifications have the effect of increasing the amount of the distribution to unsecured creditors and to reduce the time for the payment by Debtor. A chapter 13 plan may be modified consistent with § 1329(a) to require turnover of funds that would create a "windfall" to the debtor. See Murphy, 474 F.3d at 152; infra Section III (and cases cited therein). Thus, the purpose of the modification is permitted under § 1329(a).

***711 III. COMPLIANCE WITH § 1329(b)(1).**

Section 1329(b)(1) sets out the confirmation requirements applicable to modification of plans. Of the four sections made applicable by § 1329(b)(1), Debtor asserts that the proposed modification should be denied pursuant to § 1325(a)(1), § 1325(a)(3), and § 1325(a)(4). ECF No. 151, at 1-2.

A. Section 1325(a)(1)

[11] Section 1325(a)(1) provides that a court shall confirm a plan if the plan "complies with the provisions of this chapter and with the other applicable provisions of this title." Debtor contends that the proposed plan modification violates §§ 542, 1303, 1306(b), and 1327(a). ECF No. 151, at 1. None of these

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

provisions are explicitly made applicable to modification of confirmed plans under § 1329(b)(1). Debtor asserts that they apply under the general reference in § 1325(a)(1), which § 1329(b)(1) incorporates.

Debtor does not cite authority suggesting that a debtor can use proceeds from a post-confirmation sale of estate property at the exclusion of the trustee and without court approval, and neither § 1303, nor § 363(b) permit a debtor to do so. Section 1303 provides that "[s]ubject to any limitations on a trustee under this chapter, the debtor shall have, exclusive of the trustee, the rights and powers of a trustee under sections 363(b), 363(d), 363(e), 363(f), and 363(l)." But § 363(b), as incorporated by § 1303, provides that the debtor may use, sell, or lease property of the estate "other than in the ordinary course of business" only "after notice and a hearing." As observed by Collier, although the debtor has the right to use or sell property of the estate exclusive of the trustee,

> [i]t is of equal importance, however, that the chapter 13 debtor not be allowed to dispose of property of the estate other than in the ordinary course of business during the pendency of the plan, absent consent or at least the acquiescence of the chapter 13 trustee and creditors.

8 Collier on Bankruptcy ¶ 1303.02 (16th 2023). Implicit in this observation that the creditors and trustee are entitled to be heard on the disposition of the estate's interest in property is that the estate's interest must be sufficiently protected. Here, there cannot be any dispute that Debtor's interest in the Garner Property remained property of the estate. Debtor's nonexempt equity in that interest represents a significant portion of the liquidation requirement in the Plan, and the additional nonexempt net proceeds represent a significant portion of the proposed increased liquidation requirement.

Because Debtor's interest in the Garner Property remained property of the estate post-confirmation, the interest of the estate in the property must be protected in the event that the case is reconverted to chapter 7. See supra Section II.A.2. Therefore, Debtor cannot use the proceeds from the sale of the Garner Property without court approval, and turnover of the proceeds to the Trustee does not violate § 1325(a)(1) or otherwise frustrate the "purposes and spirit of the Bankruptcy Code." ECF No. 151, at 1. On the contrary, turnover protects the expectations of the creditors in this case both before conversion and under the terms of the confirmed plan.

B. Section 1325(a)(3)

[12] The proposed modification satisfies § 1325(a)(3). Section 1325(a)(3) provides that a court shall confirm a plan if "the plan has been proposed in good faith and not by any means forbidden by law." The Fourth Circuit has held that this good faith test is satisfied when modification ***712** would prevent a debtor from receiving a "substantial windfall." Murphy, 474 F.3d at 153; see also Arnold, 869 F.2d at 242 ("Certainly Congress did not intend for debtors who experience substantially improved financial conditions after confirmation to avoid paying more to their creditors."). Other courts have similarly found good faith when the proposed modification reflects a " 'significant increase in income and a commensurately increased payout to unsecured creditors.' " In re Wetzel, 381 B.R. 247, 254 (Bankr. E.D. Wis. 2008) (quoting In re Brown, 332 B.R. 562, 566 (Bankr. N.D. Ill. 2005)). The Murphy Court found that the trustee's modification was made in good faith to prevent the debtor, who realized an $80,000 appreciation in property value by selling his house less than a year after plan confirmation, from receiving a substantial windfall. 474 F.3d at 153. As in Murphy, the Trustee here recognized that Debtor's liquidation of the substantial appreciation in property value significantly altered Debtor's ability to pay. Furthermore, in this case, permitting Debtor to expend all the proceeds to which the creditors are entitled transfers the entire risk of nonpayment to the creditors, substantially frustrates the creditors' legitimate expectations when this case was commenced and subsequently converted to avoid the chapter 7 trustee's liquidation of the property, and would be inequitable. See supra note 1. Therefore, the Trustee's proposal to increase the liquidation requirement to include the post-petition liquidation value realized from the sale of the Garner Property and to require turnover of the nonexempt proceeds was made in good faith to prevent Debtor from receiving a substantial and unanticipated windfall not contemplated in the original plan and impermissibly shifting the risk of nonpayment entirely to creditors.

C. Section 1325(a)(4)

[13] **[14]** Section 1325(a)(4) provides that a court shall confirm a plan if "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

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

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 test, generally known as the "best interests of the creditors" or "liquidation value" test, is applied using the values as of the effective date of the plan as modified. See, e.g., In re Barbosa, 236 B.R. 540, 552-53 (Bankr. D. Mass. 1999); In re Walker, 153 B.R. 565, 568-69 (Bankr. D. Or. 1993); In re Morgan, 299 B.R. 118 (Bankr. D. Md. 2003); In re Nott, 269 B.R. 250, 255 (Bankr. M.D. Fla. 2000); In re Auernheimer, 437 B.R. 405, 409 (Bankr. D. Kan. 2010); In re Taylor, 631 B.R. 346, 354 (Bankr. D. Kan. 2021) (analyzing cases and finding that the liquidation test is applied as of the date of confirmation of the modified plan, but that property acquired post-petition is not included in the best interests calculation); see also Lundin, § 126.2, at ¶ 11 ("[A] majority of reported decisions fix the effective date for best-interests-of-creditors test purposes at modification as the effective date of the plan as modified.").

Reading the phrase "effective date of the plan" to constitute the petition date ignores the plain language of the statute. Although Judge Lundin argues for a petition date valuation to "avoid vagaries of the court's scheduling of confirmation," among other potential problems associated with a roving valuation determination, he concedes that "Congress demonstrated its ability to identify the date of the petition or entry of the order for relief as the magic date for other consequences." Lundin, ***713** § 90.1, at ¶ 5.[8] Using the date of confirmation of the original plan for purposes of determining liquidation value at modification similarly is at odds with the logic of § 1329(a), "which permits modification after confirmation to reflect changes after the effective date of the original plan." Id. § 126.2, at ¶ 8. Regardless, using an earlier date—whether petition date or prior confirmation date—is irreconcilable with the holding in Murphy, which required the debtor to pay the appreciated value of the debtor's petition-date property interest to the creditors.

Thus, the effective date of the plan for purposes of this test is the date of the plan as modified. This conclusion, however, does not necessarily determine which property interests are considered for purposes of determining the liquidation value on the effective date of the modified plan, or, specifically to this case, which portion of the sale proceeds from the Garner Property should be included in that calculation. This Court agrees with the court in Taylor that the property interests to be included in the valuation as of the effective date of the modified plan include only those interests under § 541, and excludes those interests that have come into the estate post-petition under § 1306. 631 B.R. at 353. Courts have struggled to delineate this concept. In determining that the proceeds from the settlement of a post-petition personal injury claim should not be included in the calculation, the court in Taylor cites Judge Lundin and Collier for the proposition that post-petition property is excluded from this calculation. Id. at 354.

Finding an ambiguity in the operative statutes, the court in In re Barrera looked to legislative history. 620 B.R. 645, 652-53 (Bankr. D. Colo. 2020) (citing H.R. Rep. No. 103-835, at 57 (1994), as reprinted in 1994 U.S.C.A.N. 3340, 3366, for the proposition that a debtor should not be penalized for paying down equity during the chapter 13 case because to do so would "create a serious disincentive to chapter 13 filings"), aff'd 22 F.4th 1217 (10th Cir. 2022). The court recognized that "one could ... attempt to distinguish between increased equity that arises from the debtor's repayment of secured debt from an increase that results from a change in market conditions," but declined to make that distinction, finding no language in § 348(f)(1)(A) or elsewhere in the Bankruptcy Code to support such a distinction. Id.

This Court respectfully disagrees that any additional statutory language is necessary. The distinction is in the property interests at issue. Appreciation is attributable to the property interest Debtor held on the petition date, while paydown of equity is attributable to Debtor's interest in his post-petition income that would not have been property of the estate in a hypothetical chapter 7. See In re Goins, 539 B.R. 510, 511, 515 (Bkrtcy.E.D.Va. 2015) (holding that the trustee was entitled to value attributable to the appreciation of the real estate because it "was *always* property of the estate under Section 541(a)," but nevertheless allowing the debtor to retain proceeds reflecting the reduction of debt from post-petition income). This distinction is fully consistent with the policy that a debtor should be no worse off by choosing ***714** chapter 13 than he would have been by filing a chapter 7. Had the debtor in this case remained in chapter 7, he would have been entitled to the value of his exemption in the Garner Property upon its sale, and he would have been entitled to retain his post-petition income. 11 U.S.C. § 541(a)(6).[9] The creditors, in turn, had the expectation to receive the value of the Garner Property, less Debtor's exemption, but did not have an expectation that they would be entitled to further reduction of any liens by payments made by Debtor toward the debt. Both these expectations are fulfilled by allocating proceeds between these interests in the Garner Property. Further, this distinction is required in this circuit under Murphy, which held that the creditors were entitled to the appreciated value of the estate property once it is sold during the chapter 13 case.

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

For these reasons, the proposed modification satisfies § 1325(a)(4). Because the effective date of the plan is the date of modification, the liquidation value requirement includes the nonexempt net value realized from the post-confirmation sale of the Garner Property, less any principal reduction attributable to Debtor's post-petition property. Accordingly, the best interests of the creditors test requires Debtor to turn over all nonexempt net proceeds from the sale of the Garner Property to the Trustee for distribution to the unsecured creditors, less any amount of proceeds attributable to principal reduction resulting from Debtor's post-petition payments and any portion of the liquidation value previously paid to creditors in this case (the result being the "Estate Proceeds"). Neither Debtor, nor the Trustee adduced any evidence of the amount of this principal reduction, if any. The Trustee's motion indicates that $60,022.28 of the original $63,744.36 attributable to the liquidation value of the Garner Property remains unpaid, and she requests an additional $31,319.57 in proceeds be turned over for distribution to unsecured creditors pursuant to the increased liquidation requirement of $109,403.00 under the proposed modification. Accordingly, the Trustee has requested turnover of a total of $91,341.85. The parties do not dispute that the remaining net proceeds held by counsel for Debtor (after payment of Debtor's exemption at closing) is $95,063.93. Therefore, it appears that Trustee has not sought turnover of $3,722.08 of the remaining net proceeds held by Debtor's counsel and that this amount may fully account for previous payments toward liquidation value and reduction in principal. Nevertheless, the record is unclear. Therefore, the Court will permit the parties fourteen (14) days to submit a stipulation of the appropriate amounts of remaining unpaid liquidation value and any principal reduction that occurred prior to the sale as a result of payments made by Debtor after the date of the filing of the chapter 7 petition.

IV. CONCLUSION

IT IS THEREFORE ORDERED, ADJUDGED, and DECREED as follows:

1. The Trustee's Motion to Modify Plan to Require Turnover of Funds and to Increase the Liquidation Requirement is granted as provided herein;

2. The plan as modified consistent with the Trustee's Motion to increase the liquidation value of the plan to $109,403.00 is approved;

3. Contemporaneous with filing the stipulation in paragraph 4 below, Counsel for ***715** Debtor shall turn over all Estate Proceeds to the Trustee for distribution consistent with the terms of the plan as modified. If the parties do not file a stipulation as contemplated by paragraph 4, Counsel for Debtor shall turnover the undisputed portion of the Estate Proceeds based on calculations as directed herein within fourteen (14) days of the date of this order, and retain any disputed portion of the Estate Proceeds pending further order of the Court. Nothing herein shall be construed as permitting counsel to retain any portion of Estate Proceeds on any basis other than a calculation of principal reduction or previous payment of liquidation value, including without limitation an appeal or contemplated appeal of this order, absent a stay of this order.

4. The parties shall have fourteen (14) days from the entry of this order to file a stipulation of the amount of Estate Proceeds. If a stipulation is timely filed, the amount in the stipulation will be deemed incorporated herein without further order, and this order shall be deemed a final order as of the date of the filing of the stipulation. If the parties do not file a timely stipulation as contemplated in this order, the Court will conduct a hearing on November 20, 2023, at 2:00 p.m. in the United States Bankruptcy Court, Courtroom 1, 101 S. Edgeworth St., Greensboro, North Carolina 27408 to determine the amount of Estate Proceeds consistent with this order.

[END OF DOCUMENT]

SO ORDERED.

All Citations

654 B.R. 703

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

Footnotes

1 Debtor states in his response to the Trustee's Motion that the Garner Property was valued at this amount as of the filing date. ECF No. 151, at 1. But Debtor did not file Schedule A/B concurrently with the petition. Debtor's original Schedule A/B, filed on December 16, 2021, listed the value of the Garner Property as “unknown.” ECF No. 16. Debtor filed his request to convert his case from chapter 7 to chapter 13 after the chapter 7 trustee filed an application to employ a real estate broker to market the property on April 6, 2022, ECF No. 43, which the Court approved on April 11, 2022. ECF No. 46. Debtor's counsel filed a notice of appearance in the case on April 12, 2022, and a motion to convert to a case under chapter 13 on the same day. ECF Nos. 49 and 50, respectively. On May 5, 2022, Debtor filed an amended Schedule A/B which stated that the resale value of the Garner Property was $260,000.00 and, assuming a six percent cost of sale, that the current value was $244,400.00. ECF No. 60, at 1. The parties do not dispute that $260,000.00 is the appropriate valuation; however, Debtor argues that this valuation relates back to the petition date, November 17, 2021, and represents the value of the Garner Property as of the petition date. Debtor offered no evidence of this valuation; nevertheless, this valuation was used for purposes of determining the liquidation value at confirmation of the original plan.

2 The parties do not dispute that Debtor's interest in the Garner Property on the petition date represented $63,744.36 of the liquidation value reflected in the original plan. The Trustee's Motion asserts that, as of the date of the Motion, a balance of $60,022.38 remained due to unsecured creditors to meet the Plan's liquidation requirement attributable to Debtor's interest in the Garner Property.

3 North Carolina property exemptions fall into one of two categories: (1) those exemptions that “allow debtors to exempt items in full, regardless of value;” and (2) those exemptions that allow debtors “to exempt an interest in value up to a specified monetary amount in the particular item.” In re Gregory, 487 B.R. 444, 450-51 (Bankr. E.D.N.C. 2013). Under N.C. Gen. Stat. 1C-1601(a)(1), Debtor exempted $35,000.00 in value of his interest in the Garner Property. Debtor's interest in the Garner Property remained property of the estate under the terms of the Plan, notwithstanding Debtor's exemption of a portion of its value.

4 The debtor owned a condominium that he valued on his schedules at $155,000, subject to a lien of $121,000. In re Murphy, 474 F.3d 143, 147 (4th Cir. 2007). It was sold post-confirmation for $235,000. Id.

5 The trustee in Murphy only sought turnover of $30,000, rather than the full nonexempt equity, because that amount would be sufficient to pay all unsecured creditors in full. 474 F.3d at 147.

6 Section 541(a) lists those interests in property that become property of the estate. There is a difference between an interest in property and the property itself. See In re Gifford, 634 B.R. 909, 917 (Bankr. M.D.N.C. 2021) (rejecting trustee's argument that conflated debtor's interest in the property with the property itself).

7 The court in Fitak determined that the appreciation in the debtor's real property was insufficiently significant to overcome res judicata where the property was sold as contemplated under the original plan and the appreciation in value was insufficient to be deemed unexpected 56 months after confirmation. The court nevertheless held that the debtor's receipt of cash from her retirement funds constituted a substantial and unanticipated change warranting modification. 92 B.R. at 250-51. The conversion of retirement funds to cash did not change the debtor's balance sheet, but the court nevertheless held that the receipt of readily available funds warranted modification. Id. As a result, the court confirmed a modified plan that included payment to allowed unsecured claims of the value of the withdrawn retirement funds but not to include payment of the appreciation value of the property. This court respectfully disagrees with the court in Fitak to the extent that it held that these issues could be parsed once res judicata is overcome. Instead, once the court determines that modification is appropriate and res judicata has been overcome, the court must ensure that the modified

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

plan meets the requirements for confirmation under 11 U.S.C. § 1325(a), including 1325(a)(4). See 11 U.S.C. § 1329(b); see also Section III, infra.

8 Not only does Congress know how to say either "the petition date" or "the order for relief" when it means to refer to that date, but the "effective date of the plan" also does not describe the petition date under any other section of the Code. See Hall v. U.S., 566 U.S. 506, 519, 132 S.Ct. 1882, 1891, 182 L.Ed.2d 840 (2012) (" '[I]dentical words and phrases within the same statute should normally be given the same meaning.' ") (quoting Powerex Corp. v. Reliant En. Servs., Inc., 551 U.S. 224, 232, 127 S.Ct. 2411, 2417, 168 L.Ed.2d 112 (2007)).

9 This distinction also would apply to the hypothetical posed by the court in Barrera in which there is an increase in value attributable to improvements to a property made by a debtor using post-petition income. 620 B.R. at 653-54.

End of Document © 2024 Thomson Reuters. No claim to original U.S. Government Works.

KeyCite Blue Flag – Appeal Notification
Appeal Filed by BASSEL v. DURAND-DAY, 5th Cir., September 15, 2023

2023 WL 5320775
United States District Court,
N.D. Texas, Fort Worth Division.

Pam BASSEL, Appellant,
v.
Victoria Florita DURAND-DAY, Appellee.

No. 4:22-cv-0994-P
|
Signed August 18, 2023

Synopsis

Background: Trustee objected to confirmation of two Chapter 13 plans based on separate classification of student loan creditors, such that those loans were allowed to be repaid by the terms of their contracts. The United States Bankruptcy Court for the Northern District of Texas, Mark X. Mullin, J., 2022 WL 14938726, overruled trustee's objections and confirmed plans. Trustee appealed.

[Holding:] The District Court, Mark T. Pittman, J., held that debtors' repayment of student loans after conclusion of commitment period were payments made "under the plan."

Affirmed.

Procedural Posture(s): On Appeal; Objection to Confirmation of Plan.

West Headnotes (7)

[1] **Bankruptcy** Scope of review in general

In reviewing the decision of a bankruptcy court, the district court functions as an appellate court and applies the standard of review used in a federal court of appeals.

[2] **Bankruptcy** Conclusions of law; de novo review

Bankruptcy Clear error

District court reviews bankruptcy court's findings of fact for clear error and any conclusions of law de novo.

[3] **Bankruptcy** Time allowed for cure

Nondischargeable debt may be dealt with "under the plan" by maintaining payments on those debts beyond the close of Chapter 13 petition. 11 U.S.C.A. §§ 1322(b)(5), 1325(b)(1)(A).

[4] **Bankruptcy** Classification and discrimination

Chapter 13 plan may place substantially similar individual claims in particular classes provided that discrimination between classes is not unfair. 11 U.S.C.A. § 1122.

[5] **Bankruptcy** Classification and discrimination

To be "fair," discrimination between classes of claims in Chapter 13 plan must serve rational, legitimate purpose of debtor and must not favor advantaged class. 11 U.S.C.A. § 1122.

[6] **Bankruptcy** Classification and discrimination

If classification of claims in Chapter 13 plan results in a class being repaid less than the amount they would have received without discrimination between classes, discrimination between the classes is "unfair." 11 U.S.C.A. § 1122.

[7] **Bankruptcy** Time allowed for cure

Chapter 13 debtors' repayment of student loans after the conclusion of the commitment period of their respective bankruptcy plans were payments made "under the plan" for purposes of approving the plans under Bankruptcy Code, even though debtors' student loans were

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

currently in forbearance. 11 U.S.C.A. §§ 1322(b)(5), 1325(b)(1)(A), 1328(a).

Attorneys and Law Firms

Ethan Scott Cartwright, Office of the Standing Ch.13 Trustee, Hurst, TX, for Appellant.

Eric Allen Maskell, Lee Lee Law Firm PC, Hurst, TX, for Appellee.

OPINION & ORDER

Mark T. Pittman, United States District Judge

***1** Before the Court is the Memorandum Opinion and Order of the United States Bankruptcy Judge (ECF No. 5). For the reasons below, the Court **AFFIRMS** and **ADOPTS** the reasoning and opinion of the Bankruptcy Judge in Case Nos. 22-40089-MXM-13 and 22-40625-MXM-13.

BACKGROUND

This appeal arises from the approval of two Chapter 13 Bankruptcy Plans—the "Evans Plan" and the "Durand-Day Plan." Both plans call for the repayment of 100% of each Debtor's general unsecured debt over a five-year period, except for each Debtor's federal student loans.

In the Bankruptcy Court, the Debtors and the Trustee stipulated that: (1) the student loan obligations at issue are nondischargeable under 11 U.S.C. § 523(a)(8), (2) the loans are currently in deferment, and (3) by their terms, the final payments for each student loan will be due after the conclusion of the five-year commitment period in which the Debtors' general unsecured debts are paid.

The Bankruptcy Judge concluded that both Debtors had the financial resources available to repay 100% of their general unsecured debts and their outstanding student loans within the commitment period. But the Bankruptcy Judge separately classified the student loan creditors such that those loans were allowed to be repaid by the terms of their contracts. The Trustee objected to this classification on two bases: (1) this classification of the student loan creditors was unfairly discriminatory, and (2) both plans therefore failed to meet either the 100% test or the disposable-income test required by statute, since the student loan debt could have been paid within five years and less than all of the Debtors' disposable income was committed to repaying creditors.

The Bankruptcy Judge overruled the Trustee's objections and approved the plans, concluding that the separate treatment of student loan debts is authorized by statute, and since they are nondischargeable, the bankruptcy plans may provide for them to be repaid by their terms—even of those payments outlast the bankruptcy commitment period.

Neither student loan creditor objected in the Bankruptcy Court, and there is no indication that Debtors will be unable to satisfy their student loan obligations.

The Trustee now appeals.

LEGAL STANDARD

[1] **[2]** In reviewing the decision of a bankruptcy court, the district court functions as an appellate court and applies the standard of review used in a federal court of appeals. *In re Webb*, 954 F.2d 1102, 1103–04 (5th Cir. 1992). Therefore, the district court reviews the Bankruptcy Court's findings of fact for clear error and any conclusions of law de novo. *In re Dennis*, 330 F.3d 696, 701 (5th Cir. 2003).

ANALYSIS

The question is whether the Bankruptcy Court erred in determining that the repayment of Debtors' student loans after the conclusion of the commitment period were payments made "under the plan" for the purposes of approving the plans under the Bankruptcy Code. Thus, this Court reviews the Bankruptcy Court's Opinion de novo.

Chapter 13 bankruptcy is governed by 11 U.S.C. § 1328(a). 11 U.S.C. § 1328(a). Debtors may obtain discharge of their debts through a court-confirmed payment plan that directs payment of their debts out of their future income over a period of time, and the court shall grant discharge of the debts "as soon as practicable after completion ... of all payments under the plan." 11 U.S.C. § 1328(a).

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

***2** **[3]** Section 1325(b)(1)(A) provides that a plan may only be approved if the amount of a creditor's claim does not exceed "the value of the property to be distributed under the plan on account of such claim" ("the 100% test") or that all the debtor's projected disposable income over the course of the payment period be contributed to repaying unsecured creditors ("the disposable income test"). 11 U.S.C. § 1325(b)(1)(A). But § 1322(b)(5) provides that a bankruptcy plan may provide for the curing of any secured or unsecured claim within a reasonable time where "the last payment is due after the date on which the final payment under the plan is due." 11 U.S.C. § 1322(b)(5). In exchange for their compliance, the debtor is entitled to a discharge of all debt provided for by the plan except those debts provided for under § 1322(b)(5) or disallowed under other applicable sections of the Code. *Matter of Foster*, 670 F.2d 478, 484 (5th Cir. 1982). Thus, nondischargeable debt may be dealt with "under the plan" by maintaining payments on those debts beyond the close of the bankruptcy petition. *In Matter of Kessler*, 655 F. App'x 242, 244 (5th Cir. 2016).

[4] **[5]** **[6]** A plan may place substantially similar individual claims in particular classes provided that the discrimination between the classes is not unfair. 11 U.S.C. § 1122; *In re Potgieter*, 436 B.R. 739, 743 (Bankr. M.D. Fla. 2010). To be fair, the discrimination must serve a rational, legitimate purpose of the debtor and must not over-favor an advantaged class. *In re Simmons*, 288 B.R. 737, 751 (Bankr. N.D. Tex. 2003) (holding modified by *In re King*, 460 B.R. 708, 710-11 (Bankr. N.D. Tex. 2011)). If a classification results in a class's being repaid less than the amount they would have received without the discrimination between classes, the discrimination is unfair. *Id.*

[7] The unique nature of student loan debt warrants their classification under Debtors' Bankruptcy Plans. Student loan debt is not granted priority under the Bankruptcy Code—so there is no obligation that it be paid in full during a bankruptcy plan—student loans continue accruing interest during a bankruptcy plan's commitment period if a debtor ceases making payments, and Congress declared certain government educational loans nondischargeable under Chapter 13 through the Student Loan Default Prevention Initiative Act of 1990. *Potgieter*, 436 B.R. at 741. Thus, debtors have every incentive to maintain payments on student loans during the course of bankruptcy because they: (1) continue to mount interest or applicable penalties, (2) cannot be relieved, and (3) will remain on the books until they are repaid. Moreover, this classification is fair because Debtors' student loans are treated no differently than those debts which will be repaid in full during the commitment period. Here, both Debtors' classes of student loan debts and classes of their general unsecured debts will be paid in full, whether through the terms of the Plans—as in the case of the general unsecured creditors—or by the terms of the debts' contract—in the case of the student loans. *See* ECF No. 5 at 13–14. And §§ 1122, 1322, and 1325 all provide the statutory mechanisms to classify and permit the student loans to be repaid under their contracts rather than by the end of the commitment period of the bankruptcy plan. This is what the Bankruptcy Court did here: the court grouped these nondischargeable, non-priority debts together and permitted them to be repaid by their own schedule under § 1322(b)(5).

The Trustee principally challenges this practice based on the theory that—since Debtors' student loans will be in forbearance during the execution of the Plans—that Debtors' student loan payments are no longer payments "under the plan" as required by statute. *See* ECF No. 6 at 13. Summed up, the Trustee contends that "[they] have not found any courts that held that payments made after the plan ends and the case is closed are payments under the plan." *Id.* This discreet issue, argues the Trustee, causes the Plans to fail, because without repaying all their student loans within plan period, the Plans do not meet either test necessary to be approved.

***3** The Fifth Circuit has held post-plan payments made directly from debtor to creditor to constitute payments "under" their respective bankruptcy plans. *Matter of Kessler*, 655 F. App'x at 244. In *Kessler*, the debtors' Chapter 13 bankruptcy plans provided for the repayment of their pre-petition mortgage arrears and post-petition mortgage payments. *Id.* The district court denied the debtors' motion for discharge, because the post-petition mortgage payments provided for by their plans were payments *under* their plans. *Id.* Thus, discharge was improper, because § 1328(a) provides that a court may grant discharge only after completion of "*all* payments under the plan." *Id.*

Such is the case here. The fact that Debtors' student loans are currently in forbearance does not mean that their repayment will not be "payments under the plan." The Bankruptcy Court fairly classified the student loan debts and statutorily provided for those debts under Debtors' plans by permitting them to be repaid on their contractually provided schedules. Thus, the 100% test met because the value of all Debtors' unsecured claims—aside from the student loans—did not exceed the

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

sum available to repay them. The fact that Debtors' student loans are currently in forbearance does not take Debtors off the hook to repay them. And, as in *Kessler*, Debtors' student loan payments are still payments "under their plans" even if the payments continue beyond the end of the commitment period of their respective bankruptcy plans.

CONCLUSION

Having conducted a de-novo review of the Bankruptcy Judge's Memorandum Opinion and Order, the Court concludes that the opinions in case Nos. Case Nos. 22-40089-MXM-13 and 22-40625-MXM-13 ought to be and are hereby **AFFIRMED** and **ADOPTED.**

SO ORDERED on this **18th day of August 2023**.

All Citations

--- F.Supp.3d ----, 2023 WL 5320775, Bankr. L. Rep. P 83,911

End of Document © 2024 Thomson Reuters. No claim to original U.S. Government Works.

654 B.R. 762
United States Bankruptcy Court, W.D. New York.

IN RE Suzanne M. EISENBERGER, Debtor.

BK 23-10035 CLB
|
Signed October 23, 2023

Synopsis

Background: In Chapter 13 case converted from one under Chapter 7, trustee objected to confirmation of plan.

[Holding:] The Bankruptcy Court, Carl L. Bucki, Chief Judge, held that proposed Chapter 13 plan could separately classify her student loans and pay those loans outside the plan.

Objection overruled.

Procedural Posture(s): Objection to Confirmation of Plan.

West Headnotes (3)

[1] **Bankruptcy** Classification and discrimination

Bankruptcy Time for completion; extension or modification

Bankruptcy Payments outside plan

Debtor's proposed Chapter 13 plan could separately classify her student loans and pay those loans outside the plan; separate classification extended to all student loans and all such claims were substantially similar in that they were nondischargeable debts incurred for the purpose of financing educational expenses, creditors in the class of general unsecured creditors would suffer no discrimination in that they would receive payment in full within the term of the plan, proposed treatment of student loans was not unfair, in that those creditors retained the full benefit of their bargain as defined by the underlying loan agreements, and even though student loans provided for repayment over a term that extended beyond the plan's duration, debtor's plan could allow for "maintenance of payments" rather than a satisfaction of the obligation. 11 U.S.C.A. §§ 1122, 1322(b)(1), 1322(b)(5), 1325(a)(4).

[2] **Bankruptcy** Requisites of Confirmable Plan

Bankruptcy Plan

Unlike standard for confirmation of Chapter 11 plan, Bankruptcy Code provision governing confirmation of Chapter 13 plan does not provide that the court may grant confirmation "only if" certain requirements are satisfied, but rather, merely creates a safe haven for confirmation in Chapter 13 and does not mandate compliance with all of the stated criteria. 11 U.S.C.A. §§ 1129(a), 1325(a).

[3] **Bankruptcy** Order of confirmation

When bankruptcy court has discretion to consider a proposed Chapter 13 plan whose confirmation is not mandated, court may have authority to impose conditions for approval. 11 U.S.C.A. § 1325(a).

Attorneys and Law Firms

Barry H. Sternberg, Esq., Barry Sternberg Law Offices, 216 Crossfield Road, Rochester, New York 14609, Attorney for Debtor.

Julie Philippi, Esq., 170 Franklin Street, Buffalo, New York 14202, Chapter 13 Trustee.

DECISION & ORDER

Carl L. Bucki, Chief United State Bankruptcy Judge.

In this Chapter 13 case, the debtor proposes to separately classify her student loans and to pay those loans outside the plan. Objecting to confirmation, the trustee argues that the amount of non-exempt assets compels full payment of the student loans within the contemplated plan duration of five

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

years. Alternatively, the trustee seeks to require that her office serve as a conduit for payments on account of student loans.

Suzanne M. Eisenberger filed a petition for relief under Chapter 7 of the Bankruptcy Code on January 18, 2023. Soon thereafter, the Chapter 7 trustee learned that submitted schedules failed to disclose ***763** that the debtor and her father were joint owners of a corporation with significant real estate holdings. When presented with this information, Eisenberger converted her case into a proceeding under Chapter 13.

The debtor represents that she owes more than $275,000 on student loans and that her other general unsecured debts total approximately $36,000. Meanwhile, Eisenberger's counsel has stipulated "that the value of the debtor's 50% interest in the corporation exceeds the value of the total amount of unsecured debt, including the significant amount of student loan debt." At the time of bankruptcy filing, the debtor's obligation to repay her educational loans was deferred. Even if the deferments were to end, however, the loans contemplate payment over a term that would extend beyond the maximum permitted duration of any plan.

Suzanne Eisenberger acknowledges that the student loans are non-dischargeable. In her plan, she proposes monthly payments to the trustee in an amount sufficient to satisfy 100% of all allowed unsecured claims other than student loans. Placing the student loans into a separate class, the plan further states that Eisenberger "will maintain the contractual installment payments and cure any default in payments." The debtor advises, however, that she anticipates no arrears in need of cure, due to current deferments. When the deferments end, the student loans will be paid not through the trustee but directly by the debtor.

At this time, the parties seek only a decision on whether the student loans can be separately classified and paid outside the plan. The Chapter 13 trustee opposes confirmation of this proposal on the basis that it fails to satisfy the guidelines of 11 U.S.C. § 1325(a)(4). This section states in relevant part as follows:

> "Except as provided in subsection (b), the 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."

In her written submission, the trustee asserts that pursuant to this section, "the plan must provide that unsecured claims receive at least as much as those claims would receive in a hypothetical chapter 7." Because the debtor's non-exempt assets exceed the sum of all student loans and other unsecured obligations, the trustee insists that distributions under the plan must satisfy all of these claims within the plan's five year duration. Eisenberger disputes the trustee's interpretation of section 1325(a)(4) and asks that we distinguish distributions under a plan from distributions through a plan. In the debtor's view, the plan fulfills the requirements of section 1325(a)(4) by preserving the rights of educational loan creditors to enforce their non-dischargeable claims. She further contends that "there is no reason to force the liquidation of assets to pay student loan debts while the Chapter 13 case is pending."

Discussion

For cases filed under Chapter 13, section 1321 of the Bankruptcy Code directs that "[t]he debtor shall file a plan." Section 1322 then defines the required and permissible contents of such a plan. For purposes of the present dispute, subdivisions (b)(1) and (b)(5) of section 1322 establish the controlling standards.

[1] In relevant part, section 1322(b)(1) provides that a plan may "designate a class or classes of unsecured claims, as provided ***764** in section 1122 of this title, but may not discriminate unfairly against any class so designated." Thus, the separate classification of claims is allowed whenever two conditions are satisfied. First, the classification must satisfy the requirements that 11 U.S.C. § 1122 would impose for cases in Chapter 11. With an exception not here relevant, section 1122 states that "a plan may place a claim or an interest in a particular class only if such claim or interest is substantially similar to the other claims or interests of such class." Here, the separate classification extends to all student loans. As required by section 1122, all such claims are substantially similar in that they are non-dischargeable debts incurred for the purpose of financing educational expenses.

The second prerequisite for separate classification is that the designation "not discriminate unfairly." 11 U.S.C. § 1322(b)(1). Creditors in the class of general unsecured creditors will suffer no discrimination, in that they will receive payment in full within the term of the plan. Meanwhile, the proposed treatment of student loans is not unfair, in that those creditors

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

retain the full benefit of their bargain as defined by the underlying loan agreements. *See In re Potgieter*, 436 B.R. 739, 743 (Bankr. M.D.Fla. 2010).

While section 1322(b)(1) sets the limits of claim classification, section 1322(b)(5) authorizes the debtor's proposed treatment of those separately classified claims. In relevant part, this later section states that the plan may "provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due." Here, the student loans provide for repayment over a term that extends beyond the plan's duration. By reason of deferments, Suzanne Eisenberger has no existing default that needs to be cured. As authorized by 11 U.S.C. § 1322(b)(5), the debtor's plan may allow for the "maintenance of payments" rather than a satisfaction of the obligation.

[2] Notwithstanding the provisions of section 1322(b), the trustee contends that 11 U.S.C. § 1325(a)(4) compels Suzanne Eisenberger to pay her student loans in full within five years of plan confirmation. This interpretation of section 1325 is misplaced for two independent reasons. First, subdivision (a)(4) of this section is not a prerequisite for confirmation, but one of nine components which together will guarantee confirmation. Section 1325(a) begins with the directive that "[e]xcept as provided in subdivision (b), the court shall confirm a plan if" the subsequent nine conditions are satisfied. Unlike the standard in 11 U.S.C. § 1129(a) for confirmation of a plan in Chapter 11, section 1325(a) does not provide that the Court may grant confirmation "only if" certain requirements are satisfied. Rather, section 1325(a) merely creates a safe haven for confirmation in Chapter 13 and does not mandate compliance with all of the stated criteria.

Even if the trustee is correct in her argument that the proposed treatment of student loans does not comply with the conditions stated in section 1325(a)(4), the consequence would only foreclose an assurance of confirmation. Confirmation then becomes discretionary. In the present instance, however, Suzanne Eisenberger proposes the maintenance of payments in a fashion expressly allowed under 11 U.S.C. § 1322(b)(5). Unless the proposal fails some other statutory restriction, the Court may exercise its discretion to confirm a plan allowing the direct payment of student obligations under the terms of the underlying loan agreements.

***765** We also overrule the trustee's objection for a second reason. The Bankruptcy Code carefully distinguishes the concepts of distribution and payment. Thus, 11 U.S.C. § 1328(a) provides that a debtor in Chapter 13 can receive a discharge upon completion "of all payments under the plan." For instances where a case is handled by someone other than a standing trustee, the trustee's compensation is limited to a percentage of "all payments under the plan." 11 U.S.C. § 326(b). Standing trustees may collect a percentage fee from "all payments received by such individual under plans." 28 U.S.C. § 586(e)(2). In contrast, section 1325(a)(4) refers not to payments under a plan, but to distributions. So long as the debtor proposes a plan that will ultimately distribute property sufficient to satisfy the student loans according to their terms, she fulfills the requirements of section 1325(a)(4).

[3] Finally, the trustee argues that at least during the pendency of this case, the Chapter 13 office should serve as a conduit for all payments on account of the student loans. Such a request is premature. The trustee has not closed the meeting of creditors and has reserved the opportunity to present other objections to the plan. In particular, aside from our ruling with regard to 11 U.S.C. § 1325(a)(4), we have yet to consider whether the debtor has satisfied the other conditions of section 1325(a). To the extent that Eisenberger satisfies those conditions, unless countermanded by the limitations of 11 U.S.C. § 1325(b), the Court must confirm the debtor's proposal. Under that circumstance, we see no basis to mandate a conduit payment of the student loans. A respected treatise concurs. When confirmation is dictated by section 1325(a), "[t]he court may not add additional requirements for confirmation." 8 COLLIER ON BANKRUPTCY ¶1325.01 (Richard Levin & Henry J. Summer eds., 16th ed. 2023). On the other hand, when the Court has discretion to consider a plan whose confirmation is not mandated under section 1325(a), we may have the authority to impose conditions for approval. Accordingly, until we decide whether plan confirmation is mandated or merely permissive, we are not positioned to consider the trustee's request for conduit payments.

Conclusion

For the reasons stated herein, the trustee's objection to plan confirmation is overruled. Accordingly, the Court will give due consideration to a plan that separately classifies student loans and that allows for the debtor to make direct payment

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

on account of those claims according to their terms. The trustee is granted leave to present other or further objections to confirmation. For this purpose and to consider any timely request to mandate conduit payments through the trustee on account of the student loans, a further hearing on confirmation shall be held at 11 A.M. on November 7, 2023.

So ordered.

All Citations

654 B.R. 762

End of Document © 2024 Thomson Reuters. No claim to original U.S. Government Works.

640 B.R. 781
United States Bankruptcy Court, D. Massachusetts.

IN RE: Russell K. MATERNE, Debtor
In re: Dominique J. Gnaman, Debtor

Case No. 20-40027-CJP, Case No. 19-40930-CJP
|
Signed April 7, 2022

Synopsis
Background: Secured creditors objected to confirmation of Chapter 13 plans in unrelated cases.

Holdings: The Bankruptcy Court, Christopher J. Panos, Chief Judge, held that:

[1] Chapter 13 plan providing for lump-sum payment after periodic payments and not providing for specific sale process that would pay creditor's allowed secured claim at, or reasonable time after, confirmation could not be confirmed, and

[2] Chapter 13 plan calling for payments that were less than contractual amount due until sale that was to occur at unspecified time during life of plan proposed impermissible modification of rights of secured creditor.

Objections sustained.

Procedural Posture(s): Objection to Confirmation of Plan.

West Headnotes (24)

[1] Bankruptcy Evidence

Burden is on Chapter 13 debtor to prove that each of the statutory criteria for confirmation is met. 11 U.S.C.A. § 1325(a).

[2] Statutes Language

Presumption generally exists that Congress means what it says in statute.

[3] Statutes Construction as written

Statutes Plain Language; Plain, Ordinary, or Common Meaning

Statutes Relation to plain, literal, or clear meaning; ambiguity

When statute's language is plain, sole function of courts, at least where disposition required by text is not absurd, is to enforce it according to its terms.

[4] Statutes Plain Language; Plain, Ordinary, or Common Meaning

Unless sufficient indication to the contrary, words in a statute will be interpreted taking their ordinary, contemporary, common meaning.

[5] Statutes Context

In interpreting the plain language of a statute, a court may look to the specific context in which the language is used, and the broader context of the statute as a whole.

[6] Bankruptcy Valuation; periodic payments

In a case under Chapter 13, while the prospect of a sale may be an issue with respect to other confirmation requirements, such as a plan's feasibility, providing for payment of a secured claim through a sale does not per se violate the statutory provision for the value of any property to be distributed under the plan on account of the secured claim to be not less than the allowed amount of the claim. 11 U.S.C.A. §§ 1325(a)(5)(B)(ii), 1325(a)(6).

3 Cases that cite this headnote

[7] Bankruptcy Modification of claim, right, or debt in general

In a Chapter 13 case, a secured creditor's rights protected from modification by the Bankruptcy Code's anti-modification provision are the rights under the original loan instruments as defined by state law. 11 U.S.C.A. § 1322(b)(2).

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

[8] **Bankruptcy** Curing Defaults

A Chapter 13 debtor may cure defaults of obligations that matured prepetition or that mature during the plan term. 11 U.S.C.A. §§ 1322(b)(3), 1322(c)(2).

[9] **Bankruptcy** Mortgages in general

Bankruptcy Time allowed for cure

A cure of a long-term mortgage may be permitted where a Chapter 13 debtor proposes to pay the claim in full on an accelerated basis within the plan term. 11 U.S.C.A. §§ 1322(b)(3), 1322(c)(1).

[10] **Bankruptcy** Curing Defaults

Bankruptcy Time allowed for cure

In a Chapter 13 case, the curing of prepetition arrears on long-term debt in default as of the petition date is allowed provided debtor postpetition: (1) cures the default within a reasonable time and (2) stays current on postpetition payments due under the parties' original agreement. 11 U.S.C.A. §§ 1322(b)(2), 1322(b)(5).

[11] **Bankruptcy** Security interests in principal residences

Chapter 13 plan that does not provide for maintenance payments, and only provides for sale within time period covered by plan that contemplates use of proceeds to pay off mortgage, would impermissibly modify secured creditor's rights. 11 U.S.C.A. § 1322(b)(5).

1 Case that cites this headnote

[12] **Bankruptcy** Liens securing claims not allowed

Bankruptcy Secured Claims; Cram Down

In a Chapter 13 case, where a fully-secured claim is "bifurcated" by the Bankruptcy Code for purposes of plan treatment into arrears that may be cured and the balance of the claim that will be maintained, the underlying nature of the allowed secured claim is not altered. 11 U.S.C.A. § 1325(a)(5).

[13] **Bankruptcy** Secured Claims; Cram Down

In a Chapter 13 case, the entirety of a debt that is fully secured constitutes the "allowed secured claim," and a plan that does more than state that the rights of the holder of that secured claim are not affected in any way by the plan "provides for" the treatment of that claim. 11 U.S.C.A. § 1325(a)(5).

2 Cases that cite this headnote

[14] **Bankruptcy** Curing Defaults

A Chapter 13 plan proposing to cure arrearages and maintain payments "provides for" treatment of such a claim, making satisfaction of the statutory provision for accommodating each creditor with an allowed secured claim a requirement of confirmation. 11 U.S.C.A. § 1322(b)(5).

[15] **Bankruptcy** Security interests in principal residences

Bankruptcy Home mortgages or similar obligations

Chapter 13 plan providing for lump-sum payment after periodic payments and not providing for specific sale process that would pay creditor's allowed secured claim on principal residence at, or reasonable time after, confirmation could not be confirmed. 11 U.S.C.A. §§ 1322(b), 1325(a)(5)(B)(iii).

1 Case that cites this headnote

[16] **Bankruptcy** Security interests in principal residences

Chapter 13 plan calling for payments on principal residence that were less than contractual amount due until sale that was to occur at unspecified time during life of plan

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

proposed impermissible modification of rights of secured creditor, and therefore it could not be confirmed. 11 U.S.C.A. §§ 1322(b)(2), 1322(b)(3), 1322(b)(5).

[17] **Bankruptcy** Valuation; periodic payments

In a Chapter 13 case, a secured claim may be paid in full through a sale that is in prospect at the time of confirmation or a reasonable time thereafter, subject to all other confirmation requirements such as feasibility and good faith. 11 U.S.C.A. §§ 1322(b)(8), 1325(a)(5).

[18] **Bankruptcy** Security interests in principal residences

In a Chapter 13 case, a debtor may sell his or her principal residence during the life of a traditional "cure and maintain" plan and pay the secured claim in full from proceeds of that sale. 11 U.S.C.A. §§ 1322(b)(8), 1325(a)(5).

1 Case that cites this headnote

[19] **Bankruptcy** Amount of Repayment; De Minimis Repayment

In a Chapter 13 case, the equal payment provision prohibits confirmation of a sale plan, over the objection of a secured creditor holding a mortgage of a principal residence, that contemplates periodic payments followed by a lump-sum payment. 11 U.S.C.A. § 1325(a)(5)(B)(iii).

2 Cases that cite this headnote

[20] **Bankruptcy** Valuation; periodic payments

Bankruptcy Time allowed for cure

In a Chapter 13 case, a non-consensual plan that provides for a secured claim to be paid in full through a sale that is in prospect at the time of, or at a reasonable time after, confirmation, with or without payments prior to the sale, may be confirmed subject to all other confirmation requirements such as feasibility and good faith. 11 U.S.C.A. §§ 1322(b)(8), 1325(a)(5).

[21] **Bankruptcy** Claims and assets; propriety and feasibility in general

To meet burden of demonstrating feasibility of Chapter 13 plan that proposes sale of collateral to satisfy secured claim, debtor may need to provide evidence as to marketing efforts, terms of sale, and generally show that debtor is motivated to effectuate sale process, as well as disclosing any other factors which may impact payment of claim. 11 U.S.C.A. §§ 1322, 1325.

[22] **Bankruptcy** Factors considered in determining presence of good faith

Although the test of whether a Chapter 13 plan has been proposed in good faith cannot be reduced to a mechanical checklist, courts consider: (1) debtor's accuracy in stating her debts and expenses, (2) debtor's honesty in the bankruptcy process, including whether she has attempted to mislead the court and whether she has made any misrepresentations, (3) whether the Bankruptcy Code is being unfairly manipulated, (4) the type of debt sought to be discharged, (5) whether the debt would be dischargeable in a Chapter 7, and (6) debtor's motivation and sincerity in seeking Chapter 13 relief. 11 U.S.C.A. § 1325(a)(3).

[23] **Bankruptcy** Good Faith in General

Good faith, as required to confirm a Chapter 13 plan, ultimately is a concept, not a construct, that derives from equity. 11 U.S.C.A. § 1325(a)(3).

[24] **Bankruptcy** Factors considered in determining presence of good faith

While the proposal of a sale plan alone is insufficient to establish bad faith that would prevent confirmation of a Chapter 13 plan, a sale plan proposing sale periods that could run through the last month of the term of the plan, unaccompanied by milestones related to actual efforts to sell, such as the hiring of a broker or the listing of the property by a date certain,

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

> and the accrual of significant postpetition arrears, may constitute circumstances from which a lack of good faith might be inferred. 11 U.S.C.A. § 1325(a)(3).

Attorneys and Law Firms

***783** Robert W. Kovacs, Jr., Kovacs Law, P.C., Worcester, MA, for Debtor.

MEMORANDUM OF DECISION

Christopher J. Panos, United States Bankruptcy Judge

Before the Court are objections by secured creditors to confirmation of Chapter 13 plans in two unrelated cases. While the plans and the confirmation objections of the secured creditors are not identical, the cases share certain common issues presented by Chapter 13 "sale" plans, pursuant to which a debtor treats the claim of a secured creditor, including prepetition arrears, by proposing to sell the debtor's principal residence that secures the mortgage during the term of the plan. In the plans before me, the debtors do not specify a time for the sales to occur, such that the sales could take place at any time before the respective plan terms expire. As the objections to confirmation raise overlapping legal issues related to sale plans, I am issuing a single memorandum of decision to address the issues together. For the reasons set forth below, I will sustain ***784** the objections of the secured creditors in each of the cases. [1]

I. FACTS AND PROCEDURAL HISTORY

A. Dominique J. Gnaman

On June 6, 2019, Dominque J. Gnaman filed a petition for relief under Chapter 13 of the Bankruptcy Code. Wilmington Trust, NA, successor trustee to Citibank, N.A., as Trustee for Structured Asset Mortgage Investments II Inc., Bear Stearns ALT-A Trust, Mortgage Pass-Through Certificates, Series 2006-4 ("Wilmington") is the current holder of the first mortgage of the real property located at 102 Jordan Road, Franklin, Massachusetts (the "Franklin Property"). The debtor owns the single-family Franklin Property individually and values it at $553,655.00 on Schedule A/B. There is no dispute that this is Mr. Gnaman's principal residence. On Schedule C, Mr. Gnaman claims a homestead exemption in the Franklin Property in the amount of $500,000.00 under Mass. Gen. Laws ch. 188, § 3. Wilmington, through its servicer, Select Portfolio Servicing, Inc., filed a secured proof of claim in the amount of $411,417.95, including prepetition arrears of $206,561.84.

Wilmington objects (Case No. 19-40930, Dkt. No. 36) to confirmation of the Chapter 13 plan (Case No. 19-40930, Dkt. No. 26) proposed by Mr. Gnaman. [2] Mr. Gnaman seeks to cure his prepetition arrears by selling the property that secures Wilmington's mortgage at any time up to the conclusion of the plan's 60-month term. The plan provides that, until the property is sold, Mr. Gnaman will pay contractual monthly mortgage payments directly to Wilmington. Mr. Gnaman proposes to pay Wilmington the full amount of its claim from proceeds of the proposed sale. Wilmington objects to this treatment, asserting that it violates §§ 1325(a)(3), (a)(5), and (a)(6) and 1322(b)(5) of the Bankruptcy Code. [3]

Mr. Gnaman addresses Wilmington's secured claim in two sections of his plan, each of which must be considered to determine Wilmington's plan treatment. Part 3.A.2 of the plan, *Maintenance of Contractual Installment Payments (To Be Paid Directly to Creditors)*, provides that Mr. Gnaman will directly maintain contractual mortgage payments to Select Portfolio Servicing, Inc. [4] "outside" of the plan, meaning that the debtor will make the payments directly to the mortgagee, instead of through the Trustee as a conduit. [5] ***785** Additionally, in Part 8.6 of the plan, *Nonstandard Plan Provisions*, the debtor proposes to pay the balance of the mortgage claim of Wilmington in a lump sum (sometimes called a "balloon payment"), including prepetition arrearages, through the sale of the Franklin Property. Mr. Gnaman's plan specifically provides that:

> Subject to further order of the Court[,] the Debtor is to sell his real property located at 102 Jordan Rd., Franklin, MA 02038-1219[.]

Proceeds of the sale shall be distributed as follows:

> (1) To pay any secured claim against the property[,] including a mortgage to Select Portfolio Servicing, Inc[;]

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

(2) To pay any expenses associated with a real estate transaction, including but not limited to, attorney's fees, closing costs, realtor commissions;

(3) Any exempt funds shall be retained by the debtor; and

(4) Any non-exempt funds shall be turned over the standing trustee to pay creditors.

Gnaman Plan 6, Part 8.6.

Mr. Gnaman left Part 3.A.1 of the plan blank, which references "prepetition arrears to be paid through this plan." There is also no timetable associated with the sale of the Franklin Property, so Mr. Gnaman is proposing to retain the Property for a period of up to 60 months in which he would sell the Franklin Property and pay Wilmington's claim balance from the sale proceeds of its collateral. The debtor does not provide for any alternative treatment of Wilmington's claim if the Franklin Property is not sold during the 60-month plan period.

There does not appear to be any sale presently in prospect. Mr. Gnaman has never sought to employ a broker to list the Franklin Property in his case. Wilmington also asserts, upon information and belief, the property is not listed for sale.

In its objection, as supplemented by its additional briefing, Wilmington objects to the plan on numerous grounds.[6] Specifically, Wilmington argues that (i) cure of Mr. Gnaman's default under a 60-month sale plan is an unreasonable period of time and, because it is does not provide for cure "within a reasonable time," runs afoul of the anti-modification provision of § 1322(b)(2); (ii) the "balloon" payment contemplated through the sale to cure the prepetition arrears violates § 1325(a)(5)(B)(iii)(I) requiring periodic payments to be in "equal amounts"; (iii) the plan is not feasible under § 1325(a)(6) given the lack of movement toward a sale or guideposts for progress regarding the sale process; and (iv) the plan is not proposed in good faith pursuant to § 1325(a)(3) for those same reasons.

***786 B. Russell K. Materne**

On January 7, 2020, Russell K. Materne filed a petition for relief under Chapter 13 of the Bankruptcy Code. Bank of America, National Association ("BoA") holds both the first and second mortgages of the real property located at 140 Oak Knoll Road, Carlisle, Massachusetts (the "Carlisle Property"). The debtor owns the single-family Carlisle Property with his non-filing spouse as tenants by the entirety and values his interest at $1,320,000.00 on Schedule A/B. There is no dispute that this is Mr. Materne's principal residence. On Schedule C, Mr. Materne claims a homestead exemption in the Carlisle Property in the amount of $500,000.00 under Mass. Gen. Laws ch. 188, § 3. BoA, through its servicer, PNC Bank, National Association ("PNC Bank"), filed a secured proof of claim for the first mortgage in the amount of $889,187.51, including prepetition arrears of $243,367.33. BoA filed a secured proof of claim for its second mortgage in the amount of $82,463.70, including prepetition arrears of $8,373.42.

BoA has filed two separate objections to confirmation, (Case No. 20-40027, Dkt. No. 50, the "First Mortgage Objection")[7] and (Case No. 20-40027, Dkt. No. 68, the "Second Mortgage Objection"), of the debtor's Chapter 13 plan (Case No. 20-40027, Dkt. No. 25).[8] Mr. Materne proposes to cure his prepetition arrears by selling the property that secures BoA's first and second mortgages at any time prior to the conclusion of the plan's 36-month term. Until the property is sold, Mr. Materne proposes to make monthly "adequate protection" payments to BoA in amounts less than the monthly payments provided under BoA's first mortgage and less than the amount of the monthly escrow for insurance and real estate taxes required by that mortgage. In the First Mortgage Objection, BoA objects to this treatment, asserting that it violates §§ 1325(a)(1), (a)(3), (a)(5), and (a)(6) and 1322(b)(2). In the Second Mortgage Objection, BoA does not focus on specific provisions at issue, but generally references §§ 1322 and 1325 and objects to the fact that, although the plan proposes a sale, there is no time limit on the sale term and no realtor has been retained.[9]

With respect to the specific treatment of BoA under his plan, Mr. Materne marked "none" in Part 3 of the plan governing secured claims and addresses the BoA claims entirely in Part 8 of his plan, *Nonstandard Plan Provisions*. In Part 8.7 of the plan, which the debtor captions "[t]reatment of secured lender mortgage / sale [p]lan," the debtor notes that he and his non-filing spouse will sell the Carlisle Property, which will be subject to further order of the Court, and that the claims of BoA, including prepetition arrearages, will be paid in a lump sum from the proceeds of such sale. The plan specifically provides that:

Proceeds of the sale shall be distributed as follows:

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

***787** (1) To pay any secured claim against the property[, u]pon information and belief there is a first and second mortgage held against the [Carlisle Property] to Pnc Mortgage[;]

(2) To pay any expenses associated with a real estate transaction, including but not limited to, attorney's fees, closing costs, realtor commissions;

(3) The non-filing spouse shall retain her 50% interest in the net sale proceeds;

(4) Any exempt funds shall be retained by the debtor; and

(5) Any non-exempt funds, to the extent necessary to pay claims, shall be turned over the standing trustee to such creditors.

Materne Plan 5. Additionally, in Part 7.a of the plan, Mr. Materne proposes the following "Adequate Protection/ Maintenance Payments" to PNC Mortgage and BoA [10]:

The Chapter 13 Trustee is to make monthly adequate protection / maintenance payments to the secured lender in the amount of $1,525.50 per month. Said payment shall include impounding for property tax and property insurance.

The adequate protection payment shall cease upon the earliest of (1) dismissal of the case, (2) [conversion] of the case to another chapter, (3) the filing of a further amended plan, (4) [a]pproval by the Court of a [h]ome loan [m]odification, (5) Order of the Court to cease the payments on the [m]otion of the [d]ebtor or other interested party, [or] (7) [t]he Court granting relief from the automatic stay as to the subject property.

Id. [11]

There is no timeline proposed for the sale of the Carlisle Property, so Mr. Materne is proposing to retain the Carlisle Property for a period of up to 36 months during which he and his non-debtor spouse would sell the property and pay BoA's claims in full from the sale proceeds. The debtor does not provide for any alternative treatment of BoA's claims if the Carlisle Property is not sold during the plan term. With respect to the first mortgage, BoA states that the monthly post-petition mortgage payments total $4,727.63 and that the proposed adequate protection payments of $1,525 do not cover the tax and insurance escrow amount of $1,931.70.

There does not appear to be any sale presently in prospect regarding the Carlisle Property. Mr. Materne notes he has been "self-marketing" the property since the commencement of the case and that he is working on unspecified improvements to the property "to make it more marketable." Materne Br. 3 (Case No. 20-40027, Dkt. No. 89). In his response to the First Mortgage Objection, Mr. Materne states he has employed a real estate broker, *see* Materne Resp. ¶ 3 (Case No. 20-40027, Dkt. No. 53), but the debtor has not filed any application with the Court seeking to employ a broker and never mentioned an outside broker in his supplemental briefing. In the First Mortgage Objection, BoA asserts that pursuant to an internet search conducted at the time of the objection, the Carlisle Property is not listed for sale.

In the First Mortgage Objection, as supplemented, [12] BoA argues that (i) Mr. Materne's ***788** attempt to reduce contractual payments and cure the prepetition default through a sale is a modification that violates the anti-modification provision of § 1322(b)(2), citing, among other cases, *Nobelman v. Am. Sav. Bank*, 508 U.S. 324, 113 S.Ct. 2106, 124 L.Ed.2d 228 (1993), and disputing Mr. Materne's contention that the claim is being paid in full without modification under § 1325(a)(5)(B); (ii) the proposed adequate protection payments are impermissible and Mr. Materne's reliance on §§ 361, 362 and § 1322(b)(11) to support such payments is misplaced; (iii) the plan is not feasible under § 1325(a)(6) given no timeline is included for the sale and lack of concrete progress towards a sale, notwithstanding the debtor's purported self-marketing of the property; and (iv) the plan is not proposed in good faith pursuant to § 1325(a)(3) for those same reasons. In the Second Mortgage Objection, in addition to general objections as to the unlimited sale term and lack of progress toward a sale, BoA asks for clarification of the "amount of adequate protection to be paid to each creditor while [a] sale is attempted." Second Mortg. Obj. ¶ 5 (Case No. 20-40027, Dkt. No. 68). Mr. Materne responded that he was "unable to respond to the request of the lender for clarification." Materne Resp. ¶ 5 (Case No. 20-40027, Dkt. No. 70).

II. JURISDICTION

This Court has jurisdiction over confirmation of a plan, which arises under the Bankruptcy Code, pursuant to 28 U.S.C. §§ 157(a) and 1334 and Rule 201 of the Local Rules of the United States District Court for the District of Massachusetts. The confirmation of a plan and the objections thereto are core

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

proceedings within the meaning of 28 U.S.C. § 157(b)(2)(A) and (L). Accordingly, I have authority to enter a final order with respect to each of confirmation objections in these matters.

III. DISCUSSION

[1] A court shall confirm a Chapter 13 plan if it meets all of the confirmation requirements of § 1325(a) and complies with the rest of the Code. *See* 11 U.S.C. § 1325(a)(1). "[T]he burden is on the debtor to prove that each of the statutory criteria for confirmation is met." *Austin v. Bankowski*, 519 B.R. 559, 563 (D. Mass. 2014).

The debtors' plans provide that the secured claims of Wilmington and BoA, respectively, including amounts necessary to cure prepetition arrearages, will be paid in full through a sale at some unspecified time during the term of the plan. Each of the debtors request that his plan be confirmed over the secured creditors' objections and attempt to cure prepetition arrearages through a sale, although in Mr. Materne's case, the debtor takes great care to avoid characterizing his treatment of BoA's claims as a "cure" of prepetition arrears. [13] Both debtors contend that their ***789** plans appropriately treat the claims of the secured creditors under § 1325(a)(5)(B), to the extent applicable, by providing for full payment of the secured claims. The debtors also each assert that subparagraph (iii)(I) of § 1325(a)(5)(B) (which shall be referred to herein as the "equal payments provision") is not triggered because payments are being made pursuant to the sale and not in monthly periodic payments. As to the Gnaman plan, presumably the debtor views contractual maintenance payments being paid directly by the debtor, as opposed to through the Trustee, as meaning the claim is not "provided for by the plan." Mr. Materne contends that his proposed "adequate protection" payments are not subject to the equal payments provision because, while intended to be made by the Chapter 13 Trustee from plan payments, he does not intend those payments to be periodic payments to cure or maintain BoA's secured claim.

With respect to the Wilmington objection, Mr. Gnaman also acknowledges in his supplemental brief that the plan is silent as to which subsection of § 1322 governs the plan's cure and maintain provisions, but clarifies that, in addition to § 1322(b)(5), "the Debtor is also treating the mortgage claim under [§ 1322(b)(3) and (8)]." Gnaman Br. 5 (Case No. 19-40930, Dkt. No. 66). With respect to the First Mortgage Objection, Mr. Materne claims that he is not treating the BoA claims under §§ 1322(b)(2), (b)(3), or (b)(5) and that by paying the claims in full, he does not need to look to the permissive provisions of § 1322 to propose a confirmable plan, but that, if necessary, § 1322(a)(8) supports his proposed treatment of the secured claims. Mr. Materne contends that the plan otherwise complies with § 1325(a)(5)(B) by paying the claims in full upon sale. *See* Materne Br. 5 (Case No. 20-40027, Dkt. No. 89). With respect to the adequate protection payments, Mr. Materne argues that the payment in no way modifies the claim and that § 1322(b)(2) would be satisfied, because the contractual payment amounts are not being altered, they are just "delayed" until the property is sold. *Id.* at 6–7. Mr. Materne asserts that adequate protection payments less than the full monthly contractual amount are appropriate pursuant to § 1322(b)(11), the catch-all provision that allows a debtor to "include any other appropriate provision not inconsistent with this title" in a plan. *Id*.

Each debtor argues that the unrestricted duration of obtaining a sale over the life of a Chapter 13 plan is appropriate, arguing that the only temporal limitation under the Bankruptcy Code to effectuate a "cure through sale" is the statutory plan term limit under § 1322(d). Presumably, the debtors' contention that § 1322(b)(5) is not applicable to their proposed treatments of the secured creditors are intended to bolster this argument because I would not need to examine the "reasonable time" or "maintenance of payments" components of that provision in analyzing whether the plans could be confirmed over the objections of the secured creditors. Because the sale plans filed by these debtors illustrate common issues presented by Chapter 13 plans where debtors attempt to retain possession of their homes pending a sale, but are unable or unwilling to propose "cure and maintain" plans that provide for cure of prepetition arrearages in equal payments over the life of a plan and maintenance of postpetition contractual payments, I address them together to provide guidance as to how I will apply the statute in considering confirmation of similar plans ***790** and to set out my analysis should any party wish to seek appellate review to provide further clarity with respect to these issues.

A. Application of §§ 1322(b) and 1325(a)(5)

"Sections 1322 and 1325 establish, respectively, the content and methods of confirming a proposed reorganization plan." *Wells Fargo Bank, N.A. v. Sagendorph (In re Sagendorph)*, 562 B.R. 545, 547 (D. Mass. 2017). Provisions of the Bankruptcy Code governing confirmation of a Chapter 13 plan have been subject to varying judicial interpretation, and the amendments to the Code provided in Bankruptcy Abuse

Prevention and Consumer Protection Act of 2005 (BAPCPA) appear to have further muddied the waters.[14] Given the wide-ranging interpretations of the same provisions by courts, confirmation options for debtors are not uniformly defined.[15] For example, the equal periodic payment amendment incorporated into § 1325(a)(5)(B)(iii)(I) has been interpreted as both prohibiting and permitting balloon payments at the end of plan terms. *Compare Hamilton v. Wells Fargo Bank, N.A. (In re Hamilton)*, 401 B.R. 539, 541, 543 (B.A.P. 1st Cir. 2009) (determining "a balloon payment is not equal to the payment that preceded it, and thus violates § 1325(a)(5)(B)(iii)(I)"); *In re Benedicto*, 587 B.R. 573, 576 (Bankr. S.D. Fla. 2018) (holding "[t]o find that the final payment is not recurring, and therefore is not periodic, is a stretch") *with In re Cochran*, 555 B.R. at 898 (concluding provision does not prohibit balloon payments; "[a] balloon payment satisfies the debt in full, and thus by definition cannot be repeated periodically, whether in equal amounts or otherwise"). Additionally, the difference between a debtor's ability to cure pursuant to §§ 1322(b)(3) and (b)(5) and the relationship of those provisions with the prohibition against modifying debts secured by a debtor's principal residence has also been the subject of differing legal conclusions. *Compare, e.g., Anderson v. Hancock*, 820 F.3d 670, 674 (4th Cir. 2016) (embracing a narrow view of a debtor's ability to cure defaults under §§ 1322(a)(3) and (5)) *with Di Pierro v. Taddeo (In re Taddeo)*, 685 F.2d 24, 27 (2d Cir. 1982) (concluding that "the power to 'cure any default' granted in [§] 1322(b)(3) and (b)(5) is not limited by the ban against 'modifying' home mortgages in [§] 1322(b)(2) because we do not read 'curing defaults' under (b) (3) or 'curing defaults and maintaining payments' under (b)(5) to be modifications of claims."); *In re McDonald*, 397 B.R. 175, 178 (Bankr. D. Me. 2007) (holding that "§ 1322(e) did nothing to upset [the] determination [in ***791** *Rake v. Wade*, 508 U.S. 464, 113 S.Ct. 2187, 124 L.Ed.2d 424 (1993)] that a cure proposal under § 1322(b)(5), with or without interest, is a proposal to modify a secured claim under a plan. As such, it must meet the requirements of § 1325(a)(5)"). One commentator has also raised the question as to whether a secured claim having a term longer than the plan term can be properly addressed by a debtor's "compliance with § 1322(b)(5) without also being entitled to satisfaction in one of the three ways provided in § 1325(a)(5)." Lundin on Chapter 13, § 78.4, at ¶ 18 (speculating that "Congress just overlooked the need for a cross-reference to § 1322(b)(5) in the list of ways to satisfy an allowed secured claim holder in § 1325(a)(5)"); *In re Gordon*, 217 B.R. 973, 975–76 (Bankr. S.D. Ga. 1997) (harmonizing §§ 1325(a)(5) and 1322(b)(5) in considering the treatment of a secured IRS claim by concluding that that the "total value distributed to the [secured creditor], therefore, is the cash reduction in the principal balance which was owed on the date of filing and a nondischargeable unpaid balance [and c]ombining these two value components meets the requirements of § 1325(a)(5)," but recognizing the awkwardness of that construction.). In considering the confirmation objections to the plans in these cases, I must wade into these muddy waters and address the circumstances of when a "sale" plan may be confirmed over the objection of a home mortgage lender.

[2] **[3]** **[4]** **[5]** Determination of the objections to confirmation of the "sale" plans in these cases require me to construe several provisions of both §§ 1322 and 1325. A presumption generally exists that Congress means what it says in a statute. *See, e.g.*, *Montreal, Maine & Atlantic Railway, Ltd.*, 558 B.R. 473, 491 n.16 (B.A.P. 1st Cir. 2016), *aff'd*, 953 F.3d 29 (1st Cir. 2020) (" '[C]ourts must presume that a legislature says in a statute what it means and means in a statute what it says there.' ") (quoting *Conn. Nat'l Bank v. Germain*, 503 U.S. 249, 253–54, 112 S.Ct. 1146, 117 L.Ed.2d 391 (1992) (collecting authorities)). "[W]hen the statute's language is plain, the sole function of the courts—at least where the disposition required by the text is not absurd—is to enforce it according to its terms." *Lamie v. U.S. Tr.*, 540 U.S. 526, 534, 124 S.Ct. 1023, 157 L.Ed.2d 1024 (2004) (quotation and citation omitted). Unless "sufficient indication to the contrary," words will be interpreted "taking their ordinary, contemporary, common meaning." *Pioneer Inv. Servs. Co. v. Brunswick Assocs. Ltd. P'ship*, 507 U.S. 380, 388, 113 S.Ct. 1489, 123 L.Ed.2d 74 (1993) (quotation and citation omitted). In interpreting the plain language of the statute, I also look to "the specific context in which the language is used, and the broader context of the statute as a whole." *Robinson v. Shell Oil Co.*, 519 U.S. 337, 341, 117 S.Ct. 843, 136 L.Ed.2d 808 (1997).

As discussed, § 1325(a) provides that the court shall confirm a Chapter 13 plan if that plan meets the requirements set out in that section. *See* 11 U.S.C. § 1325(a). With respect to each allowed secured claim "provided for by the plan," § 1325(a)(5) enumerates three alternative options, for a debtor proposing a plan, only one of which must be satisfied: (i) obtain the acceptance of the holder of the secured claim, § 1325(a)(5)(A), (ii) satisfy the conditions of "cramdown" by providing in the plan that the holder of the allowed secured claim will retain its lien and receive distributions under the plan having a present value equal to the amount of the allowed secured claim, § 1325(a)(5)(B), or (iii) surrender the

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

property securing such claim to the holder, § 1325(a)(5)(C). Here, the secured creditors object to and, therefore, do not accept their proposed treatment under the respective ***792** plans. Additionally, neither plan provides for surrender of the property securing the mortgage loans. To be confirmed, only one option remains—the Plan must satisfy the conditions of § 1325(a)(5)(B), which allows a debtor to provide for the treatment of a secured claim over objection of the secured creditor if certain criteria set forth in subsections (i), (ii), and (iii) of § 1325(a)(5)(B) are met.

[6] It is uncontroverted that each plan complies with § 1325(a)(5)(B)(i) because the secured creditors will retain the mortgages securing their respective claims. Section 1325(a)(5)(B)(ii) provides that the value of any property to be distributed under the plan on account of the secured claim be not less than the allowed amount of the claim. While Wilmington disputes that I can value the "prospect" of a sale for purposes of a plan's compliance with § 1325(a)(5)(B)(ii), *see* Wilmington Br. 5 (Case No. 19-40930, Dkt. No. 67), neither Wilmington nor BoA disputes that the respective plans propose to pay its secured claim in full with all contractual interest, *see* 11 U.S.C. § 1325(a)(5)(B)(ii) (providing that "the value, as of the effective date of the plan, of property to be distributed under the plan on account of such [allowed secured] claim is not less than the allowed amount of such claim."); 11 U.S.C. § 1322(e) (providing that "[n]otwithstanding subsection (b)(2) of this section and sections 506(b) and 1325(a)(5) of this title, if it is proposed in a plan to cure a default, the amount necessary to cure the default, shall be determined in accordance with the underlying agreement and applicable nonbankruptcy law" and clarifying no interest upon interest due with respect to cure payments, narrowing Supreme Court's holding in *Rake v. Wade*, 508 U.S. at 473, 113 S.Ct. 2187). While the prospect of a sale may be an issue with respect to other confirmation requirements, such as a plan's feasibility under § 1325(a)(6), providing for payment of a secured claim through a sale does not violate § 1325(a)(5)(B)(ii), *per se*.

The parties disagree as to whether and how subsection (iii)(I) of § 1325(a)(5)(B) applies where payment of a secured claim is treated by providing for certain continuing payments followed by a sale of the creditor's collateral and payment in full of the secured claim from proceeds of the sale (both prepetition arrears and the balance due on the mortgage note at the time of the payoff). [16] Section 1325(a)(5)(B)(iii) provides "*if*—(I) property to be distributed pursuant to this subsection is in the form of periodic payments, such payments shall be in equal monthly amounts." 11 U.S.C. § 1325(a)(5)(B)(iii) (emphasis added). Congress added the equal payments provision as part of BAPCPA. The legislative history is not clear with respect to its intent and courts have viewed the intent of the amendment differently. Some courts prohibiting balloon payments have noted that the provision was added "in response to creditors' concerns about balloon and quarterly payments .... The equal payment provision prevents debtors from back loading payments to secured creditors or paying them other than on a monthly basis." ***793** *In re Hamilton*, 401 B.R. at 543 (citations omitted). Other courts have been critical of that view. *See, e.g.*, *In re Olsen*, 604 B.R. 790, 803 (Bankr. W.D. Wis. 2019) (observing "[c]ourts have struggled to find primary sources detailing the legislative purpose behind section 1325(a)(5)(B)(iii)(I)") (citations omitted)). As one court adopting a contrary view has explained,

> Upon the Court's review, cases prohibiting balloon payments as contrary to the history or purpose of § 1325(a)(5)(B)(iii)(I) do so based on unsupported judicial speculation, rather than formal legislative history[.]
>
> ...
>
> This lack of cited authority is not surprising, as the only formal legislative history found by this Court ... merely echoes the wording of the subsection, without any insight as to the purpose of its enactment.
>
> ...
>
> [I]t seems that Congress intended to give creditors more certainty and regularity as to any proposed [sic] stream of payments. Requiring any stream of payments to be equal falls within the periodic payments language and functions in tandem with Congress's concerns over protecting holders of claims secured by personal property (as evident from § 1325(a)(5)(B)(iii)(II)). Accordingly, the Court determines that Congress had reasons other than prohibiting balloon payments in enacting the equal payment provision—reasons that fit more naturally with the language of the statute, and that are not implicated by the Debtor's Plan.
>
> ...
>
> Moreover, the majority rule runs against the grain of Chapter 13's underlying purposes. "In determining the meaning of the statute, we look not only to the particular statutory language, but to the design of the statute as a whole and to its object and policy." ... The interpretation argued by the [majority] would go against Congress's intent

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

> to provide a flexible means for the debtor to protect his assets, most importantly those assets necessary to pay his creditors by completing his plan, such as a house to live in or car to drive to work. This flexibility is evident in the structure of Chapter 13 itself. ... This flexibility is further reflected in the legislative history.

In re Cochran, 555 B.R. at 901–02, 904-05 (internal citations omitted).

How does the equal payments provision of § 1325(a)(5)(B)(iii) apply, if at all, to plans, such as the ones at issue here, that provide for contractual maintenance payments or "adequate protection payments" to a secured creditor pending a sale or refinancing, where the monthly amount of the proposed periodic payments is not equal to the final payment that occurs upon sale or refinancing? If the "payoff" on sale is viewed to be the last of a series of "periodic payments," the plans would violate the provisions of § 1325(a)(5)(B)(iii). In determining which interpretation is more persuasive and whether the equal payments provision is applicable to these plans, I must consider other related provisions of the Code, including the subsections of § 1322 raised by Mr. Gnaman as also governing Wilmington's plan treatment and which Mr. Materne explicitly seeks to avoid being applied to his treatment of BoA's claims.

Section 1322, entitled "Contents of Plan," lists mandatory and optional provisions that a debtor may propose in a plan. *See* 11 U.S.C. §§ 1322(a)–(b). Under appropriate circumstances, a plan proposing sale of property may be consistent with the rights and powers of a debtor under § 1303 and the provisions of § 1322(b)(8), which states that that a plan may "provide for ***794** the payment of all or part of a claim against the debtor from property of the estate or property of the debtor." 11 U.S.C. §§ 1322(b)(8), 1303; *see also* 8 Collier on Bankruptcy ¶ 1322.12 (Richard Levin & Henry J. Sommer eds., 16th ed.) ("In keeping with the aim of increasing the flexibility of chapter 13 relief, section 1322(b)(8) permits the filing of a liquidating plan in a chapter 13 case."). But § 1322(b)(8) cannot be viewed in a vacuum, and for home mortgages where the last payment is due after the plan term (also referred to as "long-term" home mortgages), § 1322(b)(2)'s prohibition on modification of the rights of the holders of such claims must be considered.

[7] Section 1322(b)(2) permits a debtor to modify the rights of a holder of a secured claim, but only if that claim is not "secured only by a security interest in real property that is the debtor's principal residence." 11 U.S.C. § 1322(b)(2). "A [secured] creditor's rights 'protected from modification by § 1322(b)(2)' are the rights under the original loan instruments as defined by state law." *Dukes v. Suncoast Credit Union (In re Dukes)*, 909 F.3d 1306, 1321 (11th Cir. 2018) (quoting *Nobelman v. Am. Sav. Bank*, 508 U.S. 324, 329–30, 113 S.Ct. 2106, 124 L.Ed.2d 228 (1993)). A debtor may not "modify" the rights of a home-mortgage lender, subject only to the exceptions provided in subsections (b)(5) and (c). 11 U.S.C. § 1322(b)(2), (b)(5) and (c). Section § 1322(c) permits a debtor to cure defaults at any time during the term of the plan as long as cure is made prior to any foreclosure notwithstanding the anti-modification provision of § 1322(b)(2). Commonly in Chapter 13 cases, a debtor will seek to preserve their home by proposing a plan that "cures" prepetition arrears over time while paying the remaining mortgage debt with interest in accordance with its terms or within the life of the plan. *See, e.g.*, Andriana Glover, *The "Cure" to the Homeowner's Bankruptcy Blues: An Analysis of A Homeowner's Ability to Cure His Mortgage Default Under S 1322(b)(5) of the Bankruptcy Code*, 34 Emory Bankr. Dev. J. 89, 91 (2017) (explaining "[a]mong the permissive provisions listed in § 1322(b), the Code provides that a debtor may cure any default. Most chapter 13 debtors rely on these provisions to save their homes.").

[8] Section 1322(b) contains two other sections specifically dealing with cure of prepetition arrears and other defaults under Chapter 13 plans.

> Subsection 1322(b)(3) broadly permits [a chapter 13] plan to provide for the curing or waiving of any default and subsection (b)(5) permits the plan to provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due.

In re Vertullo, 610 B.R. 399, 406 (B.A.P. 1st Cir. 2020) (quotations and citations omitted). The primary difference between the subsections, is that § 1322(b)(3), when read in conjunction with § 1322(c)(2), permits a debtor to cure defaults of obligations that matured prepetition or that mature

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

during the plan term—whereas § 1322(b)(5) deals exclusively with obligations where the last payment is due after the plan term. [17] *See, e.g.*, ***795** *In re Redmond*, 380 B.R. 179, 188 (Bankr. N.D. Ill. 2007); *In re Stevens*, 374 B.R. 31, 34–35 (Bankr. D.N.H. 2007) (applying Code § 1322(b)(3) for cure involving short term obligation). Section 1322(c)(2) provides that, where the last payment of a loan secured by a debtor's principal residence becomes due before the end of the debtor's plan term, the plan may provide for payment of the claim over the term of the plan—notwithstanding the anti-modification provision of § 1322(b)(2) and applicable nonbankruptcy law. It is not clear whether § 1322(b)(3), standing alone, was intended to allow an option to cure a claim secured by a principal residence where the term of that loan is longer than the plan term—but where the plan provides for early payment in full of that secured claim during the plan term through a sale. As will be discussed, the answer may ultimately be irrelevant to the confirmation issues raised by these sale plans.

Sections 1322(b)(3) and (b)(5) must be considered in the context of the "antimodification" prohibition of subsection (b)(2) where a mortgage on the debtor's principal residence is at issue. *See Anderson*, 820 F.3d at 674 (holding that anti-modification provision under § 1322(b)(2) prevented reduction of default interest rate to pre-default rate under §§ 1322(b)(3) and (5)); *but see In re Taddeo*, 685 F.2d at 27 (concluding that "the power to 'cure any default' granted in [§] 1322(b)(3) and (b)(5) is not limited by the ban against 'modifying' home mortgages in [§] 1322(b)(2) because we do not read 'curing defaults' under (b) (3) or 'curing defaults and maintaining payments' under (b)(5) to be modifications of claims"); 8 Collier on Bankruptcy ¶ 1322.07 (same, citing, among others, *In re Taddeo*, 685 F.2d 24 (2d Cir. 1982)).

[9] While the general cure provision of § 1322(b)(3) is not explicitly limited to any particular kind of debt, some courts have declined to permit application of § 1322(b)(3) to long-term mortgage debt, reasoning that § 1322(b)(5) is a more specific subsection relating to the treatment of long-term home mortgage debt. *See United States v. Easley*, 216 B.R. 543, 546 (W.D. Va. 1997) (determining that "[i]n order to give effect to the limitations in § 1322(b)(5), § 1322(b)(3) cannot apply to such long-term mortgages). *But see*, Lundin on Chapter 13, § 78.4, at ¶ 17 (stating, without citation to decisional authority, that "[a]rguably, § 1322(b)(3) allows a Chapter 13 plan to cure or waive default with respect to any debt, including a long term debt, without satisfying the reasonable time or maintenance of payments requirements in § 1322(b)(5)."). If the secured debt at issue is a short-term debt that has matured or matures prior to the due date of the final plan payment, a debtor could not use § 1322(b)(5) to cure, but may look to § 1322(b)(3). *See generally*, 8 Collier on Bankruptcy, ¶ 1322.07 (noting "section 1322(b)(3) is applicable to all claims, including short-term debts such as ... debts that are secured only by a security interest on the debtor's principal residence and that mature prior to the date on which the final plan payment is due. Any doubt with respect to the latter category should be eliminated by section 1322(c)(1)"). [18] On its face, there is overlap ***796** between § 1322(b)(3) and (b)(5) that raises questions as to how § 1322(b)(3) fits within the confirmation scheme for plan treatment of secured claims. [19] While there is some support for holding that Congress may have intended § 1322(b)(3) to apply to cure of defaults for secured claims that had matured or were for a shorter term than the plan period, leaving long-term home mortgage debt to be provided for as set forth in § 1322(b)(5), [20] it is possible to read § 1322(b)(3) together with § 1322(c)(1) to permit a cure of a long-term mortgage where a debtor proposes to pay the claim in full on an accelerated basis within the plan term. Ultimately, in the context of a long-term home mortgage, whether cure could be undertaken under § 1322(b)(3) or (b)(5) does not appear to matter because, if cure is made pursuant to § 1322(b)(3), a debtor would not have the benefit of § 1322(c)(2) and would be subject to the anti-modification provision of § 1322(b)(2). Presumably, this would require a debtor to make monthly payments in accordance with the terms of the mortgage during the term of the plan, effectively maintaining payments as would otherwise be required by § 1322(b)(5). If the plan were to provide for periodic payments to avoid an impermissible modification under § 1322(b)(2), the equal payments provision under § 1325(a)(5)(B)(iii) would still have to be addressed.

[10] **[11]** Section 1322(b)(5) states that, "notwithstanding" the anti-modification prohibition for debt secured by a debtor's principal residence of § 1322(b)(2), a plan may "provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due ...." 11 U.S.C. § 1322(b)(5); *see also In re Nosek*, 544 F.3d at 45 (noting that "[n]otwithstanding the general exception set forth in § 1322(b)(2), which prevents the modification of a lender's rights secured by a debtor's primary residence, § 1322(b)(5) explicitly 'authorizes debtors to cure any defaults on a long-term debt, such as a mortgage, and to maintain payments on the debt during the life of

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

the plan.' ") (quoting *Rake v. Wade*, 508 U.S. 464, 113 S.Ct. 2187, 124 L.Ed.2d 424 (1993)). Thus, § 1322(b)(5) allows for the curing of prepetition arrears on long-term debt in default as of the petition date provided the debtor: "(1) cure[s] the default ***797** *within a reasonable time* and (2) stay[s] current on postpetition payments due under the parties' original agreement."[21] *In re Euliano*, 442 B.R. 177, 186 (Bankr. D. Mass. 2010). A plan that does not provide for maintenance payments, and only provides for a sale within the time period covered by plan that contemplates use of proceeds to pay off mortgage, would impermissibly modify the secured creditor's rights. *Compare Phila. Life Ins. Co. v. Proudfoot (In re Proudfoot)*, 144 B.R. 876, 878 (B.A.P. 9th Cir. 1992) (holding that plan violated § 1322(b)(2) because "by withholding payments, the plan created defaults which modified [secured creditor's] rights as a creditor whose only security was the Debtor's principal residence"); *In re Gavia*, 24 B.R. 573, 575 (B.A.P. 9th Cir. 1982) (same; concluding that sale plans that proposed to withhold current mortgage installments for up to six months to sell debtors' residences and pay mortgages from sale proceeds created, rather than cured, default and served to modify rights of creditors in violation of § 1322(b)(2)); *In re Newton*, 161 B.R. 207, 217 (Bankr. D. Minn. 1993) (holding that "obviously, any proposal to toll a debtor's obligation of periodic debt service works a modification of the mortgagee's contractual rights in violation of § 1322(b)(2), whether the tolling is indefinite or for a fixed term. More problematic are proposals such as the one at bar, where a cure would be effected by joint means, one defined by periodic cash payments but only partly efficacious, and the other contingent on a future market transaction"); *with In re Dunn*, 399 B.R. 909 (Bankr. W.D. Wash. 2009) (notwithstanding *Proudfoot* and *Gavia*, holding that proposed "sale" plan did not impermissibly modify rights of secured creditor whose only security was an interest in debtor's residential real property ***798** because although plan did not provide for current ongoing payments, plan provided for immediate stay relief by stipulation or upon confirmation so that bank had the option to foreclose, therefore, in effect, bank had the same rights under the plan that it would have had outside of bankruptcy).

While these debtors argue that the provisions of § 1322(b)(2) need not be considered because each is simply "paying" the claim in full as permitted by § 1325(a)(5), it seems apparent that Congress intended the anti-modification provisions of § 1322(b)(2) to prohibit the delay and uncertainty that would be associated with sale plans, such as these, having no definite sale date when cure will be made. Section 1322(b)(8) would certainly allow full payment of a secured claim from proceeds of a sale on the effective date of a plan or, possibly, within a reasonable time thereafter, but to interpret § 1322 and § 1325(b) to allow confirmation of a plan that provides for an indefinite cure period within the plan term would essentially read the anti-modification provision and other parameters established under § 1322(b) out of the Code.[22] While "permissive" in the sense that § 1322(b) provides that a plan "may" include certain provisions, reading the statutory scheme as a whole, considering the legislative intent and the mandatory implication of the anti-modification provision of § 1322(b)(2), leads me to the conclusion that, whether cure is achieved pursuant to § 1322(b)(3) or (b)(5), a plan providing for treatment of a claim secured by a mortgage of a debtor's primary residence having a final payment due after the plan period must provide for (i) cure within a reasonable time[23] and (ii) periodic postpetition contractual payments to avoid an impermissible modification as prohibited by § 1322(b)(2). Again, this assumes that the plan does not provide for full payment of the secured claim from proceeds of a sale on the effective date of a plan or within a reasonable time thereafter.

B. Does § 1325(a)(5)(B)(iii) apply to postpetition contractual "maintenance" payments?

If a debtor is providing for payment of a long-term home mortgage loan in a plan, the Code would appear to require a debtor to comply with § 1325(a)(5)(B)(iii) where that plan that proposes to maintain monthly contractual payments (or make other periodic payments) and to cure arrearages during the life of the plan.[24] *Cf.* ***799** *Rake v. Wade*, 508 U.S. at 469, 113 S.Ct. 2187, *superseded on other grounds by statute*, Bankruptcy Reform Act of 1994, Pub. L. No. 103-394 § 305, 108 Stat. 4106–34 ("Section 1322(b)(5) expressly authorizes debtors to cure any defaults on a long-term debt, such as a mortgage, and to maintain payments on the debt during the life of the plan. Under § 1322(b)(5), a plan may provide for the curing of any defaults and the maintenance of payments on a long-term debt "notwithstanding" § 1322(b)(2)'s prohibition against modifications of the rights of home mortgage lenders."); *In re McDonald*, 397 B.R. at 178 (sustaining confirmation objection to plan which provided for change in payment amounts regarding cure proposal in later months and holding that subsequent legislative amendment "did nothing to upset *Rake's* determination that a cure proposal under § 1322(b)(5) ... is a proposal to modify a secured claim under a plan. As such, it must meet the requirements of § 1325(a)(5)."); *In re Wagner*, 342 B.R. 766, 772 (Bankr. E.D. Tenn. 2006) (holding

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

that long term maintenance payments pursuant § 1322(b)(5) are still subject to the equal monthly payment requirement); *but see In re Davis*, 343 B.R. at 328 (allowing for cure of arrearages in unequal monthly installments because § 1325(a)(5) is inapplicable where claim is treated under § 1322(b)(5)); *In re Erickson*, 176 B.R. 753, 757 (Bankr. E.D. Pa. 1995) (in a case where the Chapter 13 trustee objected to confirmation based on feasibility, determining "[s]ale plans generally do not per se modify secured creditors' rights; they merely delay immediate payment to creditors in consideration for what is often accelerated full payment."); *In re Randell*, 638 B.R. 104, 110 (Bankr. E.D. Wis. 2022) (internal quotations and citation omitted) (determining that "nothing in § 1322(e) abrogated *Rake's* holding that mortgage arrearages paid off under the terms of the plan are an element of an allowed secured claim provided for by the plan and must meet the requirements of section 1325(a)(5)"). In *Rake*, each of the debtor's plans in the separate cases at issue proposed to pay all postpetition contractual mortgage payments directly to the creditor and to cure the prepetition mortgage arrearages, without interest, over the term of the plan. *Rake v. Wade*, 508 U.S. at 472, 113 S.Ct. 2187. The oversecured mortgage creditor objected to confirmation claiming it was entitled to postpetition interest on the arrearages, when the contract did not provide for additional interest. *Id.* Because the plans "provided for" the creditor's claim by establishing repayment terms for the arrearages as permitted ***800** by § 1322(b)(5), the Supreme Court ruled that the creditor was entitled to interest to satisfy the "present value requirement" of § 1322(b)(5)(5)(B)(ii). [25] *Id.* at 473, 113 S.Ct. 2187 (later abrogated as to the interest issue by enactment of § 1322(b)(e)). In reaching its holding, the Supreme Court considered § 1328(a), which also contains the phrase "provided for by the plan," and noted:

> As used in § 1328(a), that phrase is commonly understood to mean that a plan 'makes a provision' for, 'deals with,' or even 'refers to' a claim. [Citation omitted]. In addition, § 1328(a) unmistakably contemplates that a plan 'provides for' a claim when the plan cures a default and allows for the maintenance of regular payments on that claim, as authorized by § 1322(b)(5). Section 1328(a) states that 'all debts provided for by the plan' are dischargeable, and then lists three exceptions. One type of claim that is 'provided for by the plan' yet excepted from discharge under § 1328(a) is a claim 'provided for under section 1322(b)(5) of this title.' § 1328(a)(1). If claims that are subject to § 1322(b)(5) were not 'provided for by the plan,' there would be no reason to make an exception for them in § 1328(a)(1).

Id. at 474–75, 113 S.Ct. 2187.

Some courts have distinguished *Rake* in other contexts and others have come to a different conclusion as to whether maintenance payments are "provided for under the plan." *See, e.g.*, *Cohen v. Lopez (In re Lopez),* 372 B.R. 40, 49–50 (B.A.P. 9th Cir. 2007), *aff'd and opinion adopted,* 550 F.3d 1202 (9th Cir. 2008) (holding, in the context of a Chapter 13 trustee's objection to maintenance payments being made directly to a lender outside the plan, that regular, postpetition maintenance payments are in amounts no different from what the debtor would have paid had he or she never defaulted and are not modified by the Chapter 13 bankruptcy and not provided for by the plan); *In re Bullard*, 475 B.R. 304, 308–309 (Bankr. D. Mass. 2012), *aff'd*, 494 B.R. 92 (B.A.P. 1st Cir. 2013) (in the context of a hybrid plan appearing to involve multi-unit property in which one of the units is the debtor's principal residence and with respect to which the creditor did not object to bifurcation based on the nature of the property, concluding that under § 1322(b)(5) that "a debtor may pay a prepetition arrearage in full through the plan and, upon plan completion, the default is deemed cured and the relationship between the parties continues ... [;] the secured claim is simply riding through the bankruptcy on its original terms, it is not a 'secured claim provided for by the plan' and is not subject to the present value requirement of 11 U.S.C. § 1325(a)(5)(B)(ii)"); *In re Clay*, 339 B.R. 784, 785-86, 787, 788 (Bankr. D. Utah 2006) (determining in the context of an objection to confirmation by the Chapter 13 Trustee to a plan where the debtor had only secured debt and proposed to make cure payments on home mortgages through the ***801** plan and all other payments directly to secured creditors that BAPCPA did not change the right of Chapter 13 debtors to choose to pay secured creditors directly so long as the contract rights of those creditors are not altered. The requirement in § 1325(a)(5) that equal monthly payments be made to allowed secured claims provided for by § 1325(a)(5) does not change the pre-BAPCPA result because "a secured claim is only 'provided for by the plan,' and thus subject to the requirements of § 1325(a)(5), if the creditor is not paid pursuant to the terms of the contract."). *see also In re Dukes*, 909 F.3d at 1315 (in case analyzing "provided for language" in the context of discharge injunction application and concluding that "*Rake* does not stand for the proposition that a plan 'provides for' a claim merely by mentioning it. To the contrary, it suggests that a claim is 'provided for' where the plan supplies terms that will govern the repayment of the claim").

In *Lopez*, the Bankruptcy Appellate Panel for the Ninth Circuit addressed the "provided for" language in the context

of determining whether direct payments could be made to a home mortgage lender and ruled that "[w]hile this is a difficult issue, with arguments on both sides, this panel nevertheless concludes that the ongoing maintenance payments are not modified by the Chapter 13 bankruptcy." *In re Lopez*, 372 B.R. at 50. The court was persuaded by the following passage in *Rake* as supporting its conclusion: " '[a]s authorized by § 1322(b)(5), the plans essentially split each of respondent's secured claims into two separate claims—the underlying debt and the arrearages. While payments of principal and interest on the underlying debts were simply 'maintained' according to the terms of the mortgage documents during the pendency of petitioners' cases, each plan treated the arrearages as a distinct claim to be paid off within the life of the plan pursuant to repayment schedules established by the plans.' " *Id.* at 48–49 (quoting *Rake,* 508 U.S. at 473, 113 S.Ct. 2187). Based on that language, the court in *Lopez* reasoned that:

> ...Rake assumed that the entire home mortgage claim was comprised of two separate parts. First, there is the amount in arrears. This amount consists of prepetition obligations due but not paid—that is, the claims are "mature"—as of the filing. Second, there is the regular, ongoing post-petition maintenance payments, in amounts no different from what the debtor would have paid had he or she never defaulted. These consist of obligations under the relevant documents that, but for any pre-petition acceleration of maturity, would be unmatured as of the filing. Thus, bankruptcy law and the plan only modify the claim in relation to the scheduled payments in default at filing. Post-petition payments are different; they are ongoing payments, not due at filing, which will continue to be made after plan completion. They are not altered by the plan.

In re Lopez, 372 B.R. at 48–49. The *Lopez* court concluded any statements that could be read to classify maintenance payments as being "provided for" by a plan in *Rake* should be viewed as distinguishable *dicta* since the focus in that case was the treatment of payments necessary to cure arrears and there was other language in *Rake* "contradict[ing] the unitary view of home mortgage claims." *Id.* at 48. [26]

***802** **[12]** **[13]** **[14]** "The Bankruptcy Code does not define 'maintenance of payments,' but courts have interpreted this provision to mean the original contractual payments of principal and interest over the time frame specified in the note." [27] *In re Bullard*, 475 B.R. at 308–09. While well-reasoned arguments can be made for a "bifurcated-claim approach" such as was adopted by the *Lopez* court, the language of § 1322(b)(5) and the language of *Rake* militate against that interpretation. Section 1322(b)(5) applies to "each allowed secured claim provided for by the plan" and provides requirements for confirmation of a plan. Secured claims are not "allowed" in two parts. Debts are owed under a mortgage note that may include both arrearages and principal amounts that may not yet be due as acknowledged in *Rake*. The *Lopez* court observes that the Code allows a debtor to bifurcate claims into secured and unsecured claims where the value of the collateral is less than the amount of the claim. *See* 11 U.S.C. § 506(a). But where a fully-secured claim is "bifurcated" by the Code for purposes of plan treatment into arrears that may be cured and the balance of the claim that will be maintained, the underlying nature of the allowed secured claim is not altered. Compare 11 U.S.C. § 506(a)(where portions of the amount of secured claims may be determined not to be secured so as to be determined to be general unsecured claims). The entirety of a debt that is fully secured constitutes the "allowed secured claim," and a plan that does more than state that the rights of the holder of that secured claim are not affected in any way by the plan "provides for" the treatment of that claim. For example, by implementing the cure provisions of § 1322(b)(3), (b)(5), or (c), a plan provides for treatment of a component of that claim. Other subsections of § 1325(a)(5) appear to assume that the section applies to the entire allowed amount of the secured claim. *See* 11 U.S.C. § 1325(a)(5)(A) (referring to acceptance by the holder of "such claim"), 1325(a)(5)(B)(i) (referring to the holder of such claim when requiring lien retention and referring to payment of the "underlying debt"), 1325(a)(5)(B)(ii) (requiring that a plan distribute at least the present value of the "allowed amount of such claim" "on account of such claim"), and 1325(a)(5)(C) (addressing surrender of the property securing such claim). Finally, it is not likely that Congress intended that § 1325(a)(5) be interpreted to apply to maintenance payments made "through the plan" in districts where such conduit plans are required, but not to apply to maintenance payments made in districts that allowed

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

direct payments by debtors. As such, I conclude that a plan proposing ***803** to cure arrearages and maintain payments pursuant to § 1322(b)(5) "provide[s] for" treatment of such a claim, making satisfaction of § 1325(a)(5) a requirement of confirmation. *Cf. Rake*, 508 U.S. at 474, 113 S.Ct. 2187 (interpreting § 1325(a)(5) in the context of other provisions in the Code); *In re Melillo*, 385 B.R. 476, 481 (Bankr. D. Mass. 2008) (holding that "[§] 1325(a)(5)(B)(iii)(I) does not preclude the curing of a default within a reasonable time or the maintenance of payments on a long term debt as it only controls the manner in which payments are made" and concluding § "1322(b)(5) just means that the entire secured claim need not be paid in full under certain circumstances allowing cure of default, but the claim is still an allowed secured claim.") (quotations and citations omitted)), *vacated on other grounds, sub nom.*, *In re Flynn*, 402 B.R. 437 (B.A.P. 1st Cir. 2009); *In re Schultz*, 363 B.R. 902, 906 (Bankr. E.D. Wis. 2007) (holding that "periodic payments must be equal, period. This applies when the default is cured and only current payments and the arrearage are being paid pursuant to the plan pursuant to 11 U.S.C. § 1322(b)(5) and when a long-term or matured debt are paid in full under the plan"). While the interpretation of § 1325(a)(5) adopted by *Lopez* would provide courts welcome flexibility in addressing confirmation of Chapter 13 plans, I feel constrained by the language of that provision and the dicta in *Rake* to conclude that § 1325(a)(5)(B)(iii) would apply to periodic maintenance payments and any cure payments for which a plan provides.

C. Does § 1325(a)(5)(B)(iii) preclude lump-sum payoffs upon the sale of a principal residence?

[15] **[16]** I now return to the question of whether the plans may include a lump sum cure and payoff where they provide for periodic payments to be paid directly by Mr. Gnaman or "adequate protection payments" to be disbursed by the Chapter 13 Trustee from plan payments made by Mr. Materne.

First, the Bankruptcy Code does not expressly contemplate post-confirmation adequate protection payments as part of a plan. Section 361 provides the means by which adequate protection may be provided when required by § 362, 363, or 364. Those provisions address circumstances when a secured creditor may be entitled to adequate protection from diminution of the value of its collateral during the pendency of a bankruptcy case. By providing adequate protection, a debtor may avoid relief from the automatic stay; use, lease or sell collateral; or obtain approval of priming liens. Neither § 1322(b) nor § 1325(a)(5) mention adequate protection or provide that adequate protection payments may be an alternative for the treatment of secured claims provided by those sections for confirmation of a plan.[28] As such, for purposes of analysis, I view the adequate protection payments proposed by Mr. Materne as a form of periodic payment provided for by the plan on account of the secured claim of BoA. *See, e.g.*, *In re Hamilton*, 401 B.R. at 543 (in response to the debtor's argument that his proposed balloon payment under his plan meant that the plan did not provide ***804** for "periodic payments" that would dictate application of § 1325(a)(5)(B), the First Circuit Bankruptcy Appellate Panel ("BAP") rejected the debtor's argument, stating that "[t]he [d]ebtor's argument is an invitation for the Panel to elevate form over substance by allowing the Debtor to sidestep statutory requirements by attaching a label to his plan payments other than the one that actually applies. We must decline the invitation."); *In re Acosta*, No. 08-11411, 2009 WL 2849096, at *3 (Bankr. N.D. Cal. May 7, 2009) ("The debtors' plan calls for monthly interest-only payments for four or five years, with a balloon at the end. Their argument is that the interest payments are 'adequate protection payments' and not 'periodic payments.' The court declines their invitation to engage in this sophistry; payments are payments."); *In re Luckett*, No. 07-24706-SVK, 2007 WL 3125278, at *1 (Bankr. E.D. Wis. Oct. 24, 2007) (determining that adequate protection payments are property distributed to a secured creditor and must be in equal monthly amounts, concluding that "[c]alling the property distributed on the claim 'adequate protection payments' does not change the fact that this is property distributed on the claim. If made over time, the distributions of the property on the claim must be in equal monthly amounts, and, unless [the creditor] consents, the balloon payment at the end of the Plan will not satisfy this requirement."); *but see In re Cochran*, 555 B.R. at 897 (noting "[s]ome courts seem to suggest that adequate protection payments, even though regularly occurring, may not qualify as 'periodic payments' under § 1325(a)(5)(B)(iii)(I)"); *In re Bollinger*, No. BR 10-62344, 2011 WL 3882275, at *4 n. 12 (Bankr. D. Or. Sept. 2, 2011) (stating "11 U.S.C. § 1325(a)(5)(B)(iii)(I) does not, of course, prohibit a single payment in full at any time during the course of the plan, assuming all other elements of §§ 1325 and 1322 have been complied with. Where the collateral is real property adequate protection payments appropriate under § 361 maybe [sic] addressed in a plan or separately."). Consequently, both the Materne plan and the Gnaman plan propose to make periodic payments (although "in" the plan in the case of Materne and directly by Gnaman) and cure with a lump sum payment that will also pay the secured claim in full.

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

Having considered the various provisions of § 1322 and having determined that each of the debtor's plans must satisfy the requirements of § 1325(a)(5)(B)(iii)(I) because they each include periodic payments, it is necessary to determine whether the plans comply with the "equal payments" requirement of that provision. There are majority and minority interpretations of whether balloon payments are prohibited under § 1325(a)(5)(B)(iii)(I).

> The majority holds this subsection prohibits balloon payments. *See, e.g.*, *In re Miceli*, 587 B.R. 492, 502 n.13 (Bankr. N.D. Ill. 2018) (noting the "nearly universal line of cases which ha[ve] held that the subsection prohibits balloon payments"). These cases argue a balloon payment is part of the stream of periodic payments. It follows that the monthly payments and eventual balloon payment are periodic payments not in "equal monthly amounts." ... A growing minority view interprets the "periodic payments" language differently.

In re Olsen, 604 B.R. at 803 (in case were modification was permissible under § 1322 because mortgage claim part of commercial transaction, applying § 1325 as qualifying the requirements of § 1322 and holding that a balloon payment does not violate § 1325(a)(5)(B)(iii)); *In re Cochran*, 555 B.R. at 906 (declining to follow the majority rule in case not involving exception to modification and holding that "balloon payments ***805** are not 'periodic payments' proscribed by § 1325(a)(5)(B)(iii)(I)"); *see also* Keith M. Lundin, Lundin on Chapter 13, § 74.14, at ¶ 7 ("At present, a majority of reported decisions reads the equal monthly amount requirement in § 1325(a)(5)(B)(iii) to prohibit the use of balloon payments by sale or refinancing to manage the curing of mortgage arrearages when periodic payments are also contemplated by the plan.").

The BAP has followed the majority view and has ruled that a "balloon payment" at the end of a 60-month plan violated § 1325(a)(5)(B)(iii). *In re Hamilton*, 401 B.R. at 541, 545–46. In that case, the proposed plan provided for bifurcation of a secured creditor's claim, monthly plan payments to the chapter 13 trustee in the amount of $5,397 that would result in distributions of $4,029.77 per month on account of the secured portion of the claim (which was less than the monthly payment required to pay the modified claim in 60 months), and a balloon payment "[i]n or before the 60th month" through a refinancing. *Id.* After dispensing with the debtor's arguments that the plan specifically provided that payments were not to be considered "periodic payments" and that discretionary payment provisions in the plan made § 1325(a)(5)(B)(iii) inapplicable, the BAP held that the debtor's plan provided for "periodic payments" and that "11 U.S.C. § 1325(a)(5)(B)(iii)(I) prohibits balloon payments on secured claims where the creditor has not accepted the plan and the debtor has not surrendered the property." *Id.* at 541 (also noting that "[o]verwhelmingly, courts have held that by its very terms, a balloon payment is not equal to the payment that preceded it, and thus violates § 1325(a)(5)(B)(iii)(I) with respect to periodic payments on a secured claim under a chapter 13 plan").

Courts adopting the minority interpretation have held that, where applicable, § 1325(a)(5)(B)(iii) does not prohibit a balloon payment and have interpreted "periodic payments" to refer only to those payments and not a balloon payment that would pay off the loan. As discussed by one such court,

> Because "periodic" payments are regularly reoccurring and balloon payments are not, balloon payments are not "property to be distributed ... in the form of periodic payments" and, consequently, are outside the scope of § 1325(a)(5)(B)(iii)(I). This conforms with the common and technical understanding of these terms. For example, *Webster's Third New International Dictionary* defines "periodic" as something that is "characterized by periods," occurs "at regular intervals," and occurs "repeatedly from time to time." ... These definitions establish that a final, balloon payment is distinct and separate from the preceding "periodic payments." Accordingly, it is only the periodic payments—and not the balloon payment—that are subject to the "equal monthly amounts" directive of § 1325(a)(5)(B)(iii)(I).
>
> The language of § 1325(a)(5)(B) indicates that the property distributed on account of a claim need not be of a singular type and need not be made in a singular manner. Importantly, § 1325(a)(5)(B)(iii) does not include a definite article, such as 'the.' For example, the related, immediately preceding provision—§ 1325(a)(5)(B)(ii)—refers to 'the value, as of the effective date of the plan, of property,' indicating that there is only one value, but allowing for numerous articles 'of property.' Section 1325(a)(5)(B)(iii) does not state 'if the property to be distributed pursuant to ***806** this subsection;' rather, it states 'if property.'

In re Cochran, 555 B.R. at 898–99.

In Gnaman, the debtor argues that the plan effectively "bifurcates" Wilmington's secured claim into the pre-petition arrearages to be cured on sale of the Property and the

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

remaining balance as to which the contractual payments will be maintained and the balance of the secured claim will be paid from proceeds of the contemplated sale of the Franklin Property. As discussed above, the Gnaman plan proposes to cure the prepetition mortgage arrears by a single payment upon the sale of the Franklin Property. As to the "non-cure" portion of Wilmington's secured claim, Mr. Gnaman proposes to "maintain" by making periodic contractual payments as required by § 1322(b)(5) in even amounts as contemplated by § 1322(b)(5), but the Debtor also proposes a "balloon" payment upon sale. The Code specifically contemplates that a debtor may sell property during the pendency of the case. *See* 11 U.S.C. §§ 363, 1303, and 1322(b)(8). Notably, under the terms of standard mortgages and applicable non-bankruptcy law, a mortgagor would be permitted to sell mortgaged residential property at any time prior to a foreclosure provided that all amounts due under the mortgage were paid at the time of the sale.

It is difficult to conceive that Congress would have intended to prohibit confirmation of a plan that proposed to maintain contractual mortgage payments, cure arrears, and pay off the full amount of the secured claim in a reasonable period of time upon the sale of a property in which the mortgagee enjoys an equity cushion where the debtor demonstrates a good faith reason for delaying the sale.[29] Yet, as discussed above, a majority of courts that have considered this issue have concluded that the equal payment provision of § 1325(a)(5)(B)(iii)(I) would operate to prohibit confirmation of such a plan. *See, e.g.*, *Hamilton*, 401 B.R. at 544; *In re Benedicto*, 587 B.R. at 576; *In re Miceli*, 587 B.R. at 502 n.13. By adopting a strict literal interpretation of the equal payment provision added to the Code by BAPCPA, courts avoid an inevitable large volume of evidentiary hearings on the issues of feasibility of distant future sales (or refinancings), "reasonableness of the timing of a cure," and the good faith of the debtor proposing delayed treatment. Plans like those proposed by Messrs. Gnaman and Materne illustrate certain possibilities for those evidentiary issues where those plans provide no timetable for a sale, details about a sale process, or information about why the unspecified time to cure is "reasonable."

[17] **[18]** The Code does provide some flexibility for plans to cure and satisfy allowed secured claims through a sale that might allow confirmation of a plan similar to the hypothetical plan discussed above. I interpret § 1322(b)(8) and § 1325(a)(5) to permit a secured claim to be paid in full through a sale that is in prospect at the time of confirmation or a reasonable time thereafter, subject to all other confirmation requirements such as feasibility and good faith.[30] Moreover, a debtor may sell ***807** his or her principal residence during the life of a traditional "cure and maintain" plan and pay the secured claim in full from proceeds of that sale. Admittedly, where confirmation of a plan is denied because a secured creditor has objected because there is no specific sale process contemplated, such an interpretation does not assist a debtor who cannot afford to propose a "cure and maintain" plan, but wishes to rely on the perceived equity in his or her home until a sale at some undefined time during the plan period cures defaults and pays the secured claim in full.

[19] The minority position is appealing and could be said to give life to both § 1322(b)(5), which contemplates curing of defaults within a "reasonable" time while maintaining contractual or adequate protection payments, and § 1322(a)(8), which contemplates that a plan may provide for the payment of all or a part of a claim from property of the estate. *See, e.g., In re Cochran*, 555 B.R. at 898–99 (concluding balloon payment are not a "periodic payment" under the plain language of § 1325(a)(5)(B)(iii)(I)); Hon. W. Homer Drake, Jr., Hon. Paul W. Bonapfel, & Adam M. Goodman, Chapter 13 Practice & Procedure § 5:18 (2016) ("The term 'periodic payments' could be construed to mean regular, recurring payments that are made to reduce a secured claim during the plan's term but not to a final one that completely satisfies it. A regular installment payment or payment of interest on the debt is a 'periodic' one, whereas a lump sum payment is not .... [T]his interpretation of 'periodic payments' accomplishes the primary objective of the new provisions of Code § 1325(a)(5)(B)(iii) ...."; Lynn M. LoPucki, *House Swaps: A Strategic Bankruptcy Solution to the Foreclosure Crisis*, 112 Mich. L. Rev. 689, 729–33 (2014) ("Had the drafters ... intended [section 1325(a)(5)(B)(iii)(I)] to prohibit balloon payments and periodic payments, the drafters would have said 'all plan payments' instead of 'such payments.' "). Unfortunately, the majority interpretation is most consistent with the language of § 1325(a)(5)(B)(iii), the smattering of legislative intent to spare holders of secured claims from uneven payments and indefinite balloon payments, consistent administration of Chapter 13 cases, and persuasive authority in this Circuit. While not entirely satisfactory, in the absence of clarification by Congress, I have determined that the equal payment provision of § 1325(a)(5)(B)(iii) is best read to prohibit confirmation of a sale plan, over the objection of a secured creditor holding a mortgage of a principal residence, that contemplates periodic payments followed by a lump-sum payment.

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

D. Another path: §§ 1322(b)(8) and 1325(a)(5)

[20] Each of the debtors argues that payment of a secured claim in full through a sale is consistent with § 1322(b)(8) and § 1325(a)(5). That may be correct as the ***808** Code would certainly permit confirmation of a sale plan that proposes payment in full of an allowed claim secured by a home mortgage at the time of confirmation and possibly with some delay. Should either debtor elect to propose a non-consensual plan that provides for cure and payment of allowed claims secured by long-term mortgages through a sale of residential property that does not satisfy the cure and maintain option provided by § 1322(b)(5) or the cure and "no modification" option contemplated by § 1322(b)(5) and (c)(1), the statutory path to confirmation could be through § 1322(b)(8) and § 1325(a)(5). These provisions may permit confirmation of a non-consensual plan that provides for a secured claim to be paid in full through a sale that is in prospect at the time of or at a reasonable time after confirmation, with or without payments prior to the sale, subject to all other confirmation requirements such as feasibility and good faith.

If the plans were to be amended to provide for a sale that is in prospect at the time of or at a reasonable time after confirmation, all statutory confirmation requirements must be met, and each debtor would have to demonstrate the reasonableness of the proposed timing for the sale and payment of the claim, feasibility, and good faith. Section 1325(a)(6) requires that "the debtor will be able to make all payments under the plan and to comply with the plan," 11 U.S.C. § 1325(a)(6), and a plan must be proposed in good faith to be confirmed, 11 U.S.C. § 1325(a)(3). Evidence that would support these determinations is likely to overlap and courts sometimes discuss these requirements together.

[21] In determining whether confirmation of a debtor's sale plan is appropriate, some courts have focused on the feasibility requirement in the context of determining the "reasonableness" of a proposed cure period and have required that sale plans identify, with sufficient specificity, the terms of the sale, including the listing price and terms, a timeline for the proposed sale, and a default remedy or other alternative if the sale fails to close within the proposed time frame. *See In re Weltlich*, No. 12-30181, 2012 WL 3782553 (Bankr. N.D. Ohio Aug. 31, 2012) (determining sale plan was reasonable and feasible effort, following listing of property for sale); *In re Erickson*, 176 B.R. at 758 (denying confirmation because plan failed to provide any specifics of conditions or timing of sale); *In re Newton*, 161 B.R. at 218 (finding that court cannot confirm a plan unless specifics of condition and timing of the sale are provided). As one court explained:

> The plan should specify the terms under which the debtor proposes to market the property, including the listing price and the length and commencement date of the listing agreement. It also should incorporate a default remedy to relieve the affected mortgagee(s) from the automatic stay, if the sale does not close by the end of the proposed cure period. If an affected mortgagee objects to confirmation, the debtor must produce evidence as to past marketing efforts, the state of the market for the subject asset, current sale prospects, the existence and maintenance of any "equity cushion" in the property, and all other circumstances that bear on whether the creditor will see its way out of the case financially whole. If the debtor cannot produce anything more than remote speculation as to the terms or date of a sale; if market conditions are eroding the value of the collateral; if the debtor's efforts at a sale are not directed or energetic enough; or if any other factors demonstrate that the creditor will not receive the value of its secured rights within a circumscribed, specified, and ***809** "reasonable" cure period, the court cannot confirm the plan.

In re Erickson, 176 B.R. at 757–58. Courts typically focus on whether a plan that provides for a sale of property has the necessary specificity to show that the debtor will be able to make all payments contemplated under the plan in order to meet the feasibility requirement of § 1325(a)(6). *See, e.g., In re Milano*, 2012 WL 1965661 (Bankr. N.D. Ohio, May 31, 2012) (finding plan modification not feasible where there was a lack of specifics regarding the debtor's proposed sale plan); *In re Lynch*, 2009 WL 1955748, *5 (Bankr. E.D.N.Y. July 6, 2009) (denying confirmation because the debtor did not meet his burden to demonstrate feasibility of plan under §

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

1325(a)(6) where the plan did not specify the property subject to sale, did not project with sufficient certainty a timeframe or a date for a sale, and did not propose sale terms); *In re Erickson*, 176 B.R. at 756 (denying confirmation where the debtors' proposed plan did not specify terms of sale, when the sale was to be completed, or an alternative if the projected sale was unsuccessful); *In re Newton*, 161 B.R. at 218 (denying confirmation regarding eighteen month sale process and finding that debtors did not meet burden of demonstrating "the reasonableness and feasibility of their cure proposal, whether as to the means for effectuating it or as to the duration within which it is to be effected"). To meet the burden of demonstrating feasibility, therefore, a debtor may need to provide evidence as to marketing efforts, the terms of a sale, and generally show that the debtor is motivated to effectuate a sale process, as well as disclosing any other factors which may impact payment of the allowed secured claim. *Cf. In re Erickson*, 176 B.R. at 757–58. These requirements are not necessarily exhaustive, but are the starting points in guiding the Court's analysis for whether a plan could be confirmed over a creditor's objection and in determining feasibility of a plan.

[22] **[23]** **[24]** A plan must also be proposed in good faith in order to be confirmed. 11 U.S.C. § 1325(a)(3). The phrase "good faith" is undefined in the Code and "the legislative history provides little insight into its meaning." *Berliner v. Pappalardo (In re Puffer)*, 674 F.3d 78, 81 (1st Cir. 2012). The First Circuit has concluded that a "totality of the circumstances approach to adjudicating good faith should apply ... to inquiries under section 1325." *Id.* at 82. Although the test "cannot be reduced to a mechanical checklist[,]" *id.*, courts have considered the following circumstances when assessing whether a plan is proposed in good faith:

> (1) debtor's accuracy in stating her debts and expenses, (2) debtor's honesty in the bankruptcy process, including whether she has attempted to mislead the court and whether she has made any misrepresentations, (3) whether the Bankruptcy Code is being unfairly manipulated, (4) the type of debt sought to be discharged, (5) whether the debt would be dischargeable in a Chapter 7, and (6) debtor's motivation and sincerity in seeking Chapter 13 relief.

Sullivan v. Solimini (In re Sullivan), 326 B.R. 204, 212 (B.A.P. 1st Cir. 2005). Good faith is ultimately "a concept, not a construct" that "derives from equity." *In re Puffer*, 674 F.3d at 81. Wilmington appears to seek a bad faith determination premised on Mr. Gnaman's filing of a plan which requires a sale in order to be feasible. BoA argues that Mr. Materne's failure to address postpetition payments in a manner that would not increase postpetition arrears is bad faith. While the proposal of a sale plan alone is insufficient to establish bad faith, *see, e.g., In re Nardini*, No. 15-10244, 2015 WL 9438292, at *3 (Bankr. D. Vt. Dec. 23, 2015) (finding that filing a plan ***810** reliant on loan modification does not rise to the level of bad faith), a sale plan proposing sale periods that could run through the last month of the term of the plan, unaccompanied by milestones related to actual efforts to sell, such as the hiring of a broker or the listing of the property by a date certain, and, in Mr. Materne's case, the accrual of significant postpetition arrears, may constitute circumstances from which a lack of good faith might be inferred. In each case, evidence of the reason for a delay in the sale process will weigh in the determination of good faith.

IV. CONCLUSION

Applying the rulings and principles above, I will enter orders sustaining the objections of Wilmington and BoA to confirmation of the respective plans. Mr. Gnaman's plan provides for a lump-sum payment after periodic payments in contravention of § 1325(a)(5)(B)(iii) and does not provide for a specific sale process that would pay Wilmington's allowed secured claim at or a reasonable time after confirmation. As to Mr. Materne's plan, the debtor states that the proposed treatment of BoA's allowed secured claims is not intended to fit within with the provisions of § 1322(b)(3) or (b)(5). Because the plan calls for payments that are less than the contractual amount due until a sale that is to occur at an unspecified time during the life of the plan, the plan proposes an impermissible modification of the rights of BoA under § 1322(b)(2). In addition, the plan provides for a balloon payment in contravention of § 1325(a)(5)(B)(iii) and does not provide for a specific sale process that would pay BoA's allowed secured claims at or a reasonable time after confirmation.

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

As have other courts and commentators, I have struggled with the issues presented by the provisions of the Code governing treatment of claims secured by a home mortgage under a Chapter 13 plan. In some instances, arguments on each side of an issue are almost equally persuasive, but at the same time, unsatisfactory. These provisions of the Code would benefit from legislative amendment or appellate precedent that might make application of the statute more uniform, while retaining the flexibility governing the Chapter 13 plan process.

A separate order will enter in each debtor's case in accordance with this decision.

All Citations

640 B.R. 781, 71 Bankr.Ct.Dec. 125

Footnotes

1 The objections to confirmation raise questions of law that can be resolved on the pleadings without an evidentiary hearing. The facts referenced in this decision are either undisputed or from the Court's dockets of which I have taken judicial notice. *See* *LeBlanc v. Salem (In re Mailman Steam Carpet Cleaning Corp.)*, 196 F.3d 1, 8 (1st Cir. 1999) (observing "[t]he bankruptcy court appropriately took judicial notice of its own docket").

2 The Chapter 13 trustee, Denise M. Pappalardo (the "Trustee"), also objected to Mr. Gnaman's plan for failing to meet to the "best efforts" test under 11 U.S.C. § 1325(b)(1) (Case No. 19-40930, Dkt. No. 45) (the "Trustee's Objection"), alleging that the debtor does not devote all of his disposable income to the plan because his means test calculation is understated. *See* Tr. Obj.; Gnaman Tr. Obj. Resp. (Case No. 19-40930, Dkt. No. 49). The Court has entered a separate decision sustaining the Trustee's objection.

3 Unless otherwise noted, all section references herein are to Title 11 of the United States Code, 11 U.S.C. §§ 101, *et seq.*, as amended (the "Bankruptcy Code" or the "Code").

4 Mr. Gnaman names Select Portfolio Servicing, Inc. ("Select Portfolio") as the holder of Wilmington's claim in his plan. Select Portfolio is the servicer.

5 As explained by one commentator, "since October 1, 1979, the Bankruptcy Code has contemplated that a Chapter 13 plan must address all claims against the debtor; there is no such thing as paying a creditor 'outside the plan.' The phrase 'outside the plan' is a remnant from pre-Bankruptcy Code practice ... The inability to provide for secured debts without consent was explicitly changed by § 1322(b)(2) of the Bankruptcy Code and the pre-Bankruptcy Code practice of paying nonconsenting secured claims 'outside' the plan was effectively abolished. The Bankruptcy Code now allows for confirmation of a plan without the acceptance of secured creditors, and contemplates that all claims (including secured debt) will be dealt with through the Chapter 13 plan." 2019 No. 10 Norton Bankr. L. Adviser, Still the Same: Direct Payments In Chapter 13 Are "Payments Under the Plan," 1.

6 Wilmington's objection, as originally filed, focused on the plan's compliance with §§ 1322(b)(2) and 1325(a)(5)(B)(iii)(I). Wilmington stated that "a sixty month sale plan is unreasonable and does not comply" with the foregoing provisions. Wilmington Obj. ¶ 9 (Case No. 19-40930, Dkt. No. 36).

7 This is BoA's amended objection regarding the first mortgage as the initial objection erroneously addressed cure through modification instead of cure through sale.

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

8 Regarding the first mortgage, BoA has also moved for relief from the automatic stay with respect to the first mortgage, (Case No. 20-40027, Dkt. No. 62), which motion has been stayed pending resolution of the First Mortgage Objection, and for an interim distribution (Case No. 20-40027, Dkt. No. 119).

9 With respect to the Second Mortgage Objection, Mr. Materne filed a response denying allegations and stating the objection should be stricken because it was filed late. Debtor's Resp. (Case No. 20-40027, Dkt. No. 70). Given the circumstances of this case, including that similar issues need to be addressed in conjunction with the First Mortgage Objection, I decline to strike the Second Mortgage Objection.

10 Mr. Materne references both PNC Mortgage and BoA in the plan. PNC Bank is the servicer with respect to first mortgage as reflected in Claim No. 6.

11 The list in Mr. Materne's plan is misnumbered, as number six is missing.

12 In addition to a memorandum of law in support of its objection, *see* BoA Memo. of L. (Case No. 20-40027, Dkt. No. 90), BoA also filed a supplement to the First Mortgage Objection, stating that since the filing of the objection, two other judges in this District have considered similar confirmation objections in other cases, *In re Baptiste* (Case No. 19-13074) (Hoffman, J.) and *In re Suffoletta* (Case No. 20-10880) (Bostwick, J.), and have ruled from the bench that modification of a secured creditor's right to receive the contractual monthly payment due pursuant to the terms of its loan documents is impermissible. see BoA Suppl. (Case No. 20-40027, Dkt. No. 80). BoA provided the transcripts of the hearings as an attachment to the supplement at Dkt. No. 80.

13 Mr. Materne argues:

> It would be easy to read the plan as a “cure” plan, but the Debtor has not used the term “cure” in the plan. The Debtor has not listed the mortgage claims in part 3 of the plan. The Debtor is not treating the mortgage claims under 11 U.S.C. § 1322 (b) (3) or (5).
>
> Rather the Debtor is simply paying the claims in full through the sale of the property. It is completely unnecessary to use any provision of 11 U.S.C. § 1322 (b) for the full payment of a claim.

Materne Br. 5 (Case No. 20-40027, Dkt. No. 89).

14 As one commentator has observed regarding decisions reported after the effective date of BAPCPA, “[s]tartling and contradictory decisions interpreting new provisions of Chapter 13 are still an almost daily occurrence.” Keith M. Lundin, Lundin on Chapter 13, § 3.1, at ¶ 5, LundinOnChapter13.com (last visited April 6, 2022).

15 I recognize that this is, in part, a result of the intent of Congress to allow debtors certain flexibility in dealing with creditors. *See, e.g.*, *Ameriquest Mortg. Co. v. Nosek (In re Nosek),* 544 F.3d 34, 41 (1st Cir. 2008) (stating that “[§ 1322(b)] offers a Chapter 13 debtor flexibility in the formulation of her bankruptcy plan by listing various elements that the debtor may include in her plan”); *In re Cochran,* 555 B.R. 892, 899 (Bankr. M.D. Ga. 2016) (explaining that “[t]he legislative history of the original statutes indicates that Congress intended for debtors to have flexibility as to the property that is distributed on account of a secured creditor's claim.” (citations omitted); *In re Parker*, 15 B.R. 980, 985 (Bankr. E.D. Tenn. 1981), *aff'd sub nom. Matter of Parker*, 21 B.R. 692 (E.D. Tenn. 1982) (citing S.Rep.No.95-989, 95th Cong., 2d Sess. 141 (1978) and concluding Congress intended for debtors to have flexibility in dealing with their creditors).

16 It is clear that § 1325(a)(5)(B)(iii)(II) is not applicable as it applies only to personal property. 11 U.S.C. § 1325(a)(5)(B)(iii)(II). Courts have rejected that subsection (iii)(I) should similarly be construed as only applying to personal property. *See, e.g.*, *In re Lemieux*, 347 B.R. 460, 465 (Bankr. D. Mass. 2006) (rejecting the argument that the court should construe the language used in § 1325(a)(5)(B)(iii)(I) to pertain to personal

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

property only, and not real property, because of the explicit reference to personal property in § 1325(a)(5)(B)(iii)(II), citing to the fact that word "if" precedes both subsection (I) and (II), which are thus independent of one another).

17 Another difference not relevant to my determination is that (b)(3) also references "waiver" in addition to cure, As one commentator has noted,

> [l]ittle has been written concerning the term 'waiving' of defaults found in Code § 1322(b)(3), as contrasted with the "curing" of defaults. It can be postulated that to cure a default means to remedy a failure to perform a duty, i.e., to restore to a condition of full compliance, whereas the "waiving" of a default would mean a breach of duty or failure to perform is forgiven or ignored.

7 Norton Bankr. L. & Prac. 3d § 149:8.

18 Moreover, § 1322(c)(1) clarifies that: "[n]otwithstanding subsection (b)(2) and applicable nonbankruptcy law—(1) a default with respect to, or that gave rise to, a lien on the debtor's principal residence may be cured under paragraph (3) or (5) of subsection (b) until such residence is sold at a foreclosure sale that is conducted in accordance with applicable nonbankruptcy law." 11 U.S.C. § 1322(c)(1).

19 One court has suggested that "section 1322(c)(1), by its reference to section 1322(b)(3) and (5), usually applies to situations where the last payment of the secured claim on the original payment schedule is due after the date on which the final payment under a debtor's plan is due, i.e., *long term debt*." *In re Mendez*, 600 B.R. 321, 328 (Bankr. D.N.J. 2019). By contrast, "section 1322(c)(2) expressly applies to secured claims *on which the last payment comes due prior to the last payment under a chapter 13 plan*. In looking to cure a default on a fully matured debt over a period of time, absent the consent of the creditor, a debtor does not have a choice, a debtor can only address a default under section 1322(b)(3) through section 1322(c)(2)." *Id*. at 329.

20 The legislative history regarding § 1322(b) appears to support this reading:

> Section 1322(b)(2) of the House amendment represents a compromise agreement between similar provisions in the House bill and Senate amendment. Under the House amendment, the plan may modify the rights of holders of secured claims other than a claim secured by a security interest in real property that is the debtor's principal residence. It is intended that a claim secured by the debtor's principal residence may be treated with under Section 1322(b)(5) of the House amendment. (emphasis added).

124 Cong. Rec. S. 17, 423 (1978).

21 Some courts have concluded that § 1322(b)(5) is not implicated at all when long-term debt is paid directly by the debtor where no cure of arrearages or other defaults is necessary or full amount of the claim is being paid over the life of the plan. *See, e.g.*, *Matter of Chappell,* 984 F.2d 775, 781 (7th Cir. 1993) (determining, in the context of concluding that second mortgage debt not exempted from discharge by operation of § 1328(a)(1), that debtor did not avail himself § 1322(b)(5) because debtor proposed accelerating the second mortgage and paying it in full during the five years in which the plan was in effect, suggesting that § 1322(b)(5) is only applicable where the full amount of the secured claim is not paid during the case); *In re Rogers*, 494 B.R. 664, 669 (Bankr. E.D.N.C. 2013) ("§ 1322(b)(5) does not except the debt forming the basis of [creditor]'s claim from discharge because the debtors' confirmed plan did not contain a provision to cure prepetition arrears or default."); *Citizens Bank v. Cramer (In re Cramer)*, 477 B.R. 736, 739–740 (Bankr. E.D. Wis. 2012) (concluding postconfirmation deficiency judgment on travel trailer was dischargeable where plan provided for debtors to maintain on-going payments directly but did not make specific reference to or provide for cure under § 1322(b)(5)); *In re Starkey*, No. 15-00659, 2016 WL 3034738, at *1–2 (Bankr. D.D.C. May 18, 2016) (overruling confirmation objection and concluding claim being paid directly in its entirety by debtor leaves claim unaffected for purposes of § 1322(b)(2) because the creditor's claim is unaltered); *In re Kent*, No. BR

09-35124-TMB13, 2016 WL 9488860, at *4 (Bankr. D. Or. Jan. 22, 2016) (holding that "for a claim under § 1322(b)(5), the plan must cure a default. Because there was no default, and therefore no cure, the [m]ortgage was not provided for under § 1322(b)(5) and the exception to discharge enumerated in § 1328(a)(1) does not apply"); *but see In re Dukes*, No. 9:09-BK-02778-FMD, 2015 WL 3856335, at *5 (Bankr. M.D. Fla. June 19, 2015), *aff'd*, No. 2:15-CV-420-FTM-99, 2016 WL 5390948 (M.D. Fla. Sept. 27, 2016), *aff'd*, 909 F.3d 1306 (11th Cir. 2018) ("[W]hen [a] claim is 'long term debt' and the plan proposes for the debtor to maintain payments, the claim is provided for under § 1322(b)(5) and excepted from discharge under § 1328(a)(1). This is the case ... even if payments are current on the petition date and there is no default to be cured.").

22 At least in a case that has not been previously converted, a debtor may dismiss a Chapter 13 case any time as a matter of right. *See* 11 U.S.C. § 1307(b). Because of that, the risk of non-performance under a sale plan after a delayed sale would be shouldered by the mortgagee and, to a lesser extent, other plan constituents who may be paid from the proceeds.

23 Even if a debtor could propose to cure defaults on long-term debt under § 1322(b)(3), I would construe the Code to impose a reasonableness requirement as an element of good faith even where the statute does not use that term.

24 Several commentators have noted that it would seem that a single payment from the proceeds of a sale (and no other payments before that payment) would be permissible in a case where debt is secured by real property, but the inclusion of monthly payments would prevent confirmation. *See generally* 8 Collier on Bankruptcy ¶ 1325.06 ("Because section 1325(a)(5)(B)(iii)(I) only applies if the plan provides for periodic payments, it also does not preclude a plan providing for a single lump sum payment to a creditor. The requirement also does not apply to payments made to cure a default on a long term debt pursuant to section 1322(b)(5) [citing only *In re Davis*, 343 B.R. 326, (Bankr. M.D. Fla. 2006), which held that the enactment of § 1322(e) makes § 1325(a)(5) inapplicable to cure of long-term debt, for this proposition (*see also infra*, at n.25 for further discussion of *Davis*)]. However, the provision does appear to preclude, absent a creditor's acceptance, a plan that provides for a series of payments followed by a balloon payment in a larger amount."); Lundin on Chapter 13, § 74.14, at ¶ 7 ("Not answered by [the cases reading § 1325(a)(5)(B)(iii) to prohibit the use of balloon payments by sale where periodic payments are also contemplated] is the question whether a pure refinance or balloon payment plan—one that does not include periodic payments—would be subject to the equal monthly payment requirement in § 1325(a)(5)(B)(iii). Such a plan would still have to satisfy the condition in § 1322(b)(5) that defaults be cured within a 'reasonable time.' But both sections function without conflict when a plan cures arrearages with a single payment within a reasonable time after confirmation.") The timing of the lump sum would be critical in such a circumstance and would appear to be relatively limited to circumstances where sales or refinancings were imminent. These commentators do not address how a single lump-sum payment plan would comply with the maintenance requirements of § 1322(b)(5) or the anti-modification of § 1322(b)(2) where the secured claim is a home mortgage with a final payment due after the plan term. They may assume, without discussion, that maintenance payments are not "provided for by the plan" so that those periodic payments would not trigger the equal payment provision of § 1325(a)(5)(B)(iii).

25 I disagree with the conclusion of *Davis* that *Rake* has been entirely superseded by § 1322(e) regarding its application of § 1325(a)(5). *See In re Davis*, 343 B.R. at 328. I agree with other courts that have not followed *Davis* because § 1322(e) only addressed the amount necessary for cure, not the applicability of § 1325(a)(5)(B), and that "nothing in section 1322(b)(5), 1322(e) or 1325(a)(5)(B) indicates that section 1325(a)(5)(B) does not apply to the cure and maintenance of a secured claim through a plan other than on the issue of the amount necessary for cure." *In re Miceli*, 587 B.R. 492, 503 (Bankr. N.D. Ill. 2018); *see also In re Hamilton*, 401 B.R. 539 (1st Cir. BAP 2009); *In re Spark*, 509 B.R. 728 (Bankr. M.D. Fla. 2014). As will be discussed, *Rake* has been distinguished for other reasons by other courts.

 © 2024 Thomson Reuters. No claim to original U.S. Government Works.

26 While not referenced in *Lopez*, that court's interpretation of "provided for" in § 1325(a)(5) might also resolve the question of how the equal payments requirement of § 1325(a)(5)(B)(iii) could apply to "maintenance" payments where the allowed secured claim is based on an adjustable-rate home mortgage where, contractually, the amount of monthly payments will likely change during the term of the plan. By viewing maintenance payments made directly by debtors as not provided for by the plan, a court would not apply the equal payments provision to those payments. This would not resolve the question in so-called "conduit" districts where all payments to mortgage holders are disbursed by the Chapter 13 trustee, as opposed to districts in which the debtor makes ongoing mortgage payments directly to the mortgagee. *See, e.g.,* Gordon Bermant & Jean Braucher, *Making Post-Petition Mortgage Payments Inside Chapter 13 Plans: Facts, Law, Policy*, 80 Am. Bankr. L.J. 261, 261 (2006) (describing disbursements of ongoing, postpetition mortgage payments by trustees as "conduit payments"). I have not located any published decisions where courts have addressed this apparent "anomaly" in the statute.

27 While I address "maintenance payments" in the context of § 1322(b)(5), as discussed above, a plan providing for a purported cure under § 1322(b)(2) of an unmatured home mortgage would have to provide for similar contractual payments to avoid running afoul of the anti-modification provision of § 1322(b)(2).

28 Mr. Materne argues that § 1322(b)(11) (providing that "a plan may include any other appropriate provision not inconsistent with this title") may be the basis for his plan provision paying adequate protection. In other circumstances, it may be appropriate for a plan to provide for adequate protection payments to a secured lender, but naming periodic payments "adequate protection payments" does not eliminate a debtor's obligations not to modify a home mortgage or to comply with more specific provisions of § 1322(b) nor § 1325(a)(5).

29 It is also difficult to conceive a debtor who in good faith wishes to cure a significant prepetition arrears through a sale, rather than just buy time through a plan that may not be consummated, would not endeavor to take deliberate steps to sell the property.

30 Notably, Wilmington does not take the position that sale plans are per se unconfirmable where a secured creditor does not accept the plan, stating:

> If unable to obtain the assent of the affected secured creditor, a Chapter 13 debtor must walk a fine line of putting forth a plan which both satisfies the requirements of § 1325(a)(5) while, at the same time, being able to show that the creditor at issue is adequately protected during the limited and clearly defined sale term of the plan. For example, if a debtor proposed a sale plan which indicated that the property at issue would be sold within a six month time frame, provided that the property had sufficient equity, it would seem that the creditor would not be entitled to relief from the automatic stay during this time frame. For that reason, the debtor would presumably need not propose payments to the creditor during such sale period. As such, the Debtor would not be burdened with the task of satisfying the "equal monthly amounts" provision of § 1325(a)(5)(B)(iii)(I) as the plan would not contemplate "periodic payments."

Wilmington Br. 6. (Case No. 19-40930, Dkt. No. 67).

End of Document © 2024 Thomson Reuters. No claim to original U.S. Government Works.

PUBLISHED

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 22-1328

JOSEPH A. BLEDSOE, III,

Petitioner - Appellant,

v.

ROBERT BURNS COOK, JR.; CHERYL LOTT COOK,

Respondents - Appellee.

On Appeal from the United States Bankruptcy Court for the Eastern District of North Carolina, at Wilmington. Stephani W. Humrickhouse, Bankruptcy Judge. (21-01059-5-DMW)

Argued: May 4, 2023 Decided: June 14, 2023

Before THACKER and HEYTENS, Circuit Judges, and KEENAN, Senior Circuit Judge.

Affirmed by published opinion. Judge Heytens wrote the opinion, in which Judge Thacker and Judge Keenan joined.

Joseph A. Bledsoe, III, CHAPTER 13 TRUSTEE, New Bern, North Carolina, for Appellant. Richard Preston Cook, RICHARD P. COOK, PLLC, Wilmington, North Carolina, for Appellees.

TOBY HEYTENS, Circuit Judge:

Can Chapter 13 bankruptcy filers who earn more than the median income use their actual mortgage payments when calculating how much they can afford to pay unsecured creditors? Joining the Sixth and Ninth Circuits, we hold the answer is yes.

I.

In 2021, Robert and Cheryl Cook filed a voluntary petition under Chapter 13 of the Bankruptcy Code. That type of bankruptcy allows individual debtors "to obtain a discharge" so long as they pay their "creditors a portion of [their] monthly income in accordance with a court-approved plan." *Ransom v. FIA Card Servs., N.A.*, 562 U.S. 61, 64 (2011). "To determine how much income" debtors are "capable of paying, Chapter 13 uses a statutory formula known as the means test" to calculate debtors' "disposable income." *Id.* (quotation marks omitted).

The Cooks calculated their disposable income using Official Form 122C-2. As the form instructs, the Cooks entered the relevant "National and Local Standards" for their monthly costs for food, clothing, utilities, out-of-pocket healthcare, and vehicles.[1] The Cooks next listed the monthly amounts they pay for "Other Necessary Expenses" (as relevant here, taxes and life insurance). Finally, the Cooks recorded two "Deductions for Debt Payments" to secured creditors, including, crucially, their monthly mortgage

[1] The National and Local Standards are tables listing uniform amounts for necessities, which are prepared by the IRS to help estimate a person's ability to pay delinquent taxes. See Internal Revenue Manual §§ 5.15.1.9 (Aug. 29, 2018), 5.15.1.10 (Nov. 22, 2021), https://www.irs.gov/irm/part5/irm_05-015-001.

payment. After subtracting these amounts, the Cooks reported a monthly disposable income of $253.27, which would be used to repay unsecured creditors.

The bankruptcy trustee objected to the Cooks' proposed Chapter 13 plan. The trustee acknowledged the Cooks followed the instructions on Official Form 122C-2. The trustee maintained, however, that the form was wrong because the Bankruptcy Code only allowed the Cooks to claim the relevant Local Standards amount for their "Mortgage/Rent" deduction ($1,098) rather than their actual monthly payment ($2,233.34). Thus, the trustee reasoned, the Cooks' plan shortchanged unsecured creditors by $1,135.34 each month.

The bankruptcy court disagreed. "By correctly filling out Form 122C-2 and listing their entire mortgage payment," the court stated, the Cooks "followed the plain language of the Bankruptcy Code." JA 98. The court overruled the trustee's objection and confirmed the Cooks' plan.

The trustee asked the bankruptcy court to certify an appeal directly to this Court under 28 U.S.C. § 158(d)(2)(A). The bankruptcy court did so, concluding the case "involves a matter of public importance and a question of law requiring a resolution of conflicting decisions within the Eastern District of North Carolina, and because an immediate appeal may materially advance the progress of this case." JA 115–16 (citing § 158(d)(2)(A)). This Court granted the petition to appeal. We review interpretations of the Bankruptcy Code de novo. See *Johnson v. Zimmer*, 686 F.3d 224, 227 (4th Cir. 2012).

II.

We join the Sixth and Ninth Circuits in holding the Chapter 13 means test permits above-median income debtors to deduct the actual costs of their mortgage payments when

calculating their disposable income. See *In re Welsh*, 711 F.3d 1120, 1130 (9th Cir. 2013); *Baud v. Carroll*, 634 F.3d 327, 349 (6th Cir. 2011). We thus affirm.

A.

The relevant statutory provisions—though intricate—are straightforward. Because of the trustee's objection, the bankruptcy court could only approve the Cooks' proposed Chapter 13 plan if the plan made all "projected disposable income" available to unsecured creditors. 11 U.S.C. § 1325(b)(1)(B). Disposable income, in turn, means "current monthly income received by the debtor" minus "amounts reasonably necessary to be expended." § 1325(b)(2). And for above-median income debtors like the Cooks, the Bankruptcy Code instructs that "[a]mounts reasonably necessary to be expended . . . shall be determined in accordance with subparagraphs (A) and (B) of section 707(b)(2)." § 1325(b)(3).

We thus turn to Section 707(b)(2). The first provision of subparagraph A—which we will call Clause One—provides:

> In considering under paragraph (1) whether the granting of relief would be an abuse of the provisions of this chapter, the court shall presume abuse exists if the debtor's current monthly income reduced by the amounts determined under clauses (ii), (iii), and (iv), and multiplied by 60 is not less than the lesser of [two specified thresholds].

11 U.S.C. § 707(b)(2)(A)(i).[2] The three clauses referenced in Clause One—which we will call Clause Two, Clause Three, and Clause Four—address "[t]he debtor's monthly

[2] The referenced "paragraph (1)" says a bankruptcy court may dismiss a filing under Chapter 7 "if it finds that the granting of relief would be an abuse under the provisions of this chapter." 11 U.S.C. § 707(b)(1). The other subparagraph referenced in Section 1325(b)(3) allows a debtor to rebut any presumption of abuse created by Clause One by

expenses," "[t]he debtor's average monthly payments on account of secured debts," and "[t]he debtor's expenses for payment of all priority claims," respectively. 11 U.S.C. § 707(b)(2)(A)(ii), (iii), (iv). As relevant here, Clause Three instructs: "The debtor's average monthly payments on account of secured debts shall be calculated as the sum of . . . the total of all amounts scheduled as contractually due to secured creditors in each month of the 60 months following the date of the filing of the petition." § 707(b)(2)(A)(iii)(I).

Now apply those rules here. Everyone agrees the mortgage on the Cooks' house is a "secured debt[ ]." 11 U.S.C. § 707(b)(2)(A)(iii). Accordingly, Clause Three says the Cooks' "average monthly payments on account of" that mortgage "shall be calculated" based on the amounts "contractually due to secured creditors," § 707(b)(2)(A)(iii)(I)—that is, what the Cooks owe under their mortgage agreement. Performing that calculation, the Cooks reached an average monthly payment of $2,233.34. Then, Clause One tells the Cooks to "reduce[ ]" their "current monthly income" "by the amount[ ] determined under" Clause Three. § 707(b)(2)(A)(i). Thus, the Cooks subtracted $2,233.34 (and other uncontested amounts) from their current monthly income to reach a disposable income of $253.27. Easy-peasy.

---

demonstrating "special circumstances." U.S.C. § 707(b)(2)(B). See p. 9, *infra* (discussing that provision).

B.

The trustee offers a flurry of arguments against this straightforward reading. We are unpersuaded.

In essence, the trustee asserts the critical provision here is Clause Two—specifically, the first sentence of Clause Two's five subparts about how to calculate "[t]he debtor's monthly expenses." 11 U.S.C. § 707(b)(2)(A)(ii)(I). The language the trustee relies on reads:

> The debtor's monthly expenses shall be the debtor's applicable monthly expense amounts specified under the National Standards and Local Standards . . . issued by the Internal Revenue Service for the area in which the debtor resides, as in effect on the date of the order for relief[.]

Id. Because the Local Standards contain allowances for "[h]ousing expenses"—*and* define that term to include "mortgage (including interest)," Internal Revenue Manual § 5.15.1.10.1 (Nov. 22, 2021); see note 1, *supra*—the trustee insists the Cooks must use the lower, Local Standard number rather than their actual mortgage payment.

The trustee's argument fails multiple times over. To start, it violates "the first rule of . . . statutory interpretation," which is: "Read on." *Arkansas Game & Fish Comm'n v. United States*, 568 U.S. 23, 36 (2012). Just two sentences after the language the trustee relies on, Clause Two states: "Notwithstanding any other provision of this clause, the monthly expenses of the debtor shall not include any payments for debts." 11 U.S.C. § 707(b)(2)(A)(ii)(I). A home mortgage is, of course, a debt. Thus, read in full, Clause Two

declares that the National and Local Standards govern a debtor's "monthly expenses," while clarifying mortgage payments are not "monthly expenses." *Id.*[3]

The trustee gamely insists the "notwithstanding" clause precludes the Cooks from deducting their actual mortgage payments under Clause Three. But the trustee does not explain how a directive limited to "this clause" (that is, Clause Two) somehow extends to Clause Three. Nor does the trustee clarify how an instruction about "monthly expenses" should apply to Clause Three, which never uses that term.

Making matters worse, the trustee's argument also finds no support in the text of Clauses One and Three. Nothing in Clause One says debtors may "reduc[e]" their current monthly income "by the amount[ ] determined under" Clause Three *only* if that amount turns out to be less than the Local Standard referenced in Clause Two. 11 U.S.C. § 707(b)(2)(A)(i). Nor does Clause Three suggest that debts secured by a person's home receive less favorable treatment than other types of secured debt for which there may be no relevant National or Local Standard. Quite the contrary. Beyond allowing debtors to deduct the full amount of their "contractually due" mortgage payments, Clause Three allows debtors to deduct "any additional payments to secured creditors necessary for the

[3] A reader wondering why the IRS would have gone to the trouble of preparing county-level housing-cost figures if those amounts were inapplicable to debtors like the Cooks should recall the Standards were not created for bankruptcy purposes, but (as the trustee concedes) to assess delinquent tax liability. It makes sense then that, rather than reinvent the wheel, the means test would adopt the National and Local Standards for calculating debtors' monthly expenses. This rare display of federal efficiency does not compel this Court to adopt a mangled reading of the means test. Cf. *Ransom*, 562 U.S. at 72 ("[T]he IRS's explanatory guidelines to the National and Local Standards . . . of course cannot control if they are at odds with the statutory language.").

debtor . . . to maintain possession of the debtor's primary residence." § 707(b)(2)(A)(iii). This provision cannot be squared with the trustee's view that the means test could leave debtors like the Cooks with insufficient funds to pay their mortgage in the first place.[4]

The trustee asserts Clause Three merely tells debtors how to *calculate* their average monthly payments on secured debts but does not authorize debtors to deduct the resulting amount from their gross monthly income. True, nothing in Clause Three itself allows the Cooks to subtract the calculated amounts from their monthly income. But Clause One does. Indeed, Clause One tells debtors to deduct "the amounts determined under" Clause Three from their monthly income in the same sentence and with the same language in which it tells debtors to do the same for Clauses Two and Four. See 11 U.S.C. § 707(b)(2)(A)(i) ("the debtor's current monthly income reduced by the amounts determined under clauses (ii), (iii), and (iv)").[5]

The trustee's "Clause Three as calculator" theory faces another problem: It is not obvious why Clause Three would tell debtors to calculate a figure (and how to do it) unless the resulting number had some real-world purpose. Undeterred, the trustee responds that those calculations do have practical effect—they provide the maximum amount the Cooks

[4] In *Lynch v. Jackson*, 853 F.3d 116 (4th Cir. 2017), this Court held that two above-median income debtors whose home mortgage and car loan expenses were less than the amount listed in the Local Standards were "entitled to the full National and Local Standard amount." *Id.* at 118. As the trustee acknowledges, that decision did not consider or discuss the applicability of Clause Three to a mortgage debt. See Oral Arg. 13:34–14:13.

[5] The trustee notes that Clause Three (unlike Clauses Two and Four) does not contain the word "expense." But then, neither does Clause One. All four clauses, however, use the same word to discuss the thing being deducted: "amounts." See 11 U.S.C. § 707(b)(2)(A).

may deduct *if* they prove to the bankruptcy court the amount above the relevant Local Standard is "reasonable." Oral Arg. 4:40–5:04; see *id.* at 1:07–10. As support for this view, the trustee points to a provision—which we will call Subparagraph B—stating a debtor may "rebut[]" a "presumption of abuse" generated under Subparagraph A "by demonstrating special circumstances" that "justify additional expenses or adjustments of current monthly income for which there is no reasonable alternative." 11 U.S.C. § 707(b)(2)(B)(i); see note 1, *supra*.

That view comes with its own host of problems. For one thing, saying a debtor may rebut a presumption of abuse by showing special circumstances is different from saying a bankruptcy court may permit deductions for any debts the court concludes are reasonable. What is more, Subparagraph B only allows bankruptcy courts to assess a debtor's special circumstances if their petition is shown to be presumptively abusive under Subparagraph A; it does not alter whether and how much a debtor may deduct for secured debts as a matter of course. And nothing in Clause Three suggests there is "any qualification or limitation on the kind of secured debt that is deducted from current monthly income." *Welsh*, 711 F.3d at 1134.

At bottom, the trustee's plea for a reasonableness limitation sounds in public policy. Like the Ninth Circuit, we recognize our interpretation of Clause Three means "debtors could make secured payments on luxury or comfort items"—or expensive home mortgages—"with the result that little 'disposable income,' as that figure is calculated, remains to pay unsecured creditors." *Welsh*, 711 F.3d at 1130. One might reasonably object

to favoring one type of creditor over another or limiting a bankruptcy court's discretion to decide which debt payments are reasonable or should take priority.

"As usual," however, "there are (at least) two sides to the policy question before us," and "a rational Congress could reach the policy judgment the statutory text suggests it did." *Niz-Chavez v. Garland*, 141 S. Ct. 1474, 1486 (2021). The current statutory regime was introduced in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, which sought "to correct perceived abuses of the bankruptcy system." *Milavetz, Gallop & Milavetz, P.A. v. United States*, 559 U.S. 229, 231 (2010). In particular, the means test "supplants the [previous] practice of calculating debtors' reasonable expenses on a case-by-case basis"—a regime that "led to varying and often inconsistent determinations." *Ransom*, 562 U.S. at 65. Because "Congress made a conscious effort to cabin the discretion of bankruptcy judges" by removing the power to determine "what is or is not 'reasonably necessary,' " *Welsh*, 711 F.3d at 1130, 1134 (some quotation marks omitted), we decline to interpret the statute to restore the very power Congress removed.

* * *

The Cooks were entitled to use their average monthly mortgage payments when calculating their disposable income. The order of the bankruptcy court is thus

AFFIRMED.

UNITED STATES BANKRUPTCY COURT

DISTRICT OF NEW MEXICO

In re: VENITIA DAWN MORENO, No. 22-10886-j13

Debtor.

MEMORANDUM OPINION

The Chapter 13 Trustee ("Trustee") objects to confirmation of Debtor's chapter 13 plan on the ground that the plan fails to satisfy the projected disposable income requirement of 11 U.S.C. § 1325(b)(1)(B).[1] More specifically, the Trustee objects that Debtor, whose current monthly income is above the median income for a family of the same size, is not entitled to deduct the entire amount of the Internal Revenue Service ("IRS") Local Standard for Housing and Utilities[2] in computing disposable income because she is not obligated on a home mortgage, and her fiancé pays the entire mortgage expense for the home where they jointly reside (the "Threshold Legal Issue").[3] Debtor asserts that she is entitled to deduct the entire amount of the IRS Local Standard for Housing and Utilities.

At a status conference on plan confirmation held July 18, 2023, the parties asked the Court to decide the Threshold Legal Issue on stipulated facts. With the consent of the parties, the Court entered an order directing Debtor and the Trustee to file stipulated facts and simultaneous briefs on the Threshold Legal Issue. Debtor and the Trustee subsequently filed a Statement of

[1] All future statutory references in this Memorandum Opinion are to title 11 of the United States Code, unless otherwise specified. Title 11 of the United States Code is referred to as the "Bankruptcy Code" or simply the "Code." All cited websites were last visited on December 4, 2023.

[2] The IRS Local Standard for Housing and Utilities is sometimes referred to as the "Housing and Utilities Standard."

[3] The Trustee argues, in the alternative, that if the Court rules that Debtor is entitled to the entire IRS Local Standard for Housing and Utilities deduction, the amount of the fiancé's mortgage payment should be included in Debtor's current monthly income and her fiancé should be included in her household size.

Stipulated Facts ("Stipulated Facts" – Doc. 39) and simultaneous briefs (Docs. 36 and 38) relating to the Threshold Legal Issue.

The Court has considered the parties' positions in light of the Stipulated Facts and applicable law. The Court concludes that Debtor may deduct the entire amount the IRS has specified for the Local Standard for Housing and Utilities in the applicable locality in computing disposable income even though she has no liability for a home mortgage, she does not pay any home mortgage expenses, and the only expenses she pays in the Housing and Utilities category are for cell phone service and seasonal fuel costs.

STIPULATED FACTS[4]

Debtor and the Trustee have stipulated to the following facts only for purposes of the Court deciding the Threshold Legal Issue:

1. Debtor filed a voluntary petition for relief under chapter 13 of the Bankruptcy Code on October 31, 2023.

2. On the same date, Debtor filed her Schedules, Statement of Financial Affairs, Forms 122C-1 and 122C-2, and Chapter 13 plan.

3. Debtor's household size is two, consisting of Debtor and her 26-year-old daughter.

4. Debtor has been engaged to her fiancé for five years and they have lived together for ten years. No date is set for the wedding.

5. Debtor's fiancé is not included as a member of Debtor's household for purposes of the bankruptcy.

[4] The entirety of the Statement of Stipulated Facts (Doc. 39) is incorporated herein by reference. The Court re-states in this Memorandum Opinion those the facts contained in the Statement of Stipulated Facts necessary to resolve the Threshold Legal Issue.

6. Debtor's fiancé's income was not included in Debtor's original Form 122C-1, Schedule I, or

amended Form 122C-1.

7. Debtor's average monthly income for the six-month period prior to the filing of the voluntary petition was $8,802.07.

8. Debtor's current monthly income for the year equates to $105,624.84.

9. The median family income for a two-person household is $60,728.00.

10. Debtor is an above-median-income debtor.

11. Debtor's fiancé pays the mortgage, which is escrowed for both taxes and insurance, in the monthly amount of $1,300.00.

12. Debtor's fiancé pays all utilities, including electricity, gas, propane, water and sewer averaging $300.00 monthly. Debtor does not contribute to these expenses.

13. Debtor pays the monthly household cellular telephone expenses in the average amount of $450.00. The cellphone expense includes cellphones and Apple Watches for Debtor, her daughter, and her fiancé.

14. In the winter months, Debtor pays for pellets used in a pellet stove that Debtor and her fiancé use to decrease gas and propane utilities costs. The pellet fuel costs $280.00 to $300.00 per month, which averages to approximately $25.00 per month over the year. Debtor's fiancé does not contribute to that expense.

15. The Local Housing and Utilities Standard for a two-person household in Bernalillo County, New Mexico, for cases filed between May 15, 2022, and October 31, 2022 was $1,804.00.

16. The Housing and Utilities Standard covers mortgage or rent, property taxes, interest,

insurance, maintenance, repairs, gas, electric, water, heating oil, garbage collection, telephone (landline), cell phone, internet, and cable.

17. The amount of the Local Standard for Housing and Utilities, as used in Form 122C-2, is $599.00 for non-mortgage expenses (line 8) and $1,205.00 for mortgage/rent expenses (line 9).

18. Debtor's Form 122C-2 includes a deduction for housing and utilities expenses (lines 8 and 9).

19. Debtor's amended Form 122C-2 likewise includes a deduction for both housing and utilities expenses (lines 8 and 9).

20. Debtor's projected disposable income on line 45 of Amended Form 122C-2 is negative $236.77.

21. Debtor's sixty (60) month chapter 13 plan proposes to pay $0.00 to non-priority unsecured creditors.

22. If Debtor's mortgage/rent and utility standard deductions were removed from Amended Form 122C-2, Debtor's projected disposable income on line 45 would be $1,567.23, which would result in $94,033.80 to be paid to non-priority unsecured creditors (93% of the amount owed to non-priority unsecured creditors).

Jurisdiction, standing, and venue

The Court has jurisdiction to hear and determine the Trustee's objection to confirmation of Debtor's chapter 13 plan pursuant to 28 U.S.C. §§ 1334 and 157(a) and the order of reference contained in the Administrative Order entered by the United States District Court for the District of New Mexico in Misc. No. 84-0324. This matter, which involves confirmation of a chapter 13

plan, is a core proceeding under 28 U.S.C.§ 157(b)(2)(L). Venue is proper pursuant to 28 U.S.C. § 1409.

There is no doubt that Debtor has standing. The Trustee has statutory standing under § 1302(b)(2)(B) (which requires that the trustee appear and be heard at any hearing that concerns confirmation of a plan) and § 1325(b)(1)(B) (which requires a plan to provide for payment of projected disposable income to unsecured creditors if the trustee or holder of an allowed unsecured claim objects to plan confirmation).

The parties must also have Article III standing.[5] The Trustee, as representative of the bankruptcy estate, is charged with representing the interests of all creditors as a whole, including the interests of unsecured creditors.[6] The Trustee has Article III standing, acting in her representative capacity, to ensure that confirmation of the plan meets the requirements of the Bankruptcy Code with respect to its treatment of the claims of non-priority unsecured creditors.[7]

DISCUSSION

The Court will discuss, in this order: (i) the formula under the Bankruptcy Code for determining disposable income; (ii) why the IRS adopted National and Local Standards, how the IRS applies the Local Standard for Housing and Utilities, and the IRS's refusal to adapt its standards for bankruptcy purposes; (iii) the incorporation of the Local Standard for Housing and Utilities in Official Form 122C-2 ("Form 122C-2"); (iv) whether the Local Standard for Housing and Utilities is "applicable" if the debtor has no mortgage or rent expense but has at least one

[5] *See In re Pettine,* __ B.R.__, BAP No. 23-013, 2023 WL 7648619, at *8 (10th Cir. BAP Nov. 15, 2023) (holding that parties must have Article III standing before the bankruptcy court).
[6] *In re Cumbess*, 960 F.3d 1325, 1331 (11th Cir. 2020)*; In re Liles*, 292 B.R. 138, 139 (Bankr. E.D. Tex. 2002).
[7] The Trustee's Article III standing is similar to the Article III standing of an Official Committee of Unsecured Creditors in a chapter 11 case, acting in a representative capacity, to protect the interests of unsecured creditors as a whole.

expense within the Local Standard for Housing and Utilities; and (v) whether the division of the Local Standard for Housing and Utilities into two categories is consistent with the requirements of the Bankruptcy Code. Ultimately, the Court agrees with the holding and careful analysis in *In re Currie,* 537 B.R. 884 (Bankr. C.D. Ill. 2015), which held that a debtor is entitled to deduct the full IRS Local Standard for Housing and Utilities in calculating disposable income where the debtor did not have any mortgage indebtedness and the debtor's only housing expenses were for insurance, maintenance, and utilities associated with a home.

The statutory formula for determining disposable income

If the chapter 13 trustee or the holder of an allowed unsecured claim objects to confirmation of a debtor's chapter 13 plan, the court may not approve the plan unless "the plan provides that all of the debtor's projected disposable income to be received in the applicable commitment period . . . will be applied to make payments to unsecured creditors under the plan." § 1325(b)(1)(B).[8] Section 1325(b)(2) defines "disposable income"[9] as the debtor's "current monthly income"[10] less "amounts reasonably necessary to be expended" for the maintenance or support of the debtor and the debtor's dependents. § 1325(b)(2). For debtors whose current monthly income is above the median income for a family of the same size, amounts reasonably necessary to be expended for the maintenance or support of the debtor and the debtor's dependents (i.e., the debtors' deductible expenses) are to be determined in accordance with § 707(b)(2)(A) and (B).[11] The parties have stipulated for purposes of resolving the Threshold

[8] *See In re Currie*, 537 B.R. 884, 887 (Bankr. C.D. Ill. 2015) ("Generally, if an objection has been filed, a Chapter 13 plan must provide for contribution of all of a debtor's projected disposable income for the applicable commitment period to the payment of unsecured creditors.").
[9] "*Projected* disposable income" is not defined in the Code. *Hamilton v. Lanning*, 560 U.S. 505, 509, 510 (2010).
[10] "Current monthly income" is defined in § 101(10A).
[11] § 1325(b)(3).

Legal Issue that Debtor's current monthly income is above the median income for the size of Debtor's family.

The income side of the calculation of Debtor's current monthly income is not part of the Threshold Legal Issue addressed in this opinion. Debtor's expenses to be deducted from her currently monthly income in calculating disposable income requires use of the IRS National and Local Standards.[12]

The IRS National and Local Standards, including a discussion of the Local Standard for Housing and Utilities

The IRS has established National and Local Standards as part of its Collection Financial Standards to provide a basis for analyzing "a taxpayer's ability to pay delinquent tax liabilities, which enables [IRS] Collection employees to make appropriate collection decisions to resolve cases." Internal Revenue Manual ("IRM"),[13] § 5.15.1.1(1) (updated 08-29-2018).[14] The IRS policy for use of National and Local Standards is that "[t]axpayers will normally be allowed the

[12] *See In re Lanning*, 545 F.3d 1269, 1272 n.2 (10th Cir. 2008) ("Section 1325(b)(3) . . . provide[s] that expenses for above-median debtors must be calculated in accordance with 11 U.S.C. § 707(b)(2)(A) & (B) . . . . [and] requires the use of National and Local IRS Standards in determining expenses and deductions . . . . "), *aff'd sub nom. Hamilton v. Lanning*, 560 U.S. 505 (2010); *Currie*, 537 B.R. at 893 ("The plain language of the Code requires over-the-median income debtors to calculate disposable income through the use of the IRS National and Local Standards for certain expenses rather than by using actual expenses."); *In re Farrar-Johnson*, 353 B.R. 224, 231 (Bankr. N.D. Ill. 2006) ("Section 707(b)(2)(A)(ii)(I) . . . deems the debtor's expenses to be the 'amounts specified' in the [IRS] Local Standards."); *In re Hardacre*, 338 B.R. 718, 723 (Bankr. N.D. Tex. 2006) ("In arriving at projected disposable income for a debtor above the applicable median family income benchmark, section 707(b)(2)(A)(ii)(I) permits the debtor to deduct certain standard expense allowances that have been developed by the Internal Revenue Service.").

[13] The IRM is the official compilation of IRS policies, procedures, and guidelines. IRM, § 1.11.6.2(1) (updated 03-23-2022), https://www.irs.gov/irm/part1/irm_01-011-006. The IRM ensures IRS employees have the approved guidelines, policies, and authorities they need to carry out their responsibilities in administering tax laws and other agency obligations. IRM, § 1.11.6.2(2) (updated 03-23-2022), https://www.irs.gov/irm/part1/irm_01-011-006. Taxpayers do not have the right to enforce the IRS's use and application of its National and Local Standards. The IRM does not grant taxpayers any rights because it does not have force and effect of law. *Armstrong v. Comm'r*, 15 F.3d 970, 975 (10th Cir. 1994).

[14] https://www.irs.gov/irm/part5/irm_05-015-001.

local standard or the amount actually paid monthly, whichever is less." IRM, § 5.15.1.8(5) (updated 07-24-2019).[15] But if it is determined that a standard amount is inadequate to provide for a specific taxpayer's basic living expenses, an IRS agent is directed to allow a deviation above the National and Local Standards. IRM, § 5.15.1.8(6) (updated 07-24-2019).[16] The IRS also allows Other Necessary Expenses and Other Conditional Expenses. IRM, § 5.15.1.8(1) (updated 07-24-2019).[17] Other Conditional Expenses are expenses that are not Other Necessary Expenses but may be allowable based on the circumstances of an individual case. *Id*.

The IRS Local Standards include a Standard for Housing and Utilities based on information from the U.S. Census Bureau, American Community Survey, and Bureau of Labor Statistics data, particularized by county and the size of the family involved. IRM, § 5.15.1.10(1) (updated 11-22-2021).[18]

The IRS defines "Housing and Utilities" as follows:

> (1) Housing expenses include: mortgage (including interest) or rent, property taxes, necessary maintenance and repair, homeowner's or renter's insurance, homeowner dues and condominium fees.
> (2) The utilities include gas, electricity, water, heating oil, bottled gas, trash and garbage collection, wood and other fuels, septic cleaning, cable television, internet services, telephone and cell phone.

IRM, §§ 5.15.1.10(1), (2) (updated 11-22-2021).[19]

The IRS has specified a single dollar amount for its Local Standard for Housing and Utilities, based on family size, for each State in the United States broken down by county,

[15] *Id.*.
[16] *Id.*
[17] *Id.*
[18] *Id.*
[19] *Id.*

without breaking down the amount into the "Housing" and "Utilities" components of the Housing and Utilities Standard.[20]

An uncodified portion of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA") provides that "[i]t is the sense of Congress that the Secretary of the Treasury has the authority to alter the Internal Revenue Service standards established to set guidelines for repayment plans as needed to accommodate their use under section 707(b) of title 11, United States Code." Pub. L. No. 109-8, § 103, 119 Stat. 35 (2005). Although not entirely clear, it appears this provision means that the IRS may issue National and Local Standards adjusted for use under the Bankruptcy Code. The IRS is a bureau under the U.S. Department of the Treasury of which the Secretary of the Treasury is its head.

Notwithstanding § 1325(b)(3) which, when read in conjunction with § 707(b)(2), makes the IRS National and Local Standards applicable in chapter 7 and chapter 13 bankruptcy cases, and the "sense of Congress" that the Secretary of the Treasury has the authority to adjust the IRS National and Local Standards to accommodate their use in bankruptcy cases, the IRS has disclaimed any responsibility for use of its National and Local Standards in bankruptcy cases or for making bankruptcy adjustments to its National and Local Standards. An IRS website includes this disclaimer:

> **Disclaimer:** *IRS Collection Financial Standards are intended for use in calculating repayment of delinquent taxes. These Standards are effective on April 24, 2023, for purposes of federal tax administration only. Expense information for*

[20] *See* the IRS table for "Allowable Living Expenses Housing Standards" (which are the same as the IRS Local Standard for Housing and Utilities) for different localities that can be found by downloading and opening a .pdf chart at this website: https://www.irs.gov/businesses/small-businesses-self-employed/local-standards-housing-and-utilities. The table specifies a single dollar amount by locality and family size. *See also Currie*, 537 B.R. at 889 (the IRS Local Housing and Utilities Standard consists of "a single amount that is inclusive of all housing expenses and dependent only upon a debtor's county of residence and household size.").

> *use in bankruptcy calculations can be found on the website for the U.S. Trustee Programs.*[21]

True to the disclaimer, the Secretary of the Treasury has not adjusted the IRS Standards to accommodate their use under § 707(b).[22]

> *Use of the IRS National and Local Standards in calculating allowable deductions from current monthly income to determine disposable income*

For an above-median-income debtor, the Bankruptcy Code requires use of the IRS National and Local Standards in the calculation of the debtor's monthly expenses in computing disposable income. § 707(b)(2)(A)(ii)(I).

Section 707(b)(2)(A)(ii)(I), which references the IRS National Standards and Local Standards, provides in part,

> The debtor's monthly expenses shall be the debtor's applicable monthly expense amounts specified under the National Standards and Local Standards, and the debtor's actual monthly expenses for the categories specified as Other Necessary Expenses issued by the Internal Revenue Service for the area in which the debtor resides, as in effect on the date of the order for relief, for the debtor, the dependents of the debtor, and the spouse of the debtor in a joint case, if the spouse is not otherwise a dependent . . . . Notwithstanding any other provision of this clause, the monthly expenses of the debtor shall not include any payments for debts.

The parties agree that Debtor is an above-median-income debtor which subjects her to the requirements of § 707(b)(2)(A) and (B), including § 707(b)(2)(A)(ii)(I). The Bankruptcy Code does not incorporate any part of the IRM or make any of its provisions applicable in bankruptcy cases, other than requiring use of the monthly expense amounts specified by the IRS under applicable IRS National and Local Standards and allowing a deduction from the debtor's actual monthly expenses for the category specified as Other Necessary Expenses by the IRS, in computing disposable income. § 707(b)(2)(A)(ii)(I). Neither

---

[21] https://www.irs.gov/businesses/small-businesses-self-employed/collection-financial-standards.
[22] *See* the IRS table for "Allowable Living Expenses Housing Standards" at footnote 20. *See also In re Currie*, 537 B.R. at 889.

§ 1325(b)(3), § 707(b), nor any other provision of the Bankruptcy Code, authorizes courts, the Committee on Rules of Practice and Procedure of the Judicial Conference of the United States ("Rules Committee"), or the United States Trustee ("UST") to alter the IRS National or Local Standards to accommodate their use in bankruptcy cases or to specify any amounts under the National Standards and Local Standards that are different from the amounts issued by the IRS.

Form 122C-2's application of the IRS Local Standard for Housing and Utilities

The Rules Committee adopted Forms 122C-1 and 122C-2 as Official Forms for use in calculating disposable income in chapter 13 cases. Under Bankruptcy Rules 1001 and 9009, use of Forms 122C-1 and 122C-2 is mandatory in chapter 13 cases by above-median-income debtors, without alteration, except for minor changes not affecting wording or the order of presenting information. Fed.R.Bankr.P. 9009 ("The Official Forms . . . shall be used without alteration, except as otherwise provided in these rules[.]").

That the UST, not the IRS, divided the IRS Local Standard for Housing and Utilities into two categories using information the IRS provided to the UST is apparent from the face of Form 122C-2 itself and from the Rules Committee Notes accompanying Form 122C-2.

Part 1 of Form 122C-2 includes a section for deducting the applicable amount of the IRS National and Local Standards from current monthly income. That section of Form 122C-2 includes the following relating to the IRS Local Standard for Housing and Utilities:

> **Based on information from the IRS, the U.S. Trustee Program has divided the IRS local standard for housing for bankruptcy purposes into two parts:**
>
> ▪ Housing and Utilities – Insurance and Operating Expenses
> ▪ Housing and Utilities – Mortgage or Rent Expenses
>
> To answer the questions in lines 8-9 [which call for inserting the applicable amounts of "Insurance and Operating Expenses" and "Mortgage or Rent Expenses"], use the U.S. Trustee Program chart.

Form 122C-2 (emphasis added).

The two separate categories of "Insurance and Operating Expenses" and "Mortgage or Rent Expenses" allow a debtor to separately claim deductions for "Insurance and Operating Expenses" and "Mortgage or Rent Expenses" in the amounts specified in the UST Program chart for each of those categories under the umbrella of the IRS Local Standard for Housing and Utilities.

A Committee Note to Form 122C-2 acknowledges that the IRS provided the information to the UST to enable the UST to divide the IRS Local Standard for Housing and Utilities standard into the two categories:

> The Local Standards for housing and utilities, as published by the IRS for its internal purposes, publish single amounts covering all housing expenses; however, for bankruptcy purposes, the IRS has provided the Executive Office for the United States Trustee with information allowing a division of these amounts into a non-mortgage component and a mortgage/rent component.

Official Form 122 (Committee Note), 2005-2008 Committee Note, https://www.uscourts.gov/forms/bankruptcy-forms/chapter-13-calculation-your-disposable-income, (PDF, 242.87 KB).

Form 122C-2 also recognizes that a debtor may claim that the UST's division of the Local Standard for Housing and Utilities is incorrect. *See* Form 122C-2, Line 10. Line 10 of Form 122C-2 provides:

> If you claim that the U.S. Trustee Program's division of the IRS Local Standard for housing is incorrect and affects the calculation of your monthly expenses, fill in any additional amount you claim.
>
> Explain why: _____

Form 122C-2, line 10. Thus Form 122C-2 allows a debtor to claim the full amount of the Local Standard for Housing and Utilities irrespective of the UST's division of the

Standard into two components if the debtor claims the UST's division of the Standard is incorrect and it affects the calculation of the debtor's monthly expenses.

By providing information to the UST so that the UST could publish separate deductible amounts for a non-mortgage component and a mortgage/rent component of the Housing and Utilities Standard, the IRS did not itself adopt that division. The IRM, which is the official compilation of IRS policies, procedures, and guidelines,[23] does not separate the Local Standard for Housing and Utilities into mortgage/rent expenses and non-mortgage expenses. Instead, it separately defines "Housing" and "Utilities" without breaking down the dollar amount of the Housing and Utilities Standard between those components.[24] Further, the IRS definitions of "Housing" and "Utilities" do not correspond with "Mortgage or Rent Expenses" and "Insurance and Operating Expenses" categories on Form 122C-2.[25] Consistent with the disclaimer on the IRS website, the IRS has continued to decline to post separate categories for mortgage/rent expenses and non-mortgage expenses on its website.

Whether Housing and Utilities Standard is an "applicable" Standard if the debtor has no mortgage or rent expense

Debtor contends that because she has an expense that falls within the category of Housing and Utilities under the IRS Local Standards, she is entitled to deduct the entire amount of the IRS Local Standard for Housing and Utilities. The Trustee points out that if Debtor is allowed a deduction for the entire IRS Local Standard for Housing and Utilities Standard, her monthly disposable income would be a negative $236.77; whereas, if no such deduction is allowed, her monthly disposable income would be a positive $1,567.23, which would be sufficient to pay

[23] IRM, § 1.11.6.2(1) (updated 03-23-2022), https://www.irs.gov/irm/part1/irm_01-011-006.
[24] *See* IRM, §§ 5.15.1.10.1(1), (2) (updated 11-22-2021), https://www.irs.gov/irm/part5/irm_05-015-001 and IRS table for "Allowable Living Expenses Housing Standards" referenced at footnote 20 above.
[25] *Compare* IRM, §§ 5.15.1.10(1), (2) (updated 11-22-2021), https://www.irs.gov/irm/part5/irm_05-015-001 with lines 8 and 9 on Form 122C-2.

non-priority unsecured creditors almost 100%. The Trustee reasons that the IRS Local Standard for Housing and Utilities is not applicable to Debtor because Debtor does not have a mortgage or rent expense, given the purpose of BAPCPA "to help ensure that debtors who *can* pay creditors *do* pay them." *Ransom v. FIA Card Services, N.A.,* 562 U.S. 61, 64 (2011) (citing H.R.Rep. No. 109-31, pt.1, p. 2 (2005)).

The Trustee also suggests that Debtor might be allowed to include her cellular telephone expense on Line 46 of Form 122C-2, as a "special circumstance." Line 46 of Form 122C-2 is titled "Change in Income or Expenses." The Court does not understand how Debtor's existing cellular telephone expense could appropriately be claimed on Line 46 of Form 122C-2. The Trustee may have intended to refer to Line 43 of Form 122C-2 titled "Deduction for Special Circumstances." However, it is clear that the special circumstances deduction, which is designed to implement § 707(b)(2)(B), is inapplicable to claiming expenses for cell phone service and seasonal fuel costs. The Trustee does not argue that Debtor should be required to comply with Form 122C-2 by deducting her cell phone and home fuel expenses only in the "Housing and Utilities – Insurance and Operating Expenses" category on line 8 of Form 122C-2.

Both Debtor and the Trustee rely on the Supreme Court's decision in *Ransom v. FIA Card Services, N.A.,* 562 U.S.61 (2011), which involved vehicle-related expenses. Unlike the IRS Local Standard for Housing and Utilities, the IRS divided its Local Transportation Standard into two categories, one called "Ownership Costs" and the other called "Operating Costs,"[26] and specified separate amounts for each category. In *Ransom*, because the debtor owned his car outright, he did not make car loan or lease payments. *Ransom*, 562 U.S. at 64. Consequently, he did not have any expenses in the Ownership Costs category of the IRS Local Transportation

[26] Form 122C-2 identifies the categories as "Vehicle operation expense" and "Vehicle ownership or lease expense."

Standard. Nevertheless, the debtor claimed deductions from current monthly income in the full amounts the IRS specified for both the "Ownership Costs" and "Operating Costs" categories of the Standard. *Id.* at 67. The Supreme Court determined that a debtor who owned his car outright may not take a deduction for Ownership Costs but was entitled to take a deduction for Operating Costs when calculating projected disposable income. *Ransom*, 562 U.S. at 64, 72.

In interpreting § 707(b)(2)(A)(ii)(I), the Supreme Court focused on the word "applicable." *Id.* at 69. Based on the ordinary meaning of the term, the Supreme Court found that "an expense amount is 'applicable' within the plain meaning of the statute, when it is appropriate, relevant, suitable, or fit." *Id.* The Supreme Court reasoned that a debtor must "actually incur[ ] an expense in the relevant category" to qualify for the deduction in that category such that "[i]f a debtor will not have a particular kind of expense during his plan, an allowance to cover that cost is not 'reasonably necessary' within the meaning of the statute." *Id.* at 70-71. Because the debtor in *Ransom* did not have any expenses within the Ownership Costs category of the Transportation Standard, that category was not "applicable" to the debtor. *Id.* at 80. Thus, the debtor could not deduct the IRS Standard Ownership Costs amount because he did not have any expense in that category. *Id.*

Here, Debtor does not have a mortgage expense. The Trustee reasons that such expense therefore is not "applicable" to the Debtor so that she cannot claim a deduction under the Housing and Utilities Standard, which includes a mortgage expense. Debtor does have cell phone and fuel expenses, which the IRS includes in the Housing and Utilities Standard in its definition of "Utilities." The problem with the Trustee's argument is that, unlike the IRS Standard for Transportation (at issue in *Ransom*), which divides the Transportation Standard into two categories: "Ownership Costs" and "Operating Costs," and specifies separate amounts for each

category, the IRS did not separate the Local Standard for Housing and Utilities into two categories. The IRS separately defines "Housing" expenses and "Utilities" expenses but only specifies a single amount for the entire Local Standard for Housing and Utilities. Because the IRS Local Standard for Housing and Utilities is a singular amount and Debtor has expenses covered by the Housing and Utilities Standard, the Standard is applicable to Debtor.[27]

Whether the division of the IRS Local Standard for Housing and Utilities into two categories impermissibly modifies the Bankruptcy Code

Having determined that the IRS Local Standard for Housing and Utilities is "applicable" to the Debtor, the Court ultimately must determine whether the categories specified in Form 122C-2 limit a debtor's ability to claim the entire Housing and Utilities Standard amount. The Trustee does not address this issue, instead relying entirely on her position that the IRS Local Standard for Housing and Utilities is not applicable to Debtor at all because she does not have a mortgage expense. The Court has rejected that argument.

On Form 122C-2, Debtor claimed $1,205.00 in the "Mortgage or Rent Expenses" category, and $599.00 per month in the "Insurance and Operating Expenses" category, for a combined total of $1,804.00, which is the amount specified in the IRS Local Standard for Housing and Utilities for a household of two in Bernalillo County, New Mexico. Debtor contends that she is entitled to the entire $1,804.00 per month deduction even though she has no expense in the "Mortgage or Rent Expenses" category because she has some expenses that fall within the IRS Local Standard Housing and Utilities category.[28] Debtor argues that the division

[27] It is unnecessary for a debtor to have *all* the expenses within a particular category in order to claim the deduction. It is only when a category consists of only one expense that the deduction will not be "applicable" unless the debtor actually incurs the expense. *See Ransom*, 562 U.S. at 70 (explaining that "a deduction is so appropriate only if the debtor has costs corresponding to the category covered by the table—that is, only if the debtor will incur that kind of expense during the life of the plan.").

[28] By claiming an expense in the "Mortgage or Rent Expenses" category, Debtor recognized the UST's division of the IRS Local Standard for Housing and Utilities into two categories and claimed an expense

of the IRS Local Housing and Utilities Standard into two categories in Form 122C-2 conflicts with the Bankruptcy Code and is, therefore, unenforceable.[29]

The Court first notes that its ruling does not affect the validity of Form 122C-2.[30] Line 10 of Form 122C-2, quoted above, allows a debtor who does not have a mortgage or rent expense but pays other expenses within the IRS Local Standard for Housing and Utilities to claim the entire amount of the Housing and Utilities Standard if the debtor asserts that the UST's division of the Housing and Utilities Standard is incorrect and it affects the calculation of monthly expenses. Form 122C-2 thereby enables a debtor who does not have a mortgage or rent expense to claim the full amount of the IRS Local Standard for Housing and Utilities specified by the IRS irrespective of the UST's division of the Housing and Utilities Standard into two categories, without altering Form 122C-2 in violation of Bankruptcy Rule 9009.[31,32]

Because the IRS disclaimed any responsibility for adapting its National and Local Standards for use in bankruptcy cases, the UST stepped in to fill that void. By dividing the Housing and Utilities Standard into the two categories, which is reflected on Form 122C-2, and specifying deductible amounts for each category, the UST adapted the IRS Standards for

---

in a category that is not applicable to Debtor. Nevertheless, the Court will treat Debtor as having claimed the full amount of the IRS Local Standard for Housing and Utilities on Line 10 of Form 122C-2 instead of separately claiming deductions for "Insurance and Operating Expenses" and "Mortgage or Rent Expenses." That was Debtor's intention.

[29] Debtor argues, in the alternative, that if the Court rules otherwise, Debtor is entitled to a deduction under the Insurance and Operating Expenses category on Form 122C-2.

[30] Official Forms are entitled to a presumption of validity. *See In re Morgan*, 374 B.R. 353, 361 (Bankr. S.D. Fla. 2007) ("[T]he [Bankruptcy] Rules and the Official Forms share the presumption of validity.").

[31] *See In re Rajender*, No. 07-21945-A-13G, 2007 WL 2345018, at *1-*2 (Bankr. E.D. Cal. Aug. 7, 2007) (pointing out that Line 26 of Form 22C then in effect, which was similar to Line 10 of Form 122-C now in effect, allows debtor to contest how the UST divided the local standard for housing).

[32] To take the entire amount of the IRS Local Standard for Housing and Utilities, a debtor should leave blank the part of Form 122C-2 that divides the Housing and Utilities Standard into categories, and claim the entire amount of the Housing and Utilities Standard in Line 10. The explanation given in Line 10 for the additional claimed deduction would be that the debtor is entitled under the Bankruptcy Code to the full amount of the Local Housing and Utilities Standard issued by the IRS.

bankruptcy purposes.[33] The division into two categories appears designed to accomplish at least two objectives.

First, requiring the division of the Housing and Utilities Standard into separate categories, one for "Mortgage or Rent Expenses" and the other for "Insurance and Operating Expenses," prevents a debtor who does not have a mortgage or rent expense but who has other expenses within the Housing and Utilities Standard from taking the entire deduction for the Housing and Utilities Standard. By creating a category that isolates mortgage and rent expenses from other housing and utility expenses, it makes the mortgage and rent expenses category inapplicable to a debtor who does not have a mortgage or rent expense.[34]

This case illustrates the significance of the first objective. If Debtor could take the "Insurance and Operating Expenses" deduction but not the "Mortgage or Rent Expenses" deduction, Debtor would be required to make a meaningful payment to her unsecured nonpriority creditors instead of paying them nothing.[35]

Second, the division of the Housing and Utilities Standard on Form 122C-2 into two categories enables a debtor to take the standard deduction for Insurance and Operating Expenses regardless of the amount of the debtor's mortgage or rent expense. Form 122C-2 instructs the debtor to reduce the amount of the Mortgage or Rent Expenses deduction (but not the Insurance and Operating Expenses deduction) by the debtor's total average monthly payment "for all

---

[33]The categories for Housing and Utilities on Form 122C-2 differ from the IRS definitions. As stated above, the IRS defines "Housing" expenses to include not only mortgage payments but also "property taxes, necessary maintenance and repair, homeowner's or renter's insurance, homeowner dues and condominium fees." IRM, § 5.15.1.10(1) (updated 11-22-2021), https://www.irs.gov/irm/part5/irm_05-015-001. Form 122C-2, in contrast, isolates mortgage expenses from all other housing-related expenses.

[34] This concept is consistent with *Ransom*, which prohibits the standard deduction in a category in which the debtor has no expenses.

[35]Absent the mortgage expense deduction, Debtor would be required to pay $72,300 to her non-priority unsecured creditors over the life of her chapter 13 plan.

mortgages and other debts secured by [the debtors'] home," but not to an amount less than $0. *See* Form 122C-2, Line 9b. This allows a debtor who has non-mortgage related housing expenses to take the full Insurance and Operating Expenses deduction regardless of the amount of the mortgage expense. If the Housing and Utilities Standard were not divided into categories, a debtor's actual monthly home mortgage payments would be deducted from the amount of the entire Housing and Utilities Standard, meaning if the debtor's monthly home mortgage expenses exceeded the full amount of the Housing and Utilities Standard, the debtor would get no deduction under Housing and Utilities Standard, although the debtor could still deduct the monthly amount paid on the debtor's home mortgage from current monthly income.[36]

However, even though dividing the Housing and Utilities Standard into "Mortgage or Rent Expenses" and "Insurance and Operating Expenses" with separate deductible limits for each category may further an overarching policy underlying BAPCPA—requiring debtors to pay unsecured creditors what they reasonably can afford to pay—it conflicts with § 707(b)(2)(A)(ii)(I) of the Bankruptcy Code, which requires above-median-income debtors to use the applicable monthly expense amounts specified under the IRS National and Local Standards. The IRS Local Standard for Housing and Utilities specifies "a single amount that is inclusive of all housing expenses," *Currie*, 537 B.R. at 889, without breaking the amount down into any categories.

The Court therefore holds that Debtor, who does not have a mortgage or rent expense but does have cell phone and seasonal fuel expenses that fall within the IRS Local Housing and Utilities Standard, is entitled to deduct from current monthly income the full amount of the IRS

[36] Line 33 of Form 122C-2 allows a debtor to claim an additional deduction for "debts secured by an interest in property that [the debtors] own, including home mortgages." *See also In re Hardacre*, 338 B.R. 718, 727 (Bankr. N.D. Tex. 2006) ("The effect of section 707(b)(2)(A)(ii)(I) is to permit the debtor to deduct the greater of her actual mortgage . . . or the amounts provided in the Local Standards.").

Local Housing and Utilities Standard. *See Currie*, 537 B.R. at 894 (concluding that the debtor could deduct the entire IRS Housing and Utilities Standard despite the fact that the debtor's only housing-related expenses were for insurance and property taxes associated with property that had no mortgage indebtedness).

The UST and the Rules Committee adapted the Housing and Utilities Standard for use in bankruptcy cases, and in doing so, made practical adjustments to effectuate bankruptcy policy. However, neither the UST nor the Rules Committee has the statutory authority to materially affect substantive rights under the Bankruptcy Code. The division of the IRS Local Standard for Housing and Utilities into two categories with separate deductible limits, if it had been mandated by use of Form 122C-2, would impermissibly and materially affect substantive rights.[37] The Rules Committee, by including Line 10 on Form 122C-2 (which allows a debtor who asserts the division of the Standard is incorrect to claim an additional deductible amount), recognized this limitation might apply.[38] If the division of the IRS Local Housing and Utilities Standard had been mandated by use of Form 122C-2, the substantive effect in Debtor's chapter 13 case would have been to increase Debtor's plan payments to non-priority unsecured creditors over the life of her plan by $72,300 because Debtor would not be allowed to take the Mortgage or Rent Expenses deduction for an expense she does not actually incur; whereas, by taking a deduction in the full amount of the IRS Local Housing and Utilities Standard in accordance with what the

[37] Just as Bankruptcy Rules cannot "effect substantive rights," *In re Cluff*, 313 B.R. 323, 332 (Bankr. D. Utah 2004), *aff'd sub nom. Cluff v. eCast Settlement,* No. 2:04-CV-978 TS, 2006 WL 2820005 (D. Utah Sept. 29, 2006), if there is a conflict between and Official Form and the Bankruptcy Code, the Bankruptcy Code controls. *In re Wiegand*, 386 B.R. 238, 241 (9th Cir. BAP 2008); *see also In re Anderson*, 383 B.R. 699, 703 n.8 (Bankr. S.D. Ohio 2008) ("[T]he Official Forms can never trump the language of the Code.").

[38] Official Forms must "be construed to be consistent with these rules and the Code." Fed.R.Bankr.P. 9009(c).

Bankruptcy Code permits, Debtor will not be required to pay anything to her non-priority unsecured creditors to satisfy the disposable income requirement under the Code.

CONCLUSION

The Court recognizes that allowing Debtor to deduct from current monthly income the full amount of the IRS Local Standard for Housing and Utilities when she does not actually incur any mortgage expenses might not be good bankruptcy policy. But the Court does not have discretion to deny the full deduction based solely on bankruptcy policy. The Bankruptcy Code entitles Debtor to deduct the full amount of the IRS Local Standard for Housing and Utilities from her current monthly income notwithstanding the fact that she has no mortgage expense because she does incur at least one expense covered by the Standard. As a result of this ruling, the Court will set a preliminary confirmation hearing so that the Trustee will have an opportunity to address her alternative objections to confirmation.[39]

Robert H. Jacobvitz

ROBERT H. JACOBVITZ
United States Bankruptcy Judge

Date entered on docket: December 7, 2023

[39] The Court expresses some skepticism about the Trustee's alternative objection that Debtor's current monthly income must be increased by the amount of her fiancé's mortgage expense. Section 101(10A)(A)(i) provides that current monthly income of an unmarried individual "includes any amount paid by any entity other than the debtor . . . on a regular basis for the *household expenses of the debtor or the debtor's dependents*." (emphasis added). The fiancé's mortgage expense does not appear to be an expense of the Debtor because the Debtor owns no interest in the home encumbered by the mortgage, has no liability on the mortgage, and does not pay any mortgage expenses. *See In re Toxvard*, 485 B.R. 423 (Bankr. D. Colo. 2013) (holding that mortgage payments made by debtor's non-filing spouse on a home he owned separately and for which only he was liable were not a household expense of the debtor); *In re Baker*, 580 B.R. 662 (Bankr. E.D. Va. 2017) (holding that the monthly mortgage payment made by debtor's non-filing spouse on property acquired pre-marriage is either not a "household expense" or is not an expense "of the debtor or the debtor's dependents").

COPY TO:

Jason Michael Cline
Attorney for Debtor
Jason Cline, LLC
2601 Wyoming Blvd. NE, Suite 108
Albuquerque, NM 87112

Tiffany M. Cornejo
625 Silver Avenue SW, Suite 350
Albuquerque, NM 87102-3111