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*329 HOME MORTGAGE CRAMDOWN IN BANKRUPTCY

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***330 ABSTRACT**

This Article examines the ways in which bankruptcy law's prohibition against modifications of debtors' principal residence mortgages in chapter 13 hinders an effective response to the present foreclosure crisis. I describe the findings of my original empirical study that examined the effectiveness of the present bankruptcy system as a home-saving mechanism for underwater homeowners. In this study all the chapter 13 cases filed in the Southern District of Florida in April 2009 were scrutinized to compare the rate of effectiveness of underwater principal residence mortgage cures to other cases that proposed permissible court-ordered mortgage modifications. The study concluded that of the various forms of relief afforded to chapter 13 property owners, a principal residence underwater mortgage cure proved least effective. The study's findings suggest that removing the bankruptcy prohibition against principal residence cramdown in chapter 13 would substantially improve a bankrupt homeowner's probability of saving a home from foreclosure. Accordingly, this Article advocates amending the Bankruptcy Code to remove the restriction against a bankruptcy court ordering a principal residence mortgage modification. [1]

INTRODUCTION

The home mortgage crisis has been painful for millions of American families during the past seven years. In times of need, households turn to ***331** bankruptcy to help save homes. However, in the majority of cases, the bankruptcy system is incapable of saving homes because of a specific provision--section 1322(b)(2)--prohibiting modification, or "cramdown," of a principal residence mortgage. [2] A mortgage cramdown is a court-ordered principal balance reduction of the secured loan down to the current market value of the collateral. [3] This cramdown separates the debt into a secured portion, equal to the property market value, and an unsecured portion, that is the excess debt remaining over the collateral's value. [4] In cramdown, the secured claim is paid in full, and the unsecured claim is paid a pro rata share of amounts allocated to unsecured creditors. [5] This procedure significantly reduces a debtor's underwater mortgage obligation.

Debtors must look to alternatives to save their homes because of the principal residence mortgage cramdown prohibition. While the law allows for stripping of a totally unsecured second mortgage, an upside-down first mortgage cannot be reduced. [6] Engaging in modification plans with lenders is an option that has become readily available, but is still overwhelmingly ineffective. The greatest hurdle is that loan servicers must voluntarily modify and are typically reluctant to do so. Many modifications are repayment plans providing temporary relief. Few modifications reduce the principal balance itself, which is a necessary component of underwater loan modifications.

Court-ordered principal residence modifications in chapter 13 were not always prohibited. Before the Supreme Court's decision in 1993 in *Nobelman v. American Savings Bank*, [7] about half the jurisdictions interpreted the Code to allow cramdown of a debtor's principal residence. [8] Those courts interpreted section 506 as guiding the preliminary determination of whether a claim is secured. [9] Then, the *Nobelman* Court unanimously disagreed and held cramdown ***332** of an underwater mortgage secured only by a debtor's principal residence is prohibited under section 1322(b)(2). [10]

The purpose of this Article's empirical study was to determine the effectiveness of chapter 13 in saving a debtor's principal residence. The study compared cases with underwater homestead mortgage cures to cases with non-underwater homestead cures, lien-stripped underwater homestead properties, and mortgage cures in conjunction with lien-strips on underwater homestead properties. The hypothesis was that of these four sub-samples, this study would tend to prove, or disprove, that the effectiveness of chapter 13 as a home-saving device was the least effective where an underwater

principal residence mortgage cure was attempted. Previous empirical studies have tested the theoretical assumption that mortgage markets are sensitive to bankruptcy-modification risk, and thus the prohibition on cramdown in chapter 13 is important. [11] The limited data and research reflected herein seems to support the change to allow cramdown.

Despite section 1322 of the Code, the cramdown of a mortgage secured solely by a debtor's principal residence in chapter 13 bankruptcy may be permitted in certain circumstances. [12] These circumstances include consent or lack of objection to cramdown, additional security being taken by the creditor apart from the residence, accelerated mortgages, purchase money first mortgages, and the theory of equitable subordination. [13]

For more than half the debtors in chapter 13, their single biggest asset is their home and they enter bankruptcy to avoid foreclosure. [14] This paper proposes temporarily amending section 1322(b)(2) to allow principal residence mortgage modifications. Any such amendment should contain a sunset provision. Although a change is needed to aid the current housing crisis, the prohibition should reinstate when the housing market stabilizes.

*333 I. BACKGROUND

A bankruptcy cramdown of a mortgage is a court-ordered reduction of the principal balance of a secured loan down to the current market value of the collateral. [15] Cramdown will also result in the modification of a mortgage's interest rate and term. [16] In a chapter 13 bankruptcy, a debtor's mortgage secured only by his or her homestead that is underwater cannot be crammed down. [17] However, chapter 13 debtors are able to judicially modify terms of all other types of underwater secured claims, enabling them to change interest rates, payment amounts and principal balances on property such as vacation homes, investment properties and multifamily residences in which the owner occupies a unit. [18]

A. Treatment of Mortgages Under Current Bankruptcy Law

1. Mechanics of a Cramdown

A cramdown is the most significant type of modification because it affects the treatment of the principal amount of the creditor's claim, not just the interest. [19] For instance, if real property is purchased by a debtor pre-petition for $300,000, and a post-petition valuation sets the lender's allowed secured claim at $180,000, then the lender would reduce the amount of collateral it secured from $300,000 that it held in accordance with state law, i.e. a forty percent reduction. The cramdown approach applies to almost all types of secured debt, except for primary home mortgages and liens on motor vehicles. The 2005 amendments added language to section 1325(a) that prohibits cramdowns to secured creditors of motor vehicles that have been granted a security interest within 910 days of filing a bankruptcy petition, and for creditors holding a purchase money security interest that was granted within a year of the filing of the bankruptcy petition. [20]

*334 The effect of a cramdown is the bifurcation of the debt into a secured portion--representing the market value of the property on the filing date of the bankruptcy petition--and an unsecured portion--representing the excess of the debt over the secured portion. [21] The secured claim will be fully paid, and the unsecured claim paid a pro rata share, which is the greater of the amount general unsecured creditors would receive in a chapter 7 liquidation or the debtor's projected disposable income. [22] Normally this will result in a significant reduction in payments owed by the debtor.

In the case of *In re Mattson*, [23] Judge Robert J. Kressel called cramdown the "centerpiece of the reorganization chapters[]" and stated that the "basic rule of the cramdown is that, under a plan, a debtor must make payments to a secured creditor which have a value equal to the debtor's allowed secured claim, which is not necessarily its entire claim." [24] Under the Bankruptcy Code, a claim is a secured claim only to the extent of the value of the collateral and is an unsecured claim for the remainder. [25]

2. Cramdown Authority under the Bankruptcy Code

The general rules regarding payments to secured creditors in a chapter 13 bankruptcy case are contained in section 1325(a)(5). [26] Under the general rule of section 1325(a)(5), often called the cramdown section, the debtor can promise to pay the allowed secured claim--the value of the collateral--in full while treating the unsecured portion of the debt like any other unsecured debt. [27] The treatment of an undersecured claim is called a "cramdown" because it can be imposed over the secured creditor's objections. [28] The requirements are that a secured creditor must be paid its allowed claim in full, and that interest must be paid on the entire claim. [29]

The authority to bifurcate derives from sections 506(a) and (d), which grant the holder of a secured claim repayment of such claim to the extent of the value of the collateral and deem the lien void to the extent the lender's claim exceeds ***335** the value of the collateral. [30] If a secured creditor's claim is less than or equal to the value of the collateral, then the entire claim is "fully secured." If the creditor's "claim is greater than the value of the collateral, then the claim is 'partially secured[,]'" and "[t]he remaining portion of the initial claim continues as an unsecured claim against the estate." [31] Thus, "an undersecured claim is bifurcated by section 506(a) to yield two claims: a secured claim equal to the value of the collateral and an unsecured claim for the remainder[.]" [32]

A cramdown forces the secured creditor to reduce an allowed secured claim to 100% of the value of the collateral. To illustrate, if the amount owed to the secured creditor is $100 and the collateral has a value of $70, then a bankruptcy plan that proposes to retain the encumbered property obligates the secured creditor to reduce the allowed secured claim to $70, the value of the collateral. [33]

3. Valuation of the Secured Creditor's Claim

The value of a secured creditor's claim is the cost to the debtor to replace the collateral. In *Associates Commercial Corp. v. Rash*, [34] the Supreme Court examined the provisions of section 506(a) that call for the bifurcation of an undersecured claim in conjunction with the cramdown provision contained in section 1325(a)(5)(B). [35] Further, the Court examined whether the secured portion to be provided for in the chapter 13 plan is the amount the secured creditor could obtain at a foreclosure sale, namely the "foreclosure value," or is the value the debtor would have to pay for comparable property, namely the ***336** "replacement value." [36] Justice Ginsburg held that section 506(a) directs that the application of the replacement value standard. [37] Accordingly, the cost the debtor would necessarily incur to obtain a like asset for the same proposed use is the value that should compose the secured portion of the claim and thus the value that must be provided for in the chapter 13 plan. [38] Even though the Court brought some uniformity to valuation under section 506 with its holding, cases decided after *Rash* demonstrated that it was still unclear to lower courts how to address the problem of valuation. [39] Congress attempted to bring some uniformity to the issue of valuation by codifying the portion

of the *Rash* opinion dealing with valuation as part of the Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA") amendments. [40]

4. Plan Confirmation

Creditors with secured claims enjoy much greater protection than their counterparts with unsecured claims under section 1325(a)(5) because the holder of a secured claim retains its lien on the collateral until either the lien is satisfied pursuant to non-bankruptcy law or until the creditor receives the present value of its collateral as of the "effective date of the plan." [41] In contrast, non-priority unsecured claims in a chapter 13 plan must receive only whatever they would have received in a chapter 7 liquidation (the "Best Interests of the Creditors" Test), unless there is objection and the debtor has sufficient projected disposable income to pay more. [42] In a chapter 13 bankruptcy, the debtor may keep ***337** collateral but must pledge future earnings to pay the present value of the allowed amount of the secured claim over the life of the chapter 13 plan. The confirmation of a plan will prevent a secured creditor from demanding higher payment on a secured claim than what was provided for in the plan, and will also prevent a debtor from paying less than what was provided to that creditor under the terms of the confirmed plan. [43]

Under section 1325(a)(5)(B)(i), if a debtor fails to complete his chapter 13 plan he will lose the benefit of a cramdown, the debt will not be discharged, and following the bankruptcy, the secured creditor will once again be able to enforce any security interest with regard to all the unpaid debt. [44] If the debtor completes the chapter 13 plan, then the bifurcated, unsecured portion of a secured creditor's lien will be discharged along with other general unsecured claims after receiving the pro-rata distribution allocated to this class of creditors in the plan. [45]

Although a debtor may not alter his or her homestead's mortgage interest rate, payment amount, principal balance owed or period in which payments must be made, a debtor nevertheless maintains the right to cure a default on a primary residence mortgage in a chapter 13 plan under section 1322(b)(2). [46] A bankruptcy judge may allow the secured portion of the bifurcated debt (i.e. the allowed secured claim) to be amortized past the life of the chapter 13 plan. [47] Almost invariably, debtors seek this type of treatment as they are typically unable to pay the allowed secured claim in full over the three-to-five year plan. [48] However, some judges have held that, in addition to having to pay the pre-petition contractual rate of principal and interest, the debtor must pay the pre-petition arrears in full over the life of the plan. [49] Alternatively, the judge ***338** may allow the debtor to pay the entire amount of the allowed secured claim over the life of the chapter 13 plan, without providing for the arrears, so long as the entire allowed secured claim is accorded an interest rate equal to 2% over the prime rate as required by *Till v. SCS Credit Corp.* [50]

5. Lien-Strip

A lien-strip, unlike a cramdown, is the process of avoiding an entire lien in bankruptcy that is secured under state law but lacks an equity cushion to support any portion of the amount owed. [51] Notwithstanding the restriction imposed by section 1322(b)(2), virtually all courts have read sections 506 and 1325 to permit a lien-strip for a second or subsequent home mortgage that is entirely unsecured. [52] A "wholly unsecured" mortgage loan is not protected from the provisions prohibiting modifications of mortgages securing a debtor's homestead contained in section 1322(b)(2). [53] This is because the proper starting point in determining whether the anti-modification provision of section 1322 applies is the valuation of the collateral securing the claim under section 506(a). [54] Without first showing that a creditor has a secured claim

because of sufficient collateral value, a creditor may not invoke the protection contained in ***339** section 1322(b)(2). [55] Any subordinate lien holder under section 506 can be lien-stripped if the sum total of the senior lien holder's claim(s) meets or exceeds the fair market value of the collateral. [56] Although Justice Stevens recognized a congressional policy in favor of home lending while justifying the anti-modification provisions in section 1322(b)(2) in his *Nobelman* concurrence, courts have narrowed the anti-modification language contained in section 1322(b)(2) to apply to first or purchase money mortgages. [57] If even one dollar of a mortgage lender's interest is secured by the collateral that is a debtor's homestead, the debtor would be unable to bifurcate the lender's interest. [58] However, if the lender is "wholly unsecured," then the debtor can propose to strip the entire lien off in a chapter 13 plan and permanently avoid the lien at the conclusion of the chapter 13 case. [59] The lien-stripped mortgage is placed in the same class as unsecured, non-priority creditors in a chapter 13 bankruptcy case and receives a pro-rata portion of the distributions, usually a nominal amount that is allocated to members of that class under the confirmed chapter 13 plan. [60]

B. Mortgages in Bankruptcy: A Brief History

Chapter 13's provision prohibiting homestead cramdowns has existed since the enactment of the Bankruptcy Code in 1978. [61] Notwithstanding, until 1993 some circuits interpreted the Code to allow cramdown of a debtor's homestead. [62] Then in 1993 the Supreme Court unanimously held that section 1322(b)(2) prohibited modification of a mortgage on a debtor's homestead. [63] The historical ***340** treatment of the Code further illustrates the present-day allowances and prohibitions of mortgage modifications in bankruptcy.

1. The Bankruptcy Act and the Chandler Act

Under the 1898 Bankruptcy Act debtors were prohibited from modifying or affecting mortgage holders' rights without consent from the secured creditors. [64] A plan had to be accepted by at least two-thirds of each class of creditors and stockholders affected by the plan. [65] Then the "cramdown" clause was added to section 77 in the Bankruptcy Act of 1935. [66] Under the cramdown provision, the district court, under certain circumstances, may confirm a plan despite the disapproval of more than one-third of each affected class. [67] Subsequently in 1938 the Chandler Act was passed, which added a new chapter 13 for "wage earners." [68] For forty years thereafter, debtors could cramdown a home mortgage in a chapter 13 bankruptcy. [69]

2. The Bankruptcy Code & Enactment of Section 1322(b)(2)

When the Bankruptcy Code was first proposed in the late 1970s to replace the Bankruptcy Act, the House proposed no limitations on the ability of a wage earner to modify the rights of holders of secured claims or of undersecured claims; the Senate proposed the preservation of the expansive protections that were afforded creditors in the Bankruptcy Act by prohibiting modifications, or cramdowns, of claims secured by real estate mortgages. [70] In 1978 when the Bankruptcy Code was enacted, a key component of its reforms was in chapter 13 allowing "debtors to pay off a portion of their debts while retaining their assets." [71] The prohibition against modifying a claim that is secured only by the homestead of a debtor reflects a compromise between the 1977 House Bill and ***341** the 1978 Senate Bill. [72] This "safe harbor" protection is contained under section 1322(b)(2) of chapter 13 of the Bankruptcy Code, which states that although

modifications of rights of secured creditors are permitted, such modifications are allowed for secured debts other than those secured solely by a debtor's homestead. [73]

Although the legislative history of section 1322 is sparse, the prohibition on modification of a debtor's homestead was apparently intended to facilitate consumer reorganizations, promote the flow of mortgage capital to consumers and to reflect the economic reality that secured creditors faced by placing some of the risk of declining valuations on secured creditors. [74] In fact, there was no discussion in the Congressional Record regarding the enactment of this anti-modification provision. [75] The bill was raised during an oral exchange in the Senate during hearings between Edward J. Kulik, the Senior Vice President of the Real Estate Division of Massachusetts Mutual Life Insurance Company, his counsel Robert E. O'Malley of Covington & Burling and Senator Dennis DiConcini of Arizona. [76] This dialogue appears to be the only evidence that sheds light on the congressional intent behind the anti-cramdown provision. [77] During this exchange Senator DiConcini, to no avail, challenged the contention that without the prohibition, the flow of home mortgage credit would be affected. [78]

***342 3. Pre-*Nobelman* Interpretation of Section 1322(b)(2)**

Before 1993, a number of circuits held that the anti-modification provision of section 1322(b)(2) would apply to undersecured mortgages after the secured portion of a mortgagee's claim was reduced in accordance with section 506(a) of the Code. [79] These courts held that an undersecured claim with a security interest in a debtor's homestead may be bifurcated into two separate claims: one secured and the other unsecured. This was based on the fact that nothing in section 1322(b)(2) affects the applicability of the cramdown provisions of section 506 when making the preliminary determination as to whether the claim is, at first, to be considered secured. [80] These circuits held it was only the secured portion of the original claim that would be afforded the protection of section 1322(b)(2) and that the unsecured portion would be treated as an unsecured claim and modified under the terms of the confirmed chapter 13 plan. [81]

Some courts in these circuits further reasoned that if Congress intended the term “secured claims” reflected in section 506(a) to have a different meaning than the term “claim secured” reflected in section 1322(b)(2), Congress would not have neglected to indicate so. [82] Other circuits held that undersecured claims that attach to a debtor's primary residence should be as fully protected as those claims that are fully secured, and any bifurcation of the claim would be a clear violation of section 1322(b)(2). [83] A circuit split thus emerged regarding the extent to which a claim must be secured for purposes of invoking the prohibition against modifications of mortgage liens secured by a debtor's homestead in a chapter 13 plan. [84]

343 4. *Nobelman v. American Savings Bank

In 1993 in *Nobelman v. American Savings Bank*, [85] the Supreme Court unanimously held that section 1322(b)(2) prohibits a debtor in a chapter 13 case from relying on section 506(a) to reduce an undersecured mortgage on the debtor's homestead down to the fair market value of the property. [86] The Court found that although the “[p]etitioners were correct in looking to § 506(a)” to make a factual determination as to the judicially-derived valuation of their residence to determine the status of the lender's secured claim, the ultimate valuation would not limit the lender's rights as a claim holder because of the protection afforded the homestead lender under section 1322(b)(2). [87] The *Nobelman* Court maintained that in the absence of a controlling definition under the Bankruptcy Code, there must be a presumption

that Congress left the determination of "rights" in the property that is subject to the bankruptcy estate to the states themselves. [88] Therefore, according to the Supreme Court, the mortgagee's rights were contained in the mortgage instruments that were enforceable under state law. [89] These property rights, belonging to the lender, included "the right to repayment of the principal in monthly installments over a fixed term at specified adjustable rates of interest." [90] As such, these rights were "protected from modification by §1322(b)(2)." [91]

The holding in *Nobelman* made clear that section 506(a) could not be applied when an undersecured mortgage is secured by a security interest in the debtor's homestead and that the lender is the "holder" of a "secured claim," even if a portion of that claim was undersecured under section 506(a). [92] The practical result of *Nobelman* is that the only relief available to a chapter 13 debtor regarding principal residence mortgages that are not wholly unsecured is the right to "cure and maintain." [93] This is the right to bring current the past due arrears while maintaining the regular payments on the mortgage as they come due under section 1322(b)(5). [94]

*344 II. AUTHOR'S EMPIRICAL STUDY

In the absence of the ability to cramdown a homestead mortgage in chapter 13, the only remaining chapter 13 home-saving processes are either "lien-strips" or "mortgage cures." [95] As previously discussed, a lien-strip eliminates a wholly unsecured subordinate mortgage. [96] A mortgage cure pays pre-petition mortgage arrears, in addition to the contractual regular payments, over the life of the chapter 13 plan. [97] In this fashion, a mortgage cure results in a mortgage payment that is higher than the contractual regular payment.

I conducted an empirical study to examine whether chapter 13 serves as an effective home-saving process for underwater homeowners. I examined four different strategies used by distressed property owners in chapter 13:

i. Debtors providing for cures on underwater homestead properties;

ii. Debtors providing for cures on non-underwater homestead properties;

iii. Debtors providing for lien-strips on underwater homestead properties; and

iv. Debtors providing for lien-strips in conjunction with cures on underwater homestead properties.

I hypothesized that chapter 13 effectiveness as a home-saving process is least effective when a cure is attempted. I further hypothesized that chapter 13 was most effective when a wholly unsecured mortgage is lien stripped, whereby reducing the property's overall loan-to-value ratio. For the purposes of this study, a property was considered "underwater" if the property's loan-to-value ratio exceeded 100% at the time of filing chapter 13.

Originally cases that were filed more than five years ago were examined because most chapter 13 cases consist of five-year plans. Under this presupposition the relevant data for the 257 chapter 13 cases filed in the Southern District of Florida between April 1, 2007, and April 30, 2007, was reviewed. Of this sample, only 26 properties had loan-to-value ratios that exceeded 100% (22 were homestead properties and four were non-homestead properties). However, only nine properties had loan-to-value ratios that exceeded 110% (seven were homestead properties and two were non-homestead properties). It became apparent that during April 2007, home values had not decreased sufficiently to conduct a relevant analysis and thus these cases would not prove to be a viable sample. Instead this study used a sample consisting of the 526 chapter 13 bankruptcy cases filed in the Southern District of Florida from April 1, 2009, to April 30, 2009, to analyze the effectiveness of homestead ***345** mortgage cures where the loan-to-value ratios exceeded 100%. [98] While many of these cases were open when the data was compiled, this time period had significantly higher rates of underwater mortgage filings, many of which were severely underwater (with loan-to-value ratios greater than 110%), and so this sample served as a more accurate indicator of the potential shortcomings of chapter 13 as a home-saving process during periods of declining home values. [99]

Data for this study came from the docket and schedules drawn from PACER [100] in July 2012 for chapter 13 cases filed in the month of April 2009. There were originally 526 cases in the analysis, of which 343 cases were removed from the analysis because the case did not include any Schedule A homestead property, the debtor failed to file the appropriate schedules, the debtor voluntarily withdrew from bankruptcy, or because the case did not treat the homestead property listed on Schedule A in the plan. Thus, 183 cases with homestead Schedule A property being treated in the plan were included in the analysis.

The 183 cases were assigned codes of 1-4 based on the following four outcomes. A code of 1 was assigned to cases proving for underwater homestead cures. There were 30 of these cases (n=30). The mean loan-to-value ratio for such cases was 1.47 (LTV mean=1.47). The standard deviation for these cases was 0.39 (s.d.= 0.39). A code of 2 was assigned to cases providing for cures on non-underwater properties (n=17, LTV mean=0.72, s.d.=0.22). Cases in which lien-strips on underwater properties were applied were assigned a code of 3 (n=116 cases, LTV mean= 1.68, s.d.=0.62). Finally, cases where debtors provided for lien-strips in conjunction with cures on underwater homestead properties were assigned a code of 4 (n=20, LTV mean=1.75, s.d.=0.42). For the total 183 cases (case codes 1-4), the overall LTV ratio mean was 1.56 ***346** (s.d.=0.60). There were 136 cases that employed some form of a lien-strip (case codes 3 and 4), and the LTV ratio mean of the properties after lien-stripping was 1.33 (s.d.=0.47). The LTV ratio mean for cases that used lien-strips only (case code 3) after lien-stripping was 1.33 (s.d.=0.50). The LTV ratio mean for cases that used lien-strips in conjunction with cures (case code 4) after lien-stripping was 1.35 (s.d.=0.30).

To create a useable rubric for deeming cases “effective” or “ineffective,” cases that were discharged or open with ongoing plan payments were deemed “effective,” whereas cases that had been dismissed or cases in which the debtor surrendered the property after filing bankruptcy were deemed “ineffective.” The breakdown for each case code's effectiveness was:

CODE 1: Cases providing for underwater homestead cures: 10.0% of cases effective

CODE 2: Cases providing for underwater non-homestead cures: 41.2% of cases effective

CODE 3: Cases providing for lien-strips on underwater homesteads: 68.1% of cases effective

CODE 4: Cases providing for lien-strips in conjunction with underwater homestead cures: 30.0% of cases effective

The next step was to test the hypothesis that cases with higher LTVs may be less effective than cases with lower LTVs within the case codes that employed some form of lien-strip of a subordinate mortgage (case codes 3 and 4). To determine whether the LTV ratios influenced the effectiveness of these cases logistic regression was used. Logistic regression is a statistical technique used to model a binary (0/1) outcome, in this study whether or not the cases were effective based on predictor variables. In this analysis the predictor variable was the cases' LTV ratios. [101]

Results from logistic regression show that for cases where only lien-strips were used (case code 3), the LTV ratios were not significant predictors in these cases' chapter 13 rate of effectiveness. In other words, even as the LTV ratio increased, this did not significantly reduce the chance of cases' chapter 13 effectiveness for cases that employed only the lien-strip without a cure (Coef= 0.28, s.e.=0.38).

Similarly, for cases where lien-strips were implemented in conjunction with mortgage cures (case code 4), results were similar as the cases that used only lien-stripping (case code 3). Higher LTV ratios in cases that used both lienstrips ***347** and mortgage cures did not influence the effectiveness of such chapter 13 cases (Coef=0.92, s.e.=1.16).

T-tests were employed to test the statistical significance in the effectiveness of lien-stripping compared to the other methods of chapter 13 reorganization, and results indicated that chapter 13 cases employing lien-strips only (code 3), were significantly more likely to result in an effective outcome compared to cures for underwater homes (code 1) (T-value = 6.63, sig. 0.000). Lien-stripping (code 3) was also significantly more effective compared to cures for non-underwater homes (code 2) (T-value 2.21, sig. 0.01). Lastly, lien-stripping (code 3) was significantly more effective compared to lien-stripping in conjunction with curing (code 4) (T-value=3.39, sig. 0.000). Overall, these results lend support for the hypothesis that lien-stripping is an effective tool in the home-saving process in a chapter 13 bankruptcy case.

***348 1. Underwater Principal Residence Mortgage Cures**

As Table 1 shows, of the 183 chapter 13 cases that were treating homestead properties in their chapter 13 plans, 16.4%, or 30 cases were underwater homestead cures. Of these 30, 90.0%, or 27 cases, had either been dismissed or the property was subsequently surrendered, whereas the remaining 10.0%, or 3 cases, were either discharged or remained opened. Therefore, during this period chapter 13 proved effective, or on the path to effectiveness as an underwater homestead-saving procedure for only one-in-ten debtors attempting an underwater homestead cure. [102]

TABLE 1: RELEVANT DATA CONCERNING THE 183 CHAPTER 13 CASES FILED IN THE SOUTHERN DISTRICT OF FLORIDA IN APRIL 2009 HOMESTEAD PROPERTIES

	PERCENTAGE OF CASES OPEN OR DISCHARGED	PERCENTAGE OF CASES DISMISSED AND/OR PROPERTY SURRENDERED	TOTAL NUMBER OF CASES
Underwater Mortgage Cures Case Code 1	10.0%	90.0%	30
Non-Underwater Mortgage Cures Case Code 2	41.2%	58.8%	17
Lien-Strips of Subordinate Mortgages Case Code 3	68.1%	31.9%	116
Underwater Cures in Conjunction with Lien-Strips Case Code 4	30.0%	70.0%	20
Total	51.9%	48.1%	183

2. Underwater Principal Residence Cures Compared to Non-Underwater Principal Residence Cures

The study compared the 10.0% effectiveness of underwater homestead cures to that of non-underwater homestead cures (i.e. when the loan-to-value ratio was less than 100%). This comparison was done in order to determine what impact, if any, the underwater nature of the home would have on the effectiveness of a debtor utilizing a cure as a home-saving device. As Table 1 shows, of the total 183 chapter 13 cases providing for homestead mortgages in their chapter 13 plans, 25.7%, or 47 cases (30 underwater homestead cure cases + 17 non-underwater homestead cure cases), proposed cures for repaying the homestead mortgages. Of these 47 cases, 36.2%, or 17 cases, were proposed cures on non-underwater homesteads. [103] Of these 17 cases, only 41.2%, or seven cases, were eventually discharged or still remained open three years after the bankruptcy case was filed, i.e. the date the data was compiled. Although only 41.2% of non-underwater homestead cures proved to be effective, or still on the path to effectiveness, this was more than quadruple the 10.0% of the underwater homestead cures that were likewise situated. This would indicate that chapter ***349** 13 debtors are significantly less able to use a cure as an effective home-saving device for an underwater homestead when compared with a non-underwater homestead.

3. Underwater Principal Residence Cures Compared to Lien-Strips

The study then compared the mere 10.0% effective rate of chapter 13 cases that proposed an underwater homestead cure to that of cases that proposed lien-strips only (i.e., not in conjunction with a cure). This part of the analysis was done to

determine whether a reduction in the total amount owed on a debtor's underwater home would increase the probability that a debtor would save his or her home as a result of bankruptcy.

As Table 1 shows, of the 183 chapter 13 cases that were treating homestead properties in their chapter 13 plans, 63.4%, or 116 cases proposed a lien-strip of a subordinate mortgage. [104] Of these 116 cases, 68.1%, or 79 cases, were either discharged or remained open, and 31.9%, or 37 cases, were either dismissed or the property was later surrendered after the lien-strip was proposed. Accordingly, chapter 13 served as an effective homestead-saving device, or was pending effectiveness, roughly seven times as often when a lien-strip was sought compared to the 10.0% effective rate when an underwater homestead cure was sought.

4. Underwater Principal Residence Cures Compared to Underwater Principal Residence Cures with Simultaneous Lien-Strips

The study then compared the 10.0% effectiveness of chapter 13 cases that proposed an underwater homestead cure to that of cases that, in addition to proposing an underwater cure, proposed the lien-strip of a subordinate mortgage. This subsection was analyzed to determine whether the low effectiveness of underwater cures would substantially increase when the total debt owed on the residence was reduced.

As Table 1 shows, of the 183 chapter 13 cases that were treating homestead properties in their chapter 13 plans, 10.9%, or 20 cases, proposed an underwater senior mortgage cure in conjunction with a subordinate mortgage lien-strip. Of these 20 cases, 70.0%, or 14 cases had either been dismissed or the property was ***350** subsequently surrendered, whereas the remaining 30.0%, or six cases, were either discharged or remained open as of the date the data was compiled.

Therefore, although 10.0% of underwater mortgage cures proved effective, this rate of effectiveness increased to 30.0% when underwater homestead cures simultaneously sought to lien-strip subordinate mortgages. These findings would lend support to the premise that lowering of the total amounts owed on a debtor's residence has a noted effect on the financial or motivational ability of a debtor to see a chapter 13 plan through to discharge.

5. Analysis of Findings

The purpose of comparing the status of the chapter 13 cases when an underwater homestead cure was being attempted to that of a non-underwater homestead cure was to test the hypothesis that debtors are more likely to complete a chapter 13 plan when there is an equity cushion associated with the property. This hypothesis tended to be supported by this study's findings as illustrated by Table 1 above and Figure 1 below. Four times the number of mortgage cures associated with non-underwater properties proved effective compared to underwater mortgage cures. This tends to show that although chapter 13 mortgage cures were generally ineffective, a debtor stands a significantly better chance of using the process effectively when the homestead is not underwater.

Figure 1: Percentage of Effective Chapter 13 Cases Using Process by Category

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE

***351** The purpose of comparing chapter 13 cases where a lien-strip was sought generally, and where a lien-strip was sought in conjunction with a senior mortgage cure, to that of an underwater cure was to test the hypothesis that a reduction in the total amounts owed on a debtor's homestead would increase the effectiveness of chapter 13 as a home-saving process. The hypothesis was that if a higher percentage of cases where a debtor sought a lien-strip of a subordinate mortgage remained open or discharged, as compared to the percentage of underwater cures that likewise remained open

or discharged, that the data would tend to indicate that chapter 13 served as a more effective underwater home-saving procedure where the total amount owed on the residence was reduced. This hypothesis tended to be supported by this study's findings.

Both Table 1 and Figure 1 show that when a lien-strip of a subordinate mortgage was proposed in the chapter 13 plan, the 68.1% rate of effectiveness was nearly seven times as high as the 10.0% rate of effectiveness when an underwater mortgage cure was proposed. This was a statistically significant difference. Therefore, the findings show that a reduction of the total amount owed on underwater homestead residences dramatically increases the chances that chapter 13 will serve as an effective home-saving process.

Of the four sample procedures, the lien-stripping of a subordinate homestead mortgage exclusive of a mortgage cure proved to be the most effective chapter 13 home saving procedure. This is despite the fact that a debtor's homestead property will usually remain underwater to some extent after a lien-strip. [105] This high degree of effectiveness could reasonably be attributed to the incentivizing effect that a reduction in the total loan-to-value ratio has on the motivation of a debtor to see his/her chapter 13 plan through. A lien-strip does not become permanent, and the court order stripping is non-recordable, until the debtor completes the plan payments and receives a discharge. [106]

While only 30% of underwater homestead cures in conjunction with lien-strips proved effective, it should be noted that this is still three times more effective than an underwater homestead cure without a lien-strip. The increased effectiveness is likely a result of the incentivizing effect stripping a subordinate mortgage has on a debtor's motivation in chapter 13. The probable reason that the combined cure and lien-strip is not as effective as a lien-strip without a cure is that curing arrears can be challenging for chapter 13 debtors. Chapter 13 debtors that were unable to remain current on their regular pre-petition mortgage payments are often unable to remain current on the chapter 13 plan payments that add a portion of the arrears and trustee fees to the regular payment, significantly increasing the monthly obligation.

***352** The findings support that allowing cramdown on a debtor's primary residence would prove at least as effective as a home-saving process as lien-stripping in that cramdown would similarly reduce the loan-to-value ratio of the subject property. Cramdown reduces the loan-to-value ratio of property to the current value of the property (i.e., 100%), yet lien-stripping does not lead to such a dramatic reduction (as it leaves undersecured senior mortgages intact). As a result of the foregoing, it seems plausible that cramdown would serve as an even more effective home-saving device than lien-stripping.

III. LEGAL STRATEGIES TO AVOID APPLICATION OF SECTION 1322(B)(2)

Despite section 1322 of the Code, the cramdown of a mortgage secured solely by a debtor's homestead in a chapter 13 bankruptcy case may be permitted in certain circumstances. [107] These circumstances include consent--or lack of objection--to the cramdown, additional security being taken by the creditor apart from the homestead of the debtor, accelerated mortgages, purchase money first mortgages and the HAMP supplemental directive. [108]

A. Creditor Actions

Despite the anti-cramdown prohibition contained in section 1322, the plain reading of the Bankruptcy Code and case law provide persuasive authority for a bankruptcy judge to allow the cramdown of a homestead mortgage, should the creditor accept this treatment or absent a properly-filed objection. Section 1327(a) explains the binding effect of confirmation of a plan:

> § 1327(a) The provisions of a confirmed plan bind the debtor and each creditor, whether or not the claim of such creditor is provided for by the plan, and whether or not such creditor has objected to, has accepted, or has rejected the plan. [109]

***353** Therefore, when the plan is confirmed, all debtors and creditors are bound by the terms of the confirmed plan. [110] This can occur either by a creditor affirmatively accepting or failing to object to the proposed plan. [111]

1. Consent

Although some may argue that the plain reading of section 1322(b)(2) prohibits a bankruptcy judge from modifying a homestead mortgage regardless of creditor acquiescence, a reading of section 506(a) in conjunction with section 1325(a)(5)(a) demonstrates otherwise. Section 506(a) reflects that a claim can be bifurcated into secured and unsecured portions despite the anticramdown provision, and section 1325(a)(5)(a) lends support to the proposition that a plan proposing a homestead mortgage cramdown could be confirmed upon creditor acceptance. [112] Recall that under section 506(a)(1) a claim is secured "to the extent of the value of such creditor's interest in the estate's interest in such property ... and is an unsecured claim to the extent that the value of such creditor's interest ... is less than the amount of such allowed claim." [113] Under section 1325(a) "the court shall confirm a plan if ... (5) with respect to each allowed secured claim provided for by the plan--(A) the holder of such claim has accepted the plan." [114]

Thus, section 506(a) applies to all cases filed under the Bankruptcy Code, and clearly states that a creditor's claim is secured only to the extent of the value of the collateral. [115] Also, under section 506(a) any excess over the value of the collateral is granted an unsecured claim. [116] Section 506(a) merely concerns the classification of an undersecured claim, not with its treatment under any pertinent chapters of the Bankruptcy Code. There is no distinction made in section 506(a) for the type of collateral subject to its reach as well as no evidence of any legislative intent to exclude homestead properties from the purview of section 506(a). [117] Once a determination of the allowed secured status has been made, sections 1322 and 1325 determine the proper treatment of such claim. Even the Supreme Court in *Nobelman* has held that a valuation under section 506(a) is appropriate on a debtor's primary residence despite the anti-modification provision of section 1322(b)(2). [118]

***354** Section 1325(a)(5)(A) reflects that the bankruptcy judge must confirm a plan with respect to the treatment of a secured claim if the secured claim holder accepts the plan. [119] The premise that a claim on a debtor's homestead can be modified by the bankruptcy plan despite the anti-cramdown provision was addressed in the case of *In re Wilcox*. [120] In that case the debtors filed a motion seeking to value a creditor's junior lien at zero dollars so that it could be stripped off and ultimately discharged, and the creditor objected. [121] At the hearing, the parties compromised to reduce the lien, greatly reduce the payments on the mortgage, and waive any rights the creditor had to any contractual pre-petition arrearages to which it might otherwise have been entitled. [122] The bankruptcy trustee objected to the plan on the grounds that it violated section 1322(b)(2) because it modified a claim secured only by a lien on the debtor's principal residence. [123] Because the parties themselves agreed to the modification of the creditor's rights, the court held that the plan did not violate section 1322(b)(2) and upheld the plan. [124] The exception in section 1322 only prevents a debtor from forcing a creditor to accept modification of its lien; if the parties consent to the modification, then it is permissible. [125]

The court explained that "[i]n the end, bankruptcy is about solutions and the Trustee's position sets up an artificial--and legally unsound--barrier to the efforts of the interested parties to reach a solution that works for both sides. Sound public policy encourages the voluntary settlement of disputes." [126] In addition the court indicated that section 1322(b)(2):

> [O]perates to protect the rights of a homestead creditor like the [c]credit [u]nion. By choosing to voluntarily modify its claim for purposes of the [d]ebtor's ... [p]lan, the [c]redit [u]nion has voluntarily and knowingly waived any protection of its interests afforded by § 1322(b)(2). Certainly, a party who enjoys the protection of a statutory or even constitutional provision may waive that protection. [127]

Accordingly, the court held that it is permissible for a chapter 13 plan to reduce the amount being provided to a junior mortgagor whose claim is secured ***355** by a debtor's homestead if such reduction is a result of a compromise negotiated by the debtor and the holder of the claim. [128] The *Wilcox* holding is consistent with the requirement of 11 U.S.C. § 1325(a)(5)(A) that a secured creditor retain its lien and receive the present value of its allowed secured claim through the payments made to it under the chapter 13 plan, unless the creditor agrees to be treated differently in the plan or if the collateral is surrendered by the debtor. [129] The holding in *Wilcox*, and the clear statutory language in section 1325(a)(5)(A) give a debtor the ability to file a chapter 13 plan and propose a cramdown of the debtor's homestead in good faith, and then attempt to convince the creditor, post-petition, to accept its treatment of the plan. There is no requirement that acquiescence to the treatment must be obtained prior to the petition being filed. A creditor holding an undersecured claim may prefer to retain its lien to the full extent of the replacement value of the collateral and to receive the immediate income stream from the payments provided it through the chapter 13 plan, as required by *Associates Commercial Corp. v. Rash*, [130] rather than the debtor modifying the plan and the schedules to reflect a surrender of the property as permitted under section 1325(a)(5)(c) of the Bankruptcy Code. Thus, when considering whether to acquiesce to cramdown, a lender should consider the time value of money, in that acquiescence would permit the lender to begin to receive an income stream based on the current market value of the property, rather than have to wait to receive the diminished foreclosure value sometime in the distant future.

Adam Levitin has recently suggested this premise that despite the anti-modification provision, cramdown can still be achieved through creditor consent to the plan. [131] He proposed that cramdown can exist under the current Code and could be implemented immediately on a large scale by the Federal Housing Finance Agency requiring that Government Sponsored Enterprises ("GSEs") "adopt a policy of consenting to chapter 13 plans that have cramdown." [132] Mr. Levitin suggested this would further circumvent the two major objections of allowing cramdown in the first place: the moral hazard problem and the second lien free-rider problem. [133]

The moral hazard stems from the theory that a debtor is responsible for the loan entered into in the first place. However, by implementing a policy for consent to cramdown, the GSEs could make plan consent conditional on their ***356** own valuation, could share in appreciation and could establish eligibility cutoffs. [134] Therefore, the GSEs could establish a bright line test to determine the circumstances in which it would consent to a mortgage cramdown using net present value calculations. Further, the lender could prognosticate the likelihood and extent of the property's appreciation over the remaining life of the mortgage before the borrower sells or refinances. Additionally, bankruptcy is still a significant cost to the borrower with both the stigma of filing bankruptcy and the ramifications post-discharge. [135]

A program encouraging creditor consent to cramdown would also circumvent the issue of free-riding second liens. Completely unsecured mortgages may already be crammed down in bankruptcy. [136] But often if a debtor is unable to cure his or her first mortgage on their homestead, then they do not deal with the second mortgage either. [137] By encouraging consent to cramdown of a debtor's first mortgage, the second mortgage could be handled in turn. [138]

A creditor has other positive incentives to acquiesce to a cramdown. If a homeowner's secured creditor does not acquiesce to the cramdown, the debtor could convert the chapter 13 case to a chapter 7. This can be done by the debtor filing a notice of conversion at any time. [139] Upon conversion the lender would wait to eventually receive the diminished foreclosure value of the property. Case conversion would also bar the creditor from pursuing any deficiency post-chapter 7 discharge.

A lender's refusal to accept a plan's principal reduction may cause the debtor to surrender the property or convert the debtor's case, and the lender's foreclosure value of the property would only be realized at a later date. This diminished value would be received either after the debtor has been afforded the right to receive a chapter 7 discharge, the chapter 13 plan that does not provide for the lender is confirmed, or the lender receives relief from stay. This foreclosure value that the lender would receive at some time in the future could be further delayed by a debtor that chose to defend any *in rem* foreclosure that would necessarily ensue, once relief from stay was secured to proceed accordingly.

***357 2. Lack of Objection**

Alternatively to affirmative consent, a bankruptcy judge should confirm a plan if an affected creditor fails to timely object. If a debtor proposes a plan modifying a creditor's rights on a claim secured solely by the debtor's homestead, and the creditor chooses to avail itself of the anti-cramdown provisions of section1322(b)(2), the creditor must voice an objection to its plan treatment otherwise its silence will be construed as a waiver of the protections of section 1322(b)(2). [140]

The principle of failing to assert a statutory right constituting a waiver of such right in the context of bankruptcy was addressed by the Supreme Court in *Taylor v. Freeland & Kronz*. [141] The court held that a bankruptcy trustee's failure to timely object to a debtor's claimed exemption, regardless of whether the debtor had a colorable statutory basis for claiming the exemption, prevented the trustee from challenging the validity of the exemption. [142]

When a secured creditor holding a security interest in a debtor's homestead fails to timely object to its treatment in the debtor's proposed plan, the *res judicata* effect of a confirmed chapter 13 plan can effectively avoid a creditor's lien or modify its rights. Upon notice of the confirmation hearing, creditors have the burden of reviewing the plan and making any objections to it. [143] This ability to modify the claim of a creditor holding a security interest in a debtor's homestead may occur, absent a lender's objection, even if there is no basis in law for its treatment provided that the plan explicitly sets forth its treatment and the creditor is afforded due process. [144] The requirement of due process in this context is met when the creditor receives notice that is reasonably calculated to, and under the circumstances apprises the creditor that its rights to its claim may be altered. [145] When a debtor attempts to modify the claim of a secured creditor, the Federal Rules of Bankruptcy Procedure require that a creditor receive notice of any proposed plan, of the date, time and place of the confirmation hearing, as well as notice with regard to the proscribed time period afforded the creditor to ***358** object to its treatment in the debtor's proposed plan. [146] Thus, creditors that disregard notice do so at their own risk. [147]

The Supreme Court recently addressed the *res judicata* effect of a confirmed chapter 13 plan in *United Student Aid Funds, Inc. v. Espinosa*, [148] and held that a creditor could not challenge the terms of a plan after it had been confirmed. [149] In this case the debtor filed a plan "that proposed to discharge a portion of his student loan debt," however he did not initiate any adversary proceeding as required under the Code to effectuate such a discharge. [150] The creditor received proper notice of the plan, did not object to it, and the bankruptcy court confirmed the plan. [151] Years later the creditor filed a motion asking for a ruling that the plan was void, pursuant to Rule 60(b)(4) of the Federal Rules of Civil Procedure. [152] The Court upheld the confirmed plan stating that the creditor received adequate notice and that it could have timely objected, and further if it obtained an adverse ruling on its objection, it could have appealed timely. [153] By failing to object, the creditor waived its rights under the Bankruptcy Code.

This binding effect of chapter 13 extends to orders confirming a bankruptcy plan whether or not the plan complies with section 1322(b)(2) of the Code. [154] For example in *In re Bateman*, [155] the court upheld a confirmed chapter 13 plan even though it conflicted with the mandatory provisions of section 1322(b)(2) because the creditor failed to object to the plan's confirmation. [156] Specifically the court stated:

> The [p]lan was improperly confirmed because it conflicted with § 1322[(b) (2)]'s mandatory provisions. Had [the creditor] objected to or appealed from the [p]lan's confirmation, it would have prevailed without question, given the facts presented to us. [The creditor], however, did not do so and § 1327 binds creditors to the provision of the [p]lan. [157]

***359** This case law suggests that a creditor's failure to object to a bankruptcy plan modifying its rights of a claim on a debtor's homestead gives a *res judicata* effect to the confirmed plan that binds the lender.

B. Additional Security for the Mortgage

Because section 1322(b)(2) prohibits bankruptcy judges from modifying the rights of a mortgage lender whose claim is secured "only" by a chapter 13 debtor's homestead, any additional security interest taken by the lender in the debtor's personal property may render the section 1322(b)(2) anti-modification provision inapplicable. When determining whether a creditor's claim is secured solely by the debtor's homestead in a chapter 13 case, the bankruptcy court should examine the mortgage loan documents. [158] If the mortgage and note provide for an additional security interest in the residence, "then the claim is not secured solely by the debtor's residence and can be modified." [159] As the court observed in *Hammond v. Commonwealth Mortgage Corp.*, [160] "creditors who demand additional security ... in personalty or escrow accounts and the like pay a price." [161] "Their claims become subject to modification. Their recourse, if they wish to avoid modification, is to forego the additional security[]" at the time of the loan transaction. [162]

To determine the applicability of section 1322(b)(2), a bankruptcy judge should consider whether any additional security interest evidenced in the homestead loan documents is a component part of the real property and whether the personal property has independent value. [163] If a lender successfully argues that the taking of additional security was a mere enhancement, or that the additional collateral has little or no independent value, then the taking of such additional interest in the mortgage should not result in the lender forfeiting the anti-cramdown protections. [164] Furthermore, "the enforceability of the additional security interest or the availability or value of the additional collateral" at the time the

case is filed does not affect the ability of the bankruptcy judge to modify the claim. [165] Section 1322(b)(2) only requires that the claimholder have ***360** a security interest in something other than real property. [166] In *In re Larios*, [167] the court held that "[f]or purposes of applying § 1322(b)(2), it matters not whether the security interest has attached, nor whether it is perfected, only whether it is extant and not released, satisfied or otherwise terminated." [168]

If there is any security interest in personal property, the protection is lost. The state laws in which the debtor resides define the additional security taken by the lender as personal or real property. [169] If a bankruptcy practitioner can demonstrate that the additional security taken by a lender in a mortgage or deed of trust is personal property under applicable state law, the debtor should be entitled to cramdown the residence despite section 1322(b)(2).

1. Escrow Accounts

When a mortgage lender holds a security interest in some of the debtor's personal property as further collateralization for its claim against a debtor's homestead, it loses the anti-modification protection afforded by section 1322(b)(2). [170] This occurs when the mortgage documents create a security interest in an escrow account. [171] Accordingly, when a residential mortgage encumbers both a debtor's homestead and an escrow account that is utilized for the payment of property taxes, the lender's claim is arguably subject to cramdown despite section 1322(b)(2). [172]

The determination of whether a mortgagee's claim is secured solely by the security interest in a debtor's homestead within section 1322(b)(2) is determined by examining the loan documents. [173] If this examination reveals that such instrument provides for a security interest in addition to the security interest in the residence, then the claim is not secured solely by the debtor's homestead residence and can be modified. [174] The pledge by a debtor of the escrow funds in a security instrument and the subsequent execution of the instrument by a debtor creates a security interest in the escrow account that becomes additional security for the debt in addition to the debtor's residence. [175] The majority of bankruptcy courts have concluded that a security interest in an escrow account for taxes and ***361** insurance takes a lender's claim outside the protection of section 1322(b)(2) and subjects it to modification. [176]

For example, the court in *In re Stewart* [177] held that a security interest in an escrow account took a mortgagee's claim outside the scope of section 1322(b)(2) and thus the claim could be crammed down under section 506. [178] In that case the mortgage document contained a provision entitled "'Uniform Covenants,'" stating "'[t]he [f]unds [escrowed for the taxes and insurance premiums] are pledged as additional security for the sums secured by this [m]ortgage.'" [179] This was true even though no funds had been delivered to the mortgagee pursuant to this covenant. [180] The pledge of the escrow account was an additional security interest and therefore the claim of the mortgagee could be modified. [181]

After the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 was passed ("BAPCPA"), bankruptcy courts again addressed the issue of escrow accounts bringing a lender's claim outside the scope of section 1322(b)(2). [182] The BAPCPA redefined "debtor's principal residence" in section 101(13A) and "incidental property" in section 101(27A). [183] Under the BAPCPA, "debtor's principal residence" means "a residential structure ... including incidental property, without regard to whether that structure is attached to real property; and ... includes an individual condominium or cooperative unit, a mobile or manufactured home, or trailer." [184] The BAPCPA defines "incidental property" as:

> [P]roperty commonly conveyed with a principal residence in the area where the real property is located ... all easements, rights, appurtenances, fixtures, rents, royalties, mineral rights, oil or gas ***362** rights or profits, water rights, escrow funds or insurance proceeds; and ... all replacements or additions. [185]

The issue of taking an interest in escrow funds, as it pertains to the expanded definitions contained in section 101 under BAPCPA was specifically addressed in the case *In re Thomas*. [186] In *Thomas*, a complaint was filed to determine the secured status of a residential mortgage lender's claim and to determine whether the lender's rights were protected from modification in the debtor's chapter 13 plan. [187] The security instrument encumbering the debtor's homestead contained a covenant regarding "miscellaneous proceeds" and required that the lender use these proceeds for restoration or repair of the property if economically feasible and if its security interest was "not lessened." [188] This covenant further stated that if the restoration or repair of the property was not feasible or if the lender's security interest was somehow lessened that these miscellaneous proceeds be applied to the sums secured by the security interest, whether or not then due, with any excess paid to the debtors. [189] The *Thomas* court determined that escrow funds are not real property under Pennsylvania law, and held that the debtor's mortgage could be modified notwithstanding section 1322(b)(2) because of the creditor's security interest in the escrow funds. [190]

The United States Fourth Circuit Court of Appeals in *In re Ennis* [191] took an alternative position regarding the treatment of security interests in escrow accounts in relation to section 1322(b)(2). [192] The *Ennis* court first determined that section 1322(b)(2) "has two distinct requirements: first, the security interest must be in real property, and second, the real property must be the debtor's principal residence." [193] The court held that the definition of a debtor's homestead contained in section 101(13A) addresses only the second requirement contained in section 1322(b)(2), leaving in place the requirement that the security interest must be in personal property in order for the anti-modification protections afforded to residential mortgage lenders to apply. [194] The court stated that the "definition of 'debtor's principal residence' and the real property requirement in the anti-modification clause may each be given effect according to their plain language: 'property can be a debtor's principal residence ***363** even if it is personalty, but it cannot be subject to the [anti]-modification provision unless it is realty.'" [195]

In *In re Bradsher*, [196] Wells Fargo--the secured residential mortgage lender that was opposing cramdown--argued that section 101(13A) sweeps within the definition of a debtor's homestead "incidental property," which section 101(27B) defines as including escrow funds. [197] The court held that although Wells Fargo was correct that escrow accounts fall within the definition of a debtor's principal residence when interpreting the meaning of section 101(13A) in conjunction with section 101(27B), this alone does not mean that the anti-modification provision contained in section 1322(b)(2) was applicable. [198] A secured residential mortgage lender can only avail itself of the anti-modification protections if escrow accounts are defined as real property under applicable state law. [199] Accordingly, the court looked to North Carolina law to determine whether an escrow account would be regarded as real property, and found that the General Statutes of North Carolina contain a number of statutory definitions of real property, none of which would pull an escrow account within its purview. [200] The court concluded that "the Wells Fargo indebtedness is not secured solely by real estate that is the [d]ebtor's principal residence and thus Wells Fargo is outside the protection from modification provided under section 1322(b)(2)." [201]

However, the Third Circuit came to a different conclusion in the case of *In re Ferandos*. [202] The mortgage document in that case contained a covenant setting up an escrow account for the payment of taxes, assessments, rent and insurance. [203] Looking to the laws of the state of New Jersey and the UCC, the court held that the funds placed in escrow existed "for the purpose of paying said taxes and insurance--a cost incurred by the debtor in connection with the ownership of the real property." [204] Because the debtor retained no interest in the funds once they were put in escrow, the court reasoned that the escrowed funds were not additional collateral that would take the lender's claim outside the scope of section 1322(b)(2)'s anti-modification provision. [205] Therefore, the mortgage was not modifiable. [206]

***364** A Florida court also determined a lender that has a security interest in an escrow account forfeits its protection from section 1322(b)(2) modification. [207] The *In re Brown* court held that "an escrow account is clearly not an item which is inextricably bound to the real property [.]" [208] However, in looking to Florida law the *Brown* court determined that the escrow account at issue was not a "security interest" and was therefore subject to the anti-modification provision. [209] The mortgage documents at issue directed the debtor to pay funds to the lender for taxes and insurance, which would be held in escrow. [210] However, the lender never actually established an escrow account. [211] Reading chapter 679 of the Florida statutes, which govern formation of security interests, the *Brown* court determined that because the escrow account was never actually created, it could not ever attach to property and therefore the debtor had no rights in the collateral. [212] The mere pledge of a potential escrow account does not take a claim outside the anti-modification protection of section 1322(b)(2). [213]

Under Florida law, an escrow account is a deposit account that is maintained and controlled by a mortgagee upon which the mortgage creates a security interest. [214] When this mortgage instrument is executed by a debtor, value is given as the debtor agrees to turn over escrow funds to the mortgagee in exchange for the payment of the taxes and insurance by the mortgagee. According to the security instrument illustrated herein, the mortgagee has control over the disposition of the funds deposited in the account to pay the taxes and the insurance. [215] Under Florida Statute section 1041, the mortgagee would be the customer of the deposit institution with regard to the escrow account. [216] This pledge of funds and the establishment of an escrow account is required in order to remove the claim from the protections afforded to certain claims under section 1322(b)(2). [217]

Logically, if a mortgage lender has an interest in escrows, this interest is an interest over and above the interest in a debtor's real property that is the debtor's primary residence, removing the claim from the scope of section 1322(b)(2). An interest in the escrow account is usually found in a provision in the mortgage ***365** document listing escrows as part of collateral for the loan. [218] States require interest to be earned on escrow accounts, and thus not only would the escrowed funds that a lender attaches serve as additional security, but the interest earned on a borrower's escrowed funds would as well. [219] Furthermore, tax bills and insurance premiums are paid from a borrower's escrowed funds; a surplus may exist in a borrower's escrow account that serves to further collateralize a debtor's homestead mortgage liability. [220] Thus, there is a possibility that escrowed funds may contain monies that are not necessary to pay taxes and insurance and are nevertheless pledged as additional collateral securing a debtor's homestead mortgage obligation. [221] If lenders are interested in drafting a "modification-proof" mortgage, they ought to restrict their interest in escrowed funds to the right to apply their interest for the dedicated purpose of paying taxes and insurance alone.

2. Multi-Unit Properties

Most courts addressing the issue have held that a debtor occupying one unit of a multi-unit property does not prohibit a section 1322(b)(2) court ordered mortgage modification. [222] In *In re Scarborough,* [223] the Third Circuit held that ***366** the section 1322(b)(2) protection does not apply to a multi-unit property where the debtor lived in one unit and rented the others. [224] If a security interest is taken in personal property to further collateralize a loan, the lender loses the protection afforded by section 1322(b)(2). [225] This is the majority view. Other courts have held that the anti-modification provision applies to property used as the debtor's homestead regardless of how the mortgage is additionally secured. [226]

Some jurisdictions have applied a case-by-case approach. [227] These jurisdictions look at the predominant character of each transaction. [228] In *In re Bulson*, [229] the court cited to the following factors considered in *Brunson v. Wendover Funding* when determining the applicability of 1322(b)(2) protection:

> Whether the Debtor (to the lender's knowledge) owned other income producing properties or other properties in which she could choose to reside; whether she had a principal occupation other than as landlord, and the extent to which rental income or other business income produced from the real estate contributed to her income; whether her total income was particularly high or particularly low; whether the mortgage was handled through the commercial loan department or the residential mortgage loan department of the lender; whether the interest rates applied to the mortgage were home loan rates or commercial loan rates; the demographics of the market (e.g., are "doubles" a much more ***367** affordable "starter home" than a single, in that locale); and the extent to which, and purpose for which, potential business uses of the land (such as farming) were considered by the lender. There surely may be others. [230]

Along this line of reasoning, a debtor that purchases an income-producing property and later moves into the property should be able to cramdown the mortgage despite the debtor living in the property on the petition file date.

3. Income-Producing Property

A court must examine the mortgage documents to determine whether a claim is secured "only" by a debtor's homestead or if there is additional security in rents and profits. [231] State law defines property rights. In *In re Rosen*, [232] the mortgage defined the secured property as "all improvements ... easements, rights, appurtenances, rents, royalties, mineral, oil and gas rights and profits ...." [233] New Jersey law defined "real property" as "[e]very deed conveying land shall ... be construed to include all and singular buildings, improvements, ways, woods, waters ... rights ... and the reversion ... remainders, rents, issues and profits thereof, and of every part and parcel thereof." [234] Thus, the rents and profits arose directly from the realty, and its reference in the mortgage did not create an additional security interest; so the mortgage was not modifiable. [235] If state law defines rent as part of the property, an additional security interest in rents will not take a lender's claim outside the section 1322(b)(2) modification protections. [236]

Conversely, the *In re Jackson* [237] court, applying Illinois law held that the lender's claim was not modifiable. [238] The mortgage stated that as additional security, "the mortgagor does hereby assign to the mortgagee all the rents, issues and profits now or which may hereafter become due for the use of the premises ***368** hereinabove described." [239] Pursuant to Illinois law, a mortgagee is not entitled to rents and profits unless they have been pledged in the documents. [240]

The assignment of rents conveyed security in addition to the real estate, thereby taking it outside section 1322(b)(2)'s purview. [241]

4. Insurance Proceeds

Most courts have held that a debtor's homestead mortgage containing an interest in insurance proceeds will not lose its anti-modification protection. [242] These courts reason that insurance is tantamount to adequate protection and not a security interest. [243] It is "'merely a contingent interest--an interest that is irrelevant until the occurrence of some triggering event and not an additional security interest for purposes of § 1322(b)(2).'" [244] Language allowing a lender to use insurance proceeds does not create an additional security interest in the mortgage. [245]

However, language in the mortgage which "goes beyond the traditional right to use proceeds to pay off [an] obligation ... may constitute the pledge of additional security." [246] In *Transouth Financial Corp. v. Hill*, [247] the loan agreement had the following provision:

> S[ecurity]: To protect us if you don't repay your loan, you grant us a security interest in the collateral checked below. In addition, you assign to us any proceeds which may become payable through insurance on the property or written in connection with this loan. This includes unearned or return premiums. [248]

The court held that the lender took an additional security interest in the debtor's credit insurance proceeds and refunded premiums, and thus the claim ***369** was modifiable. [249] In *In re Jones* [250] the court held that security interests in condemnation awards and insurance proceeds constituted additional collateral, thereby making the claim modifiable. [251]

In California the Fannie Mae/Freddie Mac standard deed of trust form states:

> **Property Insurance.** *All insurance policies ... shall include a standard mortgage clause, and shall name Lender as a mortgagee and/or as an additional loss payee .... Borrower hereby assigns to Lender ... Borrower's rights to any insurance proceeds* ... Lender may use the insurance proceeds ... to pay amounts unpaid under the Note or this Security Instrument, whether or not then due. [252]

By utilizing standardized Freddie Mac Uniform Instruments the lender takes a security interest in not only the real property, but also personalty. [253] The lender has a security interest in proceeds earmarked for the replacement of furnishings, clothing, etc., which arguably removes the mortgage from the purview of the anti-modification protection. [254]

***370 5. Fixtures and Appliances**

The section 1322(b)(2) protection does not preclude a modification of an undersecured homestead mortgage claim that takes a security interest in appliances, machinery, furniture, and/or equipment. [255] In *In re Hammond*, [256] the mortgage gave the creditor a security interest in "any and all appliances, machinery, furniture and equipment (whether fixtures

or not) of any nature whatsoever now or hereafter installed in or upon said premises ....” [257] The court concluded the mortgage could be modified because of the security interest taken in the debtor's personalty. [258] Also, in *Hutchins v. Commonwealth Mortgage Corp.*, [259] the court held that where an interest was taken in all the appliances, machinery, furniture and equipment on the premises that the mortgagee's claim could be modified. [260] Cases in the Third Circuit clearly hold that a “security interest in fixtures is considered collateral in addition to the debtor's principal residence.” [261]

Not all courts have held that an interest in fixtures takes a mortgage outside the anti-modification protection. In *In re LeBlanc*, [262] the mortgage documents securing “[a]ll furniture, fixtures, and equipment, now or hereafter owned by the Mortgagor and located on, or used or intended to be used in connection with the [p]roperty or the [i]mprovements .... [T]he foregoing shall be deemed fixtures[,]” did not nullify the section 1322(b)(2) modification protection. [263] The court held that the mortgage gave a security interest in collateral that was incident of the real property. [264] It was “‘nothing more than an enhancement ... or can ... be made a component part of the real property or is of little or no independent value.’” [265]

The Florida uniform Fannie Mae/Freddie Mac Instrument states: “Borrower does hereby mortgage, grant, and convey to Lender, the following described property .... [A]nd all easements, appurtenances, and fixtures now or hereafter a part of the property.” [266] Fixtures are an interest in real property that straddle ***371** the line between real and personal property. [267] In *Dependable Air Conditioning & Appliances, Inc. v. Office of Treasurer & Insurance Commissioner*, [268] the court held that fixtures are created by attaching personal property to real property in such a manner that it becomes part of the real property. [269] Nevertheless, not all personalty attached to real property becomes part of Florida real property. The degree to which the chattel is annexed to the real property, the adaptation of the chattel to the use of the land and the intention of the parties as to whether the chattel would remain personalty or become part of the real property must be determined. [270]

Once personalty becomes a fixture, its rights are determined by real property principles as they are taxed as part of the real property. [271] They can be sold as part of the realty, and are subject to the mortgage. [272] Thus, an interest in fixtures would likely not render a debtor's homestead mortgage modifiable. However, where there is no evidence of intent to annex fixtures as a permanent accession to the real property, the articles are not fixtures. [273]

6. Mobile Homes

A security interest taken in a debtor's mobile home and the real property on which it is situated may remove the claim from section 1322(b) protection. [274] Recall there are two requirements for a claim to be excluded from modification under section 1322(b)(2): (1) the security interest must be in real property and (2) the real property must be the debtor's homestead. [275] Regarding mobile homes, “property can be a debtor's principal residence even if it is personalty, but it cannot be subject to the no-modification provision unless it is realty.” [276]

***372** If the mobile home is deemed personal property, then the claim is modifiable. [277] In most cases there is no dispute whether a mobile home is a debtor's homestead. [278] Thus, the analysis shifts to whether the home is personalty or realty. [279] As previously discussed in *Nobelman*, “[i]n the absence of a controlling federal rule, we generally assume that Congress has ‘left the determination of property rights in the assets of a bankrupt's estate to state law,’ since ‘such

[p]roperty interests are created and defined by state law.'" [280] Therefore, state law dictates whether a mobile home is realty. [281] In *In re Ennis*, [282] Virginia law was examined to determine if the debtor's homestead, a mobile home, was non-modifiable real property. [283] The security agreement granted a lien on the home situated on a rented lot. [284] The claim was modifiable because the mobile home was classified as "tangible personal property" for tax purposes and the security agreement stated the home would "'remain personal property'" and "would 'not become a fixture or part of the real property' without [lender's] written consent." [285] The debtors maintained title to the home, thus preserving its nature as personalty. [286]

BAPCPA's definition of a "debtor's principal residence" under section 101(13A) did not broaden the scope of the anti-modification provision over mobile homes. [287] Under section 101(13A) a "debtor's principal residence" is "a residential structure, including incidental property, without regard to whether that structure is attached to real property; and includes an individual condominium or cooperative unit, a mobile or manufactured home, or trailer." [288] Lenders have unsuccessfully argued that Congress intended to expand the definition of "debtor's principal residence" to include mobile homes whether affixed to real property or not, and regardless of whether they are considered ***373** real property under state law. [289] The majority of courts have held that section 1322(b)(2) is limited to real property despite section 101(13A). [290]

In *In re Oliveira*, [291] the creditor held an allowed secured claim against the debtor's mobile home. [292] However, the creditor had "no lien or any other type of interest in the real property upon which the manufactured home sits[.]" [293] The parties agreed that the mobile home constituted personalty and not realty under Texas law. [294] Notwithstanding, the creditor argued that section 101(13A) brought mobile homes within the anti-modification purview of section 1322(b)(2) regardless of whether the home was attached to real property. [295] The court rejected this argument and deemed the claim modifiable. [296]

7. Cross-Collateralization and Future Advances

Some lenders include cross-collateralization clauses in their loan and deposit account agreements. These clauses make the collateral pledged on one loan serve as collateral for any other outstanding or future loans (i.e. vehicle loans, lines of credit, credit cards, etc.) by the same institution. These clauses have the effect of converting unsecured debt (i.e. lines of credit, credit cards, etc.) into secured debt. [297]

No court has addressed whether cross-collateralization clauses take a lender's claim outside the anti-modification protection of section 1322(b)(2). However, one court discussed--albeit in dicta--that a cross-collateralized debt would cause the indebtedness to not be secured solely by a debtor's homestead. [298] In *In re Kain*, [299] the creditor had a pre-petition security interest in the debtor's crops, livestock and equipment, and additionally was granted five mortgages of the debtor's real property. [300] The creditor's indebtedness was cross- ***374** collateralized and deemed not secured solely by the debtor's principal residence. [301] Although this was a chapter 11 case, it supports the argument that this type of clause allows the claim to become modifiable.

In *In re Crystian*, [302] the court examined a cross-collateralization clause in a chapter 11 case. [303] Under section 1123(b)(5) a plan may "modify the rights of holders of secured claims, other than a claim secured only by a security interest

in real property that is the debtor's principal residence ....” [304] In *Crystian*, the debtor had a checking account with the creditor bank that was opened seven and a half years before the homestead mortgage. [305] The checking account agreement provided:

> Security interest .... [Y]ou hereby grant us a security interest upon any balance in this account to secure the payment of any debt that you, or any one of you, may owe us, whether direct or indirect, and whether due or to become due and you agree that we have the right to offset any such balance against any such debt. [306]

Because the bank acquired its claim on the debtor's homestead after the account was opened, the mortgage was additionally secured by any account balance. [307] Therefore, the bank's claim could be modified under section 1123(b)(5). [308] This provision under chapter 11 is identical to section 1322(b)(2).

If a debtor has cross-collateralized deposit accounts with the same institution holding his/her homestead mortgage, then the anti-modification provision should not apply. A deposit account is clearly the debtor's personalty that would serve as additional security for the mortgage. [309]

The following cross-collateralization clause is included in the default provisions of paragraph nineteen of the Florida Fannie Mae/Freddie Mac Uniform Mortgage: “If Borrower meets certain conditions, Borrower shall have ***375** the right to have enforcement of this Security Instrument discontinued .... Those conditions [include] that Borrower ... (b) *cures any default of any other covenants or agreements*.” [310] To reinstate a mortgage a borrower must “cure[] any default of any other ... agreements.” [311] This might include other obligations the borrower maintains with the mortgage lender including a car loan, credit card, line of credit or overdraft.

Florida statute section 697.04 states the following in regard to the enforceability of future advance clauses as they pertain to mortgages secured by real property:

> Any mortgage or other instrument given for the purpose of creating a lien on real property ... may, and when so expressed therein shall, secure not only existing indebtedness, but also such future advances .... Such lien, as to third persons without actual notice thereof, shall be valid as to all such indebtedness and future advances from the time the mortgage or other instrument is filed for record as provided by law. [312]

Under Florida law, future advances are secured when an appropriate provision is made in the mortgage securing such advancements. [313] Future advances would be fees, costs and advancements to which a secured lender would be contractually entitled to under the security instrument. A debtor's homestead whose mortgage contains a future advance clause may be subject to modification. This is because section 1322(b)(2) prevents the modification of a debtor's homestead refinance or acquisition mortgage, not unspecified future business or personal debts. [314]

8. Definition of “Debtor's Principal Residence”

BAPCPA added section 101(13A) which defines a "debtor's principal residence" as a "residential structure ... including incidental property, without regard to whether that structure is attached to real property." [315] "Incidental ***376** property" is defined under section 101(27B) as "property commonly conveyed with a principal residence in the area where the real property is located ... easements, rights, appurtenances, fixtures, rents, royalties, mineral rights, oil or gas rights or profits, water rights, escrow funds or insurance proceeds; and ... replacements or additions." [316] Because a debtor's principal residence includes incidental property, creditors argue that escrow funds and insurance proceeds would not serve as additional security causing a homestead mortgage claim to be modifiable.

The argument that BAPCPA precludes a debtor from modifying his principal residence was made in *In re Lunger*. [317] In *Lunger*, a homestead mortgage lender objected to the debtor's proposed modification of its claim under section 1322(b)(2). [318] The debtor asserted that the security interest taken in an escrow account caused the claim to be modifiable, to which the lender responded that the scope of section 1322(b)(2) had been broadened by BAPCPA. [319] The court held that Congress chose to define "incidental property" as part of a "debtor's principal residence," and thus had "effectively broadened" the definition of 1322(b)(2) to include an escrow account. [320] Even though under Pennsylvania law, an escrow account is separate property, independent of the real property, BAPCPA effectively barred the modification of a loan secured by a debtor's homestead. [321] The *Lunger* court further held that to the degree BAPCPA may be at odds with state law and pursuant to *Butner v. United States*, [322] to the extent that federal laws are in conflict with state laws, the state laws can be suspended. [323]

In reaching its holding, the court in *Lunger* relied on *In re Shepherd*,(*Shepherd I*). [324] In *Shepherd I*, [325] the creditor with a security interest in debtor's mobile home, but not in the real property on which it rested, objected to the confirmation, claiming improper modification of its homestead mortgage claim under section 1322(b)(2). [326] The *Shepherd I* court held that the section 101(13A) definition of a "debtor's principal residence," read in conjunction with section 1322(b)(2),

> ***377** results in an absurdity because § 1322(b)(2) must now be construed to provide that a debtor may not modify the claims of a creditor holding a security interest in the debtor's residential structure, including a condominium, cooperative, mobile home, or trailer, irrespective of whether it is attached to the real property, but only if the security interest includes the real property. [327]

Although the court in *Lunger* relied on *Shepherd I*, the district court reversed the *Shepherd I* decision after *Lunger* was decided. [328] In *In re Shepherd* (*Shepherd II*), [329] the district court held that the new definition of a "debtor's principal residence" does not alter the requirement under section 1322(b)(2) that it be real property. [330] The *Shepherd II* court noted the holding in *Herrin v. GreenTree-Al*, wherein the *Herrin* court held that "[i]mposing the definition of 'debtors principal residence' on § 1322(b)(2) results ... in the ... proposition that property can be a debtor's principal residence even if it is personalty, but it cannot be subject to the anti-modification provision unless it is realty." [331] Agreeing with the majority, the court in *Shepherd II* concluded that the only requirements of section 1322(b)(2) are "1) that the property in question be real property and 2) that the real property be the debtor's principal residence." [332]

The district court in *Shepherd II* reasoned that under principles of statutory construction regarding section 1322(b)(2) the "majority of courts have found that the plain meaning of the statute is clear. Because this plain meaning does not reach an illogical result, the court is not required to parse the legislative history to supplement its analysis." [333] The court

further reasoned that "[h]ad Congress intended to apply the anti-modification provision to personal property that is the debtor's principle [sic] residence ... 'it could have done so with exceptional ease by merely redacting the word 'real' or adding the words 'or personal' in [s]ection 1322(b)(2).'" [334] The court concluded that the "legislative history does not, however, give any affirmative indication that the legislature intended this to modify that real property is the only sort of principal residence ***378** that is subject to the anti-modification provision" and that "the majority of courts have found that this supports the view that § 1322(b)(2) still requires the property to be real property." [335] Thus, the district court in *Shepherd II* held "the definition of 'debtors principal residence' in § 101(13A) does not operate to extend the anti-modification provision to structures that are not real property." [336] Although the court did not address the issue of a lender taking an interest in a debtor's escrow accounts or insurance proceeds in addition to the homestead, it effectively held that the section 101(13A) does not modify the clear language of section 1322(b)(2).

In examining the intent of Congress, a bankruptcy court in Alabama held that the definition of a "debtor's principal residence" in section 101(13A) did not change or modify the clear language contained in section 1322(b)(2). [337] This is because the court could "find no legislative history indicating exactly what Congress intended by its addition to the Bankruptcy Code of § 101(13A)." [338]

C. Nonrecourse States

To cramdown a mortgage in a chapter 13 case, two sections of the Code must be utilized: section 506(a), which permits valuation of real property subject to the estate, [339] and section 1322(b)(2), which permits bifurcation of certain undersecured mortgages. [340]

Although it appears that section 506(a) and section 1322(b)(2) may be in conflict, this is not the case. Section 506(a) deals merely with a claim's classification, not with its treatment once classified. [341] Once a claim is classified its treatment is determined under the pertinent Code sections. In *Nobelman*, the Court stated that "[p]etitioners were correct in looking to § 506(a) for a judicial valuation of their collateral .... [H]owever, that determination does not necessarily mean that the "rights" the bank enjoys as mortgagee, which are protected by § 1322(b)(2), are limited by a valuation of its secured claim." [342] Section 1322(b)(5) states:

> § 1322. Contents of plan. (b) Subject to subsections (a) and (c) of this section, the plan may ... (5) notwithstanding paragraph
>
> ***379** (2) of this subsection, 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. [343]

Thus, despite the anti-modification prohibitions, a plan may provide for the cure of an "unsecured claim or secured claim." [344] Although an undersecured homestead mortgage claim may be bifurcated under section 506(a), any cure would necessarily include both secured and unsecured portions. It is the modification of the creditor's rights and not the classification of his or her claim that is protected under section 1322(b)(2). [345]

Nobelman held that the determination of property rights in bankruptcy is to be settled in state law. [346] Therefore, state law would dictate which homestead mortgage rights would not be subject to modification in bankruptcy. [347] A debtor residing in a non-recourse state may be able to cramdown a homestead mortgage because the creditor does not hold a right to a deficiency claim upon foreclosure. A creditor's rights in a non-recourse state would be held intact upon cramdown as its rights upon foreclosure are limited to the collateral's value. Any bifurcated unsecured claim need only be provided for along with other allowed general unsecured non-priority claims.

D. Statutory Exception to Section 1322(b)(2)

An exception to the prohibition against a homestead mortgage cramdown is contained in section 1322(c)(2), which provides that a debtor may modify the lender's rights if the last scheduled loan payment is due prior to the last scheduled plan payment. [348] Also, section 1322(b)(5), which permits a homestead mortgage cure, provides "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." [349] An accelerated foreclosure judgment no longer represents a "claim on which the last payment is due after ***380** the date on which the final payment under the plan is due." [350] Acceleration fully matures the performance that is due from a breaching party to a contract. [351] Thus, upon acceleration, the claim would be subject to modification under section 1322(c)(2), which states:

> § 1322. Contents of Plan. (c) Notwithstanding subsection (b)(2) and applicable nonbankruptcy law ... (2) in a case in which the last payment on the original payment schedule for a claim secured only by a security interest in real property that is the debtor's principal residence is due before the date on which the final payment under the plan is due, the plan may provide for the payment of the claim as modified pursuant to 1325 (a)(5) of this title. [352]

The phrase "original payment schedule" contained in section 1322(c)(2) is not defined in the Code and "encompasses substantially different meanings depending on whether it is read broadly or narrowly." [353] It can be understood to reflect the amortization schedule, not taking acceleration into account. [354] However, as mentioned, upon acceleration the claim no longer represents a "claim on which the last payment is due after the date on which the final payment under the plan is due" under section 1322(b)(5). If acceleration does not constitute the "last payment on the original payment schedule" under section 1322(c)(2), the debtor would not be afforded the ability to cure a default or be afforded the right to cramdown. The end result would be that, upon acceleration, a debtor would have no mechanism to save a homestead in chapter 13.

A more reasonable approach would be to define "original payment schedule" as "reach[ing] the entirety of the mortgagee's right to payment, including the fully accelerated payment[.]" [355] This is because section 1322(c)(2) should be interpreted to apply to claims maturing before or during the chapter 13 case, [356] as with a pre-petition balloon payment. [357] When the entire debt ***381** becomes due before or during the chapter 13 case, either by a lender's actions or time passage, the claim's maturity should be treated alike for homestead mortgage cramdown purposes under section 1322(c)(2). [358]

The Bankruptcy Reform Act of 1994 was intended to allow a debtor to cure a homestead mortgage arrearage and to cramdown a homestead mortgage where the last scheduled mortgage payment came due prior to the last scheduled plan payment. [359] The pertinent language of the Act is as follows:

> § 1322 of title 11, United States Code, is amended--(1) by redesignating subsection (c) as subsection (d), and by inserting after subsection (b) the following: "(c) Notwithstanding 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*; and "(2) *in a case in which the last payment on the original payment schedule for a claim secured only by a security interest in real property that is the debtor's principal residence is due before the date on which the final payment under the plan is due, the plan may provide for the payment of the claim as modified* pursuant to § 1325(a)(5) of this title." [360]

These changes were necessary because of a split of authority that existed regarding whether a debtor's right to cure terminated upon entry of the foreclosure judgment or continued through the foreclosure sale. Congress determined that the debtor's rights in chapter 13 should be safeguarded by permitting the debtor to cure until completion of the foreclosure sale. [361]

"[T]he language of § 1322(c)(2) is sufficiently broad so as to apply with equal force and result to a foreclosure judgment." [362] Courts have held that section 1322(c)(2) applies to mortgages that balloon prior to or during the bankruptcy. [363] There is no difference between a fully-matured balloon mortgage and foreclosure judgment. [364] In each instance the lender is entitled to full payment. Given the 1994 Amendments' objective of affording debtors an ***382** opportunity to save their homes and the similarity between a matured mortgage and foreclosure judgment regarding right to payment, [365] a court should construe section 1322(c)(2) to allow a homestead mortgage cramdown once a foreclosure judgment is entered.

IV. EQUITABLE SUBORDINATION OF PREDATORY LOANS

Creditors are rarely punished for pre-petition conduct in bankruptcy. Typically a creditor's punishment is administrative in nature and results from its failure to follow the bankruptcy rules of procedure. [366] For instance, an unsecured creditor that does not file a proof of claim is not entitled to payment of any pro rata distribution allocated to its class. Additionally, a creditor that receives a timely notice of a bankruptcy case's commencement but files a late proof of claim could have its claim subordinated to that of other general unsecured claimants. [367] Also, a non-insider creditor that receives a preference payment within ninety days of filing the bankruptcy case under section 547(b)(4)(A) could be made to return the amount received for an antecedent debt to the trustee to be disbursed pro-rata to creditors of the estate in relation to their respective priorities. [368] This ability of the bankruptcy trustee to claw back pre-petition assets of the debtor provides no deference to the creditor that the debt was legally owed and received by the creditor pre-petition in conformance with state law. [369] These creditors are typically powerless in determining the timing of the filing of any bankruptcy petition in order to be protected from such harsh treatment. [370]

Bankruptcy law makes certain judgments regarding the worthiness of paying certain creditors. For instance, under section 507 certain creditors are deemed by Congress as having priority claims, including taxes, wages, and familial

support obligations. [371] Furthermore, under section 523, Congress made a judgment call in determining that some debts may not be discharged in bankruptcy, including but not limited to taxes, familial support obligations, student loans, and criminal restitution. [372] In these ways bankruptcy law typically rewards creditors that it considers superior to other creditors, while rarely ***383** punishing creditors that have engaged in egregious, immoral, and reprehensible conduct before bankruptcy.

In bankruptcy, a mortgage claim that is secured solely by a debtor's homestead can only be described as being given super-priority status. This conclusion is based on the fact that if a debtor wishes to keep his homestead, the lender's secured mortgage claim would need to be satisfied in full even over administrative and priority claims, whether or not such mortgage claim is supported by the current market value of the collateral that secures it. [373] In this fashion, such residential mortgage claim is entitled to not only having its entire claim paid in full, but also for the debtor to pay such claim under the original pre-petition terms of the original not--no matter how predatory or egregious. [374]

The super-priority favorable treatment of residential mortgage lenders was likely bestowed on this class of creditors in bankruptcy based on the prudent underwriting standards that were employed when section 1322(b)(2) was added to the Code. [375] The underwriting practices of recent years have changed this historical landscape, bleeding imprudence and recklessness into its fabric. [376] Imprudent underwriting practices of recent years demonstrate that there are certainly creditors within this class that are unworthy of the special treatment. Accordingly, judges should modify the super-priority treatment afforded to a residential mortgage claim by utilizing their authority to equitably subordinate the claim under section 510(c) of the Bankruptcy Code. [377] When a claim is equitably subordinated, its priority is diminished regarding its entitlement to distributions.

Congress made explicit a bankruptcy court's authority to equitably subordinate a claim when it replaced the Bankruptcy Act with the Bankruptcy Code in 1978. [378] By including this provision in section 510(c) for equitable subordination in the Bankruptcy Code, Congress intended for bankruptcy courts ***384** to utilize case law and the newly-enacted statutory provision to develop standards to equitably subordinate a pre-petition claim. [379] Under the principle of equitable subordination, an under-secured residential mortgage claim of a lender that has behaved egregiously in underwriting the loan could, in theory, have its claim crammed down, and any bifurcated unsecured portion of the pre-petition claim may be demoted to that of a general unsecured creditor despite section 1322(b)(2). [380] While equitable subordination itself will likely not solve the foreclosure crisis, it would likely serve to deter future abusive lending practices while providing fair and equitable relief to victimized debtors. [381]

The requirement that a creditor act in a manner deserving of the special treatment that its class is entitled to receive under the Code is implicit in the Code's equitable subordination provision, section 510(c). [382] This section of the Code allows a court to subordinate all or part of a creditor's claim to other claims using "principles of equitable subordination." [383] Also, according to section 510(c), pre-petition subordination agreements are enforceable. [384] The pertinent language in section 510 states that "the court may ... subordinate for purposes of distribution all or part of an allowed claim to all or part of another allowed claim[.]" [385] The statute further reads that the court may "order that any lien securing such a subordinated claim be transferred to the estate." [386] The legislative statement pertaining to section 510(c) states that "the court may, under principles of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim to all or part of another allowed claim .... *The fact that such a claim may be secured is of no consequence to the issue of subordination*." [387]

Both the legislative statement and section 510(c)(2) evidence Congress's intent to allow equitable subordination of a secured claim; section 510(c)(2) states that a court may "order that any lien securing such a subordinated claim be transferred to the estate." [388] Accordingly, under section 510(c), a court may equitably subordinate any claim, whether secured, unsecured, priority or administrative, to that of an inferior claim, and give such lesser treatment as the inferior claim would be entitled when warranted. This section of the Code is ***385** applicable to all cases filed under title 11 of the United States Code, including chapter 13, and therefore could render the special protections afforded residential mortgage lenders under section 1322(b)(2) inapplicable because of the demotion of such claim being equitably subordinated under section 510(c).

The ability to equitably subordinate a claim is not meant to reward a debtor, but rather to punish a pre-petition creditor that has behaved badly in conjunction with its claim and to prevent unfairness in the equity of distribution to all creditors in a bankruptcy case. [389] When one creditor's pre-petition conduct negatively affects the distribution received by the debtor's other creditors, an unjust result ensues. [390] In this fashion, courts have held that the equitable subordination of a claim is remedial in nature and not punitive. [391] A pre-petition claim is subordinated as a result of inequitable conduct on behalf of a lender and cancels any advantage to the lender who has not behaved fairly that the lender otherwise would have enjoyed over other claimants of the bankrupt's estate. [392] Thus, equitable subordination reflects the policy goal of bankruptcy of equitable distribution to all of the creditors of the estate. [393] This is to promote the maximum distribution to creditors of the estate; if a post-petition mortgage payment is either eliminated or reduced under equitable subordination, the debtor will be able to increase the distribution to all classes of claims, and, most importantly, to the general unsecured creditors who may have received little distribution otherwise. When a bankruptcy court finds that the distribution provisions that would ordinarily be mandated under the Code would be unfair to some of the creditors of the estate, the court should invoke its equitable powers to subordinate a claim to demote such claim to a status below those other ethically superior claims of the estate. [394]

Notwithstanding its applicability to all sections of the Bankruptcy Code, the theory of equitable subordination is rarely applied in the context of secured mortgage claims, and most typically espoused in chapter 11 cases against shareholders of a debtor corporation, the majority of which involve corporate insiders. [395] A common theory espoused under these circumstances is that a prepetition shareholder's loan to a corporation should be treated as an inferior claim of equity instead of a secured loan, deserving no distribution under the plan of reorganization unless all the superior claims, including those of the debtor's ***386** general unsecured creditors, are paid in full. [396] Just as creditor committees advocate for the demotion of a shareholder's loan status to that of a claim of equity, a chapter 13 debtor could advocate for the demotion of the status of a residential mortgagee's secured claim that is secured only by a principal residence, rendering the protections against modification of its claim inapplicable.

The criteria for courts to rely upon when determining if a claim should be demoted under the principle of equitable subordination was explored by the United States Court of Appeals for the Fifth Circuit in the case of *Benjamin v. Diamond* (*In re Mobile Steel Co.*). [397] In *Mobile Steel*, the court held that there are three conditions that necessarily must be satisfied before a claim can be equitably subordinated: "(i) [t]he claimant must have engaged in some type of inequitable conduct[;] (ii) [t]he misconduct must have resulted in injury to the creditors of the bankrupt or conferred an unfair advantage on the claimant[; and] (iii) [e]quitable subordination of the claim must not be inconsistent with the provision of the Bankruptcy Act." [398] These requirements have been followed by other districts. [399]

Importantly, the loan in *Mobile Steel* was given by officers and directors to the company; thus, there was an insider and fiduciary relationship between the parties. [400] In contrast, the relationship between a mortgage lender and a borrower is not that of a corporate insider. [401] The claim of a non-insider may not be subordinated as easily. [402] Usually the relationship between a creditor and a debtor is an arms-length transaction and the bank owes no fiduciary duty. [403] However, the banking industry over the past decade has been characterized more as a fiduciary relationship between a mortgagee and a mortgagor and not a mere arms-length transaction. In 1997, a district court in Florida held that a fiduciary relationship may arise between a mortgage lender and a homeowner when a "'bank knows or has reason to know that the customer is placing his trust and confidence in the bank and is relying on the bank so to counsel and inform ***387** him.'" [404] Also, special circumstances can give rise to a fiduciary relationship between a bank and a borrower, such as when a lender "takes on extra services for a customer, ... receives any greater economic benefit than from a typical transaction, or ... exercises extensive control." [405] In 1999, Congress passed the Gramm-Leach-Bliley Act, [406] which removed the previous prohibition of banking companies, financial companies, securities companies and insurance companies to offer a combination of services and consolidate. [407] Now, financial holding companies may engage in any activities that are financial in nature, specifically including such things as "financial, investment or economic advisory services" and "[i]ssuing or selling instruments representing interests in pools of assets.[]" [408] Because banks have now taken on this scope of financial advising, a fiduciary relationship has arguably developed between the bank and the borrower.

In determining what constitutes "inequitable conduct," the *Mobile Steel* court focused its analysis on undercapitalization, mismanagement, breach of fiduciary duties and abuse of fiduciary position. [409] Other districts applying the *Mobile Steel* three-prong test have expanded this conduct "to include fraud, illegality and the claimant's use of the debtor as an alter ego or mere instrumentality." [410] Evidence of undercapitalization of the debtor alone is not enough to subordinate a claim. [411]

When dealing with an equitable subordination claim involving a lender that is neither an insider nor a fiduciary, "'the level of pleading and proof is elevated: gross and egregious conduct will be required before a court can equitably subordinate a claim.'" [412] Most courts have required proof by the debtor of fraud, overreaching or spoliation in order to rise to the level of inequitable conduct. [413] However, "[s]ubstantial misconduct involving moral turpitude or a breach of misrepresentation where other creditors were deceived to their damage or gross ***388** misconduct amounting to overreaching is sufficient[]" to satisfy inequitable conduct justifying subordination under section 510(c). [414]

Very few cases have addressed equitable subordination claims in the context of non-insiders and non-fiduciaries. The recent noteworthy case that did equitably subordinate a non-insider claim is *In re Yellowstone Mountain Club*. [415] In this case--a chapter 11 bankruptcy--Credit Suisse reached out to the principal shareholder and owner of Yellowstone Mountain Club and offered him a new loan product of a much larger amount than previously available, akin to a home equity loan. [416] In its due diligence before lending the money, Credit Suisse did not request audited financial statements, and had its own new form of an appraisal method. [417] The court found that the loan product was being offered primarily because of the fees received for this type of loan. [418]

Applying the *Mobile Steel* test, the court determined that the creditor's actions did arise to "inequitable conduct" as "they shocked the conscience of the [c]ourt." [419] As for the second prong of the test, the court did not go into detail about how this inequitable conduct harmed other creditors. The court concluded that Credit Suisse had such complete disregard

for other subordinate creditors as it "lined its pockets on the backs of the unsecured creditors." [420] The third prong was not addressed at all. [421] The court ultimately concluded that Credit Suisse's lending practices were predatory and overreaching, and that it must subordinate Credit Suisse's lien to that of the allowed claims of unsecured creditors. [422] When a loan is predatory in nature, it may be a significant contributing factor that leads to the debtor's insolvency; in the end this prejudices other creditors of the bankrupt's estate. The home-lending practices of the early to mid-2000s are indicative of why courts should consider the remedy of equitable subordination. [423]

Conversely, in *In re Downer* [424] --a chapter 13 bankruptcy--the court considered a debtor's request to equitably subordinate a claim on the debtor's homestead as the creditor caused them to take out a seriously under-secured ***389** loan. [425] The debtors took out a mortgage on their homestead in the amount of $411,717.01, twice the amount of the home's value at purchase only six years prior. [426] Four years after taking out this loan, the debtors filed chapter 13 bankruptcy; they valued the property at $376,311.00. [427] The lender filed a secured proof of claim in the amount of $431,489.33, and subsequently the debtors filed a complaint to equitably subordinate the claim under section 510(c). [428] The court applied the *Mobile Steel* test. [429] Although it ultimately found that equitable subordination was not appropriate, this case provides further support that an equitable subordination argument can be viable in the context of a chapter 13 case.

Under the first prong of the test, the debtors argued that the lender's conduct caused them to make a loan that was seriously under-secured, but this was insufficient to prove inequitable conduct. [430] The debtors should have also alleged fraud and overreaching in material misrepresentations made by the lender, for example, or the lender taking advantage of its superior position over the debtors. [431] Absent such allegations, and in light of the Truth-in-Lending disclosures in the mortgage contract, improvident lending decisions were not enough. [432]

The debtors in *Downer* contended that their complaint met the second prong of the *Mobile Steel* test because the inequitable conduct on behalf of the lender would cause unsecured creditors to receive less under the chapter 13 plan than if the claim was not subordinated. [433] The court determined that this legal standard was insufficient; the record did not show whether the unsecured claims were made before or after the mortgage agreement. [434] If an unsecured creditor extended credit after the mortgage was made, it cannot claim that it was injured because it would have been on notice of the security interest of the prior lender. [435] Inasmuch, the debtors in this case did not make a sufficient showing that the loan resulted in injury to or conferred an unfair advantage on other creditors. [436]

***390** Finally, the court determined whether under the third prong of the test, "the subordination of the claim will not be inconsistent with the other provisions of the Bankruptcy Code." [437] The debtors sought to bifurcate the claim into secured and unsecured portions pursuant to section 506(a) and treat the unsecured portion as an allowed unsecured claim subject to bifurcation, whereby removing this portion from the protection of section 1322(b)(2). [438] But, the court held that this type of bifurcation is explicitly prohibited under section 1322(b)(2). [439] Bifurcation is prohibited even if the loan was under-secured at the time it was made, and the subordination provision contained in section 510(c) was not intended by Congress to be an exception to section 1322(b)(2). [440] An entirely different result would have likely occurred if the debtor argued that the entire claim should be subject to section 510(c) and the entire claim demoted to that of a general unsecured creditor. In this way a section 506(a) valuation would not have been necessary, as no portion of the claim would have been an allowed secured claim and section 1322(b)(2) would not have been implemented, as this section only deals with allowed secured claims. The claim would be subordinated to assign it to its appropriate class as the first step

and later other provisions of the Code would come into play to determine the appropriate treatment, including section 1322. Once the entire claim was demoted to a general unsecured claim, only the good faith test of section 1325(a)(4) would apply to the allowed claim.

It is possible that the enactment of the Bankruptcy Code has rendered the third factor moot. [441] The fact that section 1322(b)(2) prevents modification of a loan secured by a debtor's primary residence is arguably excepted with the enactment of section 510(c), as it explicitly allows a bankruptcy court to use equitable discretion and modify and subordinate a claim.

Depending on the equities involved in a particular case, a bankruptcy court may choose to have the residential mortgage loan of a chapter 13 debtor treated in the same fashion as an investment property of the debtor, whereby bifurcating the claim into a secured portion representing the current market value of the property and an unsecured claim representing the difference in the pre-petition amounts owed on such claim. This unsecured claim could then be lumped into the class of the debtor's general unsecured creditors, as is the general practice of the treatment of a secured claim that is bifurcated under sections 1322 and 506. In more egregious cases, the court could decide to disallow the entire secured claim, rather than bifurcate it, treating the entire claim as that of a general ***391** unsecured claim of the chapter 13 debtor. When a lender has demonstrated the most outrageous pre-petition underwriting conduct, a bankruptcy court could decide, in a chapter 13 case, to strike and disallow a debtor's secured residential mortgage claim in its entirety, likening its treatment to a claim of equity in a chapter 11 case by not providing at all for the claim.

Oftentimes the holder of a debt obligation is not the original lender. However, the present holder of the debt upon bankruptcy commencement may also be liable for the inequitable conduct of the original lender. Although no court has specifically addressed the issue of equitable subordination of a claim held by a subsequent purchaser or transferee, persuasive authority suggests that the subsequent purchaser's claim could still be subordinated because of the conduct of the original lender. [442] For example, it is well-settled law in Florida when dealing with the purchase of a note and mortgage by general assignment:

> As a general rule, the assignee of a nonnegotiable instrument takes it with all the rights of the assignor, and subject to all the equities and defenses of the debtor connected with or growing out of the obligation that the obligor had against the assignor at the time of the assignment. [443]

This means that the rights that the subsequent purchaser, assignee or transferee of the loan are no greater than the original lender's rights. [444] If the original holder of the note is not entitled to be paid because of some failure of performance on its part, then the subsequent assignee is not entitled to be paid either. [445] Similarly, in *Yellowstone*, the court found that the original lender, Credit Suisse, engaged in egregious lending practices and therefore subordinated the claim. [446] Even though this was a syndicated loan, and thus involved multiple subsequent purchasers of the loan, the court imputed the inequitable conduct to the subsequent lenders as well. [447]

Multiple opinions issued by the bankruptcy court in Enron's bankruptcy have also extended equitable subordination to subsequent parties other than the original creditor. [448] In the leading case, *In re Enron Corp.*, [449] the court stated ***392** that pursuant to *Mobile Steel*, "equitable subordination is warranted if its absence would frustrate the statutory purpose of advancing equitable distribution among creditors." [450] The court held that the priority of a claim in bankruptcy should not be impacted by a subsequent transfer, and that if a claim would be subject to equitable subordination in the hands of

the transferor, it should be the same with the transferee. [451] The transferee should not have any greater rights than the transferor had; the inherent risks are merely shifted. [452] Reading section 510(c) broadly, the purpose of the statute is to prohibit a creditor that has behaved inequitably to "hinder, dilute or in any way delay the distribution to other members of the injured creditor class by means of transferring its claims." [453] Therefore, transferring a claim does not shield the claim from equitable subordination, and the remedy of equitable subordination remains with the claim. [454] Although the *Enron* decision dealt with the transfer of bankruptcy claims post-petition, [455] and not the transfer or assignment of the actual note and mortgage of the original loan, the same principles should apply.

In the absence of any other adequate remedy at law, equitable principles intervene to prevent the unjust enrichment of the wrongdoer. Equitable subordination is a remedy in bankruptcy whose roots stem not only in the historical equitable powers conveyed to bankruptcy courts, but have also found a legal statutory basis since the Bankruptcy Code was enacted in 1978 with its inclusion of a statutory basis for the equitable subordination of a claim under section 510(c) of the Code. [456] Accordingly, both a statutory and equitable basis exist to offset the abusive home lending practices employed by certain residential home mortgage lenders, ensuring that they are not rewarded for such pre-petition conduct by availing themselves of the super-priority protections afforded under section 1322.

Until such time that Congress repeals the prohibition against the modification of a homestead mortgage, bankruptcy courts should use authority under section 510(c) of the Code to address predatory and abusive pre-petition practices on a case-by-case basis. [457] The widespread implementation of such treatment would send a clear message to those that were previously involved in abusive home mortgage lending practices, to those residential mortgage lenders that are contemplating making a present or future residential mortgage loan and ***393** to past, present and future lenders generally regarding the prudent underwriting practices that were and are expected of them. The immediate widespread implementation of equitable subordination principles would therefore serve not only to redress any lender's pre-petition wrongdoing, but would allow for equitable and fair distribution to all the creditors of a bankrupt's estate and act as a deterrent against future egregious lending and underwriting practices of any class of creditors.

V. DEBUNKING THE ARGUMENTS AGAINST CRAMDOWN AND CONCLUDING REMARKS

For more than half of chapter 13 debtors, their single biggest asset is their home. [458] Plan payments are structured around home mortgage payments to avoid foreclosure. Most times these debtors have delayed seeking legal help, and by the time they do so, their financial circumstances have deteriorated significantly and they face imminent foreclosure. [459] For such debtors, chapter 13 may be the only way to save their home. [460]

One of the primary reasons debtors file chapter 13 is to save their homes. [461] Recall that 183 of the 526 chapter 13 cases that were filed in Southern District of Florida in April 2009 sought to treat a homestead mortgage in the plan. [462] As this author's empirical study showed, if debtors could cramdown underwater homestead mortgages, the dismal rate of chapter 13 discharge would likely increase. Recall that 68.1% of chapter 13 plans proved effective when a subordinate mortgage was stripped off a debtor's homestead. [463] This effective rate was almost seven times greater than the 10.0% effective rate of proposed underwater homestead cures revealed in the sample set studied. [464]

Opponents of chapter 13 homestead cramdowns argue that it would "set the precedent that the rules of the game can change, retroactively, at any time." [465] "A contract you sign today can be invalidated tomorrow, not through the

normal ***394** course of bankruptcy litigation, but because Congress says so."[466] However, in *Radford* the Supreme Court held that Congress may discharge personal obligations and impair rights under contracts under its bankruptcy powers (although it could not take substantive rights to specific property).[467] Also, bankruptcy is traditionally a major mechanism for resolving financing distress.[468] Bankruptcy creates a legal process through which the market can work out the problems created when debtors have unmanageable debt burdens.[469] Had chapter 13 been enacted without the anti-modification provision "lenders probably would not have suffered as much, nor would underwriting have become as restrictive" as predicted.[470]

"The policy presumption behind bankruptcy's special protection for home mortgage lenders is that it enables these mortgage lenders to offer lower interest rates, and thus encourages [and promotes] home ownership."[471] Thus, in bankruptcy "the policy [of] special treatment of principal home mortgages ... is based on an economic assumption of market sensitivity to bankruptcy risk."[472] The Mortgage Bankers Association (MBA) has claimed that homestead cramdowns would result in an effective increase of 200 basis points in interest rates in homestead mortgages.[473] In October 2007, the MBA predicted that if homestead cramdowns were allowed, future homestead mortgage loans would require a 20% or greater down payment.[474] These MBA figures were derived from a comparison of the interest rate spread between mortgages on single-family homesteads and investment properties.[475] The assumption was that the entire spread was attributed to the lack of cramdown protection of investor ***395** properties.[476] However, investment properties include a mortgage expense that owner-occupier properties do not.[477] Also, vacancy, nonpayment of rent, and property damage serve as additional risk of default.[478]

The argument that chapter 13 homestead cramdowns would significantly increase residential mortgage borrowing costs is flawed. Mortgages on investment properties are not the only mortgages that can be modified in bankruptcy.[479] Mortgages on vacation homes and multifamily residences can be crammed down.[480] However, conforming mortgages on these properties are priced the same as homestead residences.[481] Only investment property mortgages are priced higher.[482] This means higher interest rates on investment properties must be attributed to non-bankruptcy risk factors.[483] "The MBA figure is thus the result of a cherry-picked comparison."[484] Likewise, there is a reasonable basis that "there is a zero percent chance that the MBA's 150 basis point claim is correct."[485] "All empirical and market observational data indicates that [the] MBA's claim of an effective 150-200 basis point increase" if cramdowns were allowed, is groundless.[486] Empirical studies have shown that mortgage markets are indifferent to bankruptcy-modification risk.[487]

Only undersecured creditors would be exposed to cramdown risk.[488] The majority of borrowers seeking homestead cramdown would already be in mortgage default.[489] Accordingly, any risk would arguably have been realized prior to any borrower filing for bankruptcy.[490]

***396** Leading up to the current crisis lenders imprudently relied on home appreciation, rather than home equity, when underwriting mortgages.[491] The anti-cramdown provision may have contributed to risky lending as lenders knew they would be protected from cramdown loss.[492] Thus, section 1322(b)(2) may have hampered the effectiveness of bankruptcy as a home-saving device.[493] This proposition is supported by this author's empirical findings, which revealed

that a mere 10.0% of chapter 13 plans that proposed a underwater mortgage cure proved effective in the sample set studied. [494]

Another argument made in opposition to homestead cramdowns is that it may encourage similarly-situated debtors to view bankruptcy as an alternative to refinancing. [495] These debtors, through cramdown, would re-draft a loan according to their desired specifications. [496] New homeowners would bear the burden of higher interest rates in the future if homestead cramdown was permitted. [497] This argument is flawed as debtors view bankruptcy as a forum of last resort. [498] Also, there are considerations limiting a debtor's eligibility for bankruptcy, including exemption and income limitations, which preclude the affluent from availing themselves of bankruptcy relief.

Opponents of cramdown state that mortgages, as interests in real property, are protected by the Fifth Amendment. [499] They cite to *United States v. Security Indutrial Bank*, [500] where the Supreme Court held that bankruptcy is subject to the prohibition against taking without compensation. [501] Thus, they argue that homestead cramdown impairs a secured creditor's rights in violation of the Fifth Amendment. [502] However, in *Wright v. Union Central Life Insurance Co.*, [503] the Supreme Court held that this Constitutional right extended only to the value of ***397** the collateral. [504] Opponents further argue that *Union Central*'s protected value entitled the secured creditor to cash and not a stripped-down mortgage lien. [505] This fails to recognize that section 1325(a)(5)(B)(ii) ensures that a secured creditor will receive a lien based on the collateral's value and distributions under the plan with a present value equal to the value of the collateral by section 506(a) allowed secured claim. [506]

"[B]ankruptcy courts should endeavor to leave the secured creditor as well off as if it received that amount of the crammed down secured claim in cash." [507] The plan's "interest rate should reflect what the creditor would have earned had it taken that cash and reinvested it in loans with terms [and risks] comparable" to the debtor's treatment under the plan. [508]

Opponents of homestead cramdowns argue that section 1325(a)(5)(B)(ii) requires a secured creditor receive the collateral's value and that it is impossible to sell a crammed down mortgage on the secondary market for its face amount. [509] It could be sold only for a severe discount and thus the mortgagee will not receive the value of the collateral. [510] This argument fails to recognize that there is an absence of a marketplace for 100% loan-to-value ratio loans and that "an 'investment band' technique can be employed to hypothesize the loan['s]" value. [511] A senior band is equal to the loan-to-value ratio for which there is a market and junior band(s) are equal to the remaining amount of the secured claim. [512] The plan would be required to pay a blended interest rate derived from these hypothetical loans. [513]

If the anti-cramdown provision remains unchanged, its purview should apply only to purchase money homestead mortgages. In *Nobelman*, the Supreme Court discussed that purchase money senior mortgages were protected by Congress in order to facilitate the flow of capital into the mortgage lending market. [514] Justice Stevens, in his concurring opinion in *Nobelman*, wrote that the Court's "literal reading of the text of the statute is faithful to the intent of Congress." [515] The intent to which Justice Stevens referred was "favorable treatment of residential mortgagees ... to encourage the flow of capital into the ***398** home lending market." [516] Because home equity loans do not serve this end, they should not be afforded the protection of modification exclusion. [517]

The soundness of this position is bolstered by the enactment of section 1322(c)(2) as part of the Bankruptcy Reform Act of 1994. This section creates an exception to the anti-modification provision for certain mortgages such as balloon payments and short-term mortgages. [518] Thus, the enactment of section 1322(c)(2) demonstrates that Congress did not intend the anti-modification provision to apply indiscriminately to any and all liens that are secured by a debtor's residential mortgage. The enactment of the Bankruptcy Reform Act of 1994 overruled the Supreme Court in *Nobelman* insofar as it applied to certain mortgages.

A cramdown of a mortgage mirrors the result that an undersecured mortgage lender would experience outside of bankruptcy if the debtor defaulted on the loan: a payment that is equal to the value of the collateral and a deficiency claim against the debtor for the remainder. [519] Sections 506 (a) and (d) convey this fairly straightforward and sound policy that "creditors should not receive better treatment [inside] bankruptcy than [they would receive] outside bankruptcy[.]" [520] A secured creditor, upon receiving bankruptcy stay relief would ultimately receive the value of its collateral and an unsecured claim for any deficiency. The anti-modification provision contained in section 1322 provides that 100% of an unmodified residential mortgage must be provided for should a debtor choose to keep the collateral. [521] This is akin to a homestead mortgage lender's claim being classified as one of the enumerated claims that are not subject to discharge under section 523.

Homestead cramdowns would address the problem of high, unaffordable payments on underwater properties, a problem central to the current crisis. [522] Chapter 13 debtors would be able "to reduce and stabilize interest rates on ... adjustable rate mortgages (ARMs)"--which are typically tied to above market rates--while factoring in a reasonable premium to account for lender risk thereby reducing payments. [523] This would decrease the effect of defaults resulting from "'payment shock' that occurs when ARMs adjust and dramatically increase the [amount of a] borrower's monthly payment amount." [524] Mortgages ***399** payments would be reduced if the principal balance of the secured claim was reduced to the current market value. [525]

In chapter 13, debtors must abide by a strict budget in a disciplined manner and obtain permission from the court before incurring new debt. [526] Allowing homestead cramdowns would create a strong incentive for debtors to complete their chapter 13 plans as any cramdown benefit would be lost otherwise. [527] This premise was demonstrated in this author's study, which showed that by lien stripping a wholly unsecured mortgage the effective rate of chapter 13 was 68.1% as compared to the 10.0% effective rate of an underwater mortgage cure. [528]

Homestead cramdown would address the issue of servicers unwilling to modify the terms of securitized loans for fear of being sued by the investors for breaching the servicing agreements. [529] If section 1322(b)(2) was amended to allow for homestead cramdown, investors could not sue servicers because the modification would be pursuant to court order. [530] If homestead cramdown was allowed, both the debtor and lender would be left in a better position than if the property fell into foreclosure. Lenders would benefit as an occupied home would preserve its value and have a greater chance of appreciating in value over a vacant home. [531] The debtor would save his or her home and the lender would receive an immediate income stream based on the current market value of the property. [532] The lender would save the huge costs associated with foreclosure. [533] The lender's interest would be further secured by any future appreciation of the property until the modified claim was paid in full. [534]

Allowing homestead cramdown could provide for payment of the modified balance over the balance of the loan term even if it is extended beyond the plan ***400** period. [535] Homestead cramdown would create a low-cost, effective, fair, and immediate remedy for resolving much of the foreclosure crisis. [536]

Foreclosures affect multiple stakeholders. American homeowners lose their homes. Mortgage lenders lose a portion of their investment as they typically collect forty-to-fifty percent of the loan. [537] Neighborhoods suffer when foreclosed homes deteriorate, imposing costs on local governments and a deteriorating tax base. Security markets suffer downward pressure on instruments exposed by securitized mortgages. Foreclosures also push down real estate prices.

Likely less than one percent of all first-lien mortgages end up in bankruptcy. [538] "Since at least 1993, foreclosure rates have averaged 1.14% of all outstanding mortgages, with a low of .86% and a high of 1.69%." [539] "Many mortgage delinquent homeowners never file for bankruptcy, however, although some do file before foreclosure proceedings commence." [540] Nonetheless, "it is a reasonable assumption that a smaller percentage of mortgages end up in bankruptcy than end up in foreclosure." [541] Mortgage markets are indifferent to cramdowns because "the scope and the magnitude of the potential loss is small and might often be less than [that] incurred in foreclosure[,]" including the costs of the process and the likely lower price the lender will realize at a foreclosure sale. [542] In addition, of the mortgages that end up in bankruptcy, many do not end up in chapter 13. Of the chapter 13 cases that are filed where a debtor's principal residence is secured by a subprime mortgage, more than half are ultimately dismissed for different reasons. [543] Thus, the premise that mortgage markets are sensitive to bankruptcy modification risk is unfounded or exaggerated.

Under an unlimited cramdown regime "only a limited subset of the already highly limited universe of mortgages that end up in Chapter 13 would be subject to [cramdown]." [544] The mortgages that would be subject to cramdown would ***401** see average losses limited to $13,172.23, according to 2001 CBP data. [545] A disproportionate share of the losses would be borne by junior mortgages. [546]

The banking industry has never presented a scintilla of evidence to indicate that permitting homestead cramdowns would adversely affect the cost or availability of mortgage credit. [547] Instead, it has made simplistic arguments in opposition to cramdown. [548] Professor Adam Levitin has conducted the only empirical work regarding the effect of homestead cramdown on cost and availability, finding both insensitive to bankruptcy cramdown risk. [549]

The failure of mortgage lenders to voluntarily modify mortgages may renew the push to allow homestead cramdown. [550] According to Barney Frank (D-Mass), former chairman of the House Financial Services Committee, "[t]he best lobbyists we have for getting bankruptcy legislation passed are the servicers who are not doing a very good job of getting mortgages modified." [551]

Until negative equity is addressed there will continue to be more foreclosures filed, which in turn will beget more foreclosures and create a death spiral in the housing market. [552] None of the programs implemented to date adequately address the negative equity issue. [553] Of the 185,156 loan modifications implemented in the first quarter of 2009, only 3,389, or 1.8%, involved the reduction of the principal balance of the loans, and of these, only four of these loans were securitized, whereas the balance were portfolio loans. [554] As of December 2011, only about 40,000 loans have had their principal amounts reduced. [555] Additionally, 45.8% of the loans that were modified in 2009 did not ***402** result in

the reduction of the monthly payment amounts due from the borrower, and in fact, many actually resulted in higher payments. [556]

By the time the mortgage crisis runs its course as many as one-in-five homes will fall into foreclosure. [557] The mortgage industry, private lenders and two presidential administrations have made various efforts to quell the crisis with little success. [558] A Credit Suisse research report projected that allowing homestead modification in bankruptcy would reduce the foreclosures by twenty percent. [559] The United States has an existing system of bankruptcy courts unscathed by the nearly doubling of the number of bankruptcy filings in response to the foreclosure crisis. [560] Bankruptcy judges have expressed little reservation about the possible increase to their workload if homestead cramdown was permitted. [561] Bankruptcy has a self-supporting system of judges, clerks and courthouses in place, abating the need to create a new and costly bureaucracy to administer modifications. [562] Currently, the programs have shifted much of the cost of modification to the taxpayer by incentivizing lenders to modify. Allowing homestead cramdown would shift much of the costs to the lenders that are the root cause of the financial collapse.

Bankruptcy courts routinely work with experienced valuation experts that have the requisite experience, education, knowledge and license to take on the complex task of valuing properties for modification purposes. [563] Bankruptcy judges do not wield unfettered powers to determine the value of properties and re-write contracts; rather they are constrained by relevant case law precedent and legal statutes, which are applied uniformly and in a predictable fashion, subject to appellate oversight.

Any moral hazard that opponents of homestead cramdown argue would result is reduced or eliminated by the fact that chapter 13 is a "pay to play" system. [564] There are extreme costs and hardships debtors sustain in seeing chapter 13 through. [565] The Mortgage Bankers Association acknowledged these costs in the following press release:

> ***403** There are very real and severe consequences for consumers who declare bankruptcy. Bankruptcy is a long, arduous, very public and expensive process, costing thousands of dollars in legal costs. Even when people file for bankruptcy, almost two thirds of them are unable to fulfill the terms of their repayment plans. Filing bankruptcy will allow a federally appointed trustee to scrutinize the consumers' every expenditure. Additionally, bankruptcy stays on a consumers' [sic] credit report for 10 years, making it difficult to acquire future credit, buy a home, car or insurance and in some cases, even obtain employment. [566]

A chapter 13 debtor must agree to a budgeted plan supervised by a court-appointed trustee, must begin to make payments almost immediately, and must commit substantial resources to the plan for a three-to-five year period. [567] Chapter 13 debtors do not make the decision to file for bankruptcy lightly, and must exercise discipline to complete their plans. [568]

Allowing homestead mortgage modifications in bankruptcy would require lenders to bear some of the costs borne of their irresponsible lending practices. [569] Mortgage lenders will continue to escape the consequences of their folly if borrowers and taxpayers continue to bear the cost of mortgage modifications. [570] These lenders will not learn that unsavory behavior has downside risks unless they are held accountable. [571] At the very least, section 1322(b)(2) should be amended to allow for homestead cramdown if the mortgage lender failed to conduct due diligence in approving the loan, participated in fraud or deceit, and/or exercised predatory lending practices.

According to Sen. Dick Durbin, "[t]he banks that are too big to fail are saying that 8 million Americans facing foreclosure are too little to count [.]" [572] The current state of the housing market and overall economy is recognizably bleak. Reform has been attempted from multiple ends but none has yet been successful. Recently, the International Monetary Fund issued a concluding statement on the fiscal recovery of the United States. [573] Overall, it concluded ***404** that U.S. recovery is still tepid and faces multiple downside risks. [574] Despite certain progress and policy implementations, much vulnerability remains and appropriate resources should be devoted to help. [575] As stated in the report, Congress should give consideration to "allowing mortgages on principal residences to be modified in personal bankruptcy without secured creditors' consent[.]" [576] This further supports that amending section 1322(b)(2) to allow modification of a debtor's principal residence is necessary.

The anti-modification provision was enacted in 1978 to afford protections to a mid-twentieth century financing model that is no longer in existence today. [577] Presently, this provision of the Bankruptcy Code is misused by residential mortgage lenders, servicers and investors to defend the terms of mortgage loans that were originated with terms that were unimaginable in 1978. [578]

Nationwide, 6.5 million loans, or 12.7% of all outstanding residential loans fell into foreclosure by the end of 2012. [579] It is clear that the record number of foreclosures that have materialized since late 2006 is today a mammoth threat to the preservation of one's ownership of a home, which is the cornerstone of American life. Large numbers of American families are unable to afford their current homes because of the skyrocketing rate of unemployment, which itself is directly manifested from the irresponsible lending practices employed by the mortgage banking industry. Although a debtor who seeks to file a chapter 13 bankruptcy to save his home from foreclosure may formulate a repayment plan to address his arrearages, this relief does not address the ultimate affordability issue. The repeal of the prohibition on modifying a mortgage claim, secured only by a debtor's principal residence in bankruptcy, would improve the effectiveness of chapter 13 bankruptcy as a home-saving process. This was demonstrated by the dramatic increase in effectiveness of chapter 13 as a home-saving device when the total amount owed on a debtor's principal residence decreased. [580] In the interim, bankruptcy practitioners should study their distressed homeowners' cases carefully in order to determine whether a colorable basis exists to propose chapter 13 principal residence mortgage cramdowns.

Amending the Bankruptcy Code to allow for cramdown of a debtor's principal residence will provide the most comprehensive and cost effective ***405** system to assist in resolving this nation's mortgage crisis. A bankruptcy approach would benefit the borrower, the residential mortgage lender, the United States taxpayer, local governments and all American homeowners throughout the country. Borrowers would benefit from the increased leverage that they would gain, pre-petition, to encourage their lenders to negotiate in good faith. Lenders would benefit from a borrower choosing to avail himself of cramdown over either the debtor surrendering the property in a chapter 7 bankruptcy, or alternatively, having to see a foreclosure through to conclusion. This is because a lender in a chapter 13 case would be certain to have its claim secured by the full current market value of the property and receive the net present value of the forthcoming cash flows that are based on the retail value of its collateral, rather than the diminished foreclosure value of the property at some obscure future date. Additionally, lenders would benefit by a borrower's renewed sense of permanency in the residence, which would further encourage the borrower to invest in the continuing improvement and maintenance of the property, which serves as the lender's security for its claim. Borrowers in turn would benefit from the discipline needed to stick to the confines of a court-ordered budget required in chapter 13.

The American taxpayer would benefit from cramdown by not having to bear the cost of incentivizing lenders that made poor underwriting decisions to modify underperforming residential mortgage loans. Local governments throughout this country would benefit from increased property tax revenue when higher property values result from fewer foreclosures that result from more Americans turning to chapter 13 as an effective home-saving process. While a foreclosure sale is recorded in the public records as a sale thereby affecting the values of comparable properties in the area, any reduction in the amount owed to a residential mortgage lender resulting from cramdown would not be reflected in the public records as a sale and would not diminish the value of neighbors' homes for purposes of sale or refinance of the neighbors' property.

By instituting cramdown, Congress can protect the full benefit and meaning of a debtor's discharge in bankruptcy. The bankruptcy system in the United States exists to serve the fair and equal distribution of the estate's assets among its creditors and to assist the unfortunate debtor by giving him a fresh start in life. [581] Without allowing for cramdown of a debtor's primary residence in a chapter 13 case it will continue to be difficult for many debtors to start anew after losing their homes.

Footnotes

1 This Article is an abbreviated version of my J.S.D. dissertation from the Thomas Jefferson School of Law. I would like to acknowledge and give thanks to the extraordinary encouragement and support given me in conjunction with my J.S.D. dissertation and this Article by my J.S.D. supervisor, Professor Katherine Porter of the University of California Irvine School of Law. I would also like to thank Dean Arnold Rosenberg of the California Western School of Law for his initial supervision of my dissertation, as well as Professor May Jo Wiggins of the University of San Diego School of Law, and Professor Jean Braucher of the University of Arizona School of Law who served as my J.S.D evaluator along with Professor Katherine Porter. I would also like to thank Dr. Robert Munro of the Thomas Jefferson School of Law and Dean William Byrnes of the Thomas Jefferson School of Law for their unwavering support of my pursing the J.S.D. degree. A special thank you is also in order for Professor Jeffrey Davis of the University of Florida School of Law and Professor Jason Kilborn of the John Marshall School of Law for their valuable assistance.

2 *See* 11 U.S.C. § 1322(b)(2) (2012) (“[T]he plan may ... modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence ....”).

3 *See* Adam J. Levitin & Joshua Goodman, *The Effect of Bankruptcy Strip-Down on Mortgage Markets* 2 (Georgetown Univ. Law Ctr., Research Paper No. 1087816, 2008), *available at* http://ssrn.com/abstract=1087816 (citing 11 U.S.C. § 506 (2012)).

4 *See id.* at 26 (“Strip-down bifurcates a mortgage lender's bankruptcy claim into a secured claim for the value of the collateral and an unsecured claim for the deficiency.”).

5 *See id.* at 2 (stating chapter 13 creditors are guaranteed to receive value of secured claim, but unsecured creditors are entitled to significantly less compensation).

6 *See id.* at 3 (stating debtors can modify unsecured second mortgages and loans on other types of property but cannot modify loans secured solely by debtor's primary residence).

7 508 U.S. 324 (1993).

8 *See id.* at 327 n.2 (noting four circuits had allowed bifurcation).

9 *See, e.g.*, Bellamy v. Fed. Home Loan Mortg. Corp. (*In re* Bellamy), 962 F.2d 176, 178 (2d Cir. 1992) (“[A]n allowed claim secured by a lien is ‘a secured claim’ only up to the market value of the property on which the lien is fixed, and is an unsecured claim for the balance owed above that market value.”).

10 *See Nobelman*, 508 U.S. at 332.

11 *Cf.* Levitin & Goodman, *supra* note 3, at 41 ("There is no empirical evidence that supports a conclusion that permitting either strip-down or other forms of modification of principal home mortgage loans in bankruptcy would have more than a minor impact on mortgage interest rates or home ownership rates.").

12 *See In re* Bradsher, 427 B.R. 386, 391-92 (Bankr. M.D.N.C. 2010) (holding lender was "outside the protection from modification provided under section 1322(b)(2)" because the debt was "not secured solely by ... Debtor's principal residence").

13 *See, e.g., id.* (holding lender was not protected by section 1332(b)(2) because loan was secured by escrow account in addition to debtor's principal residence); *see also* Juliet M. Moringiello, *Mortgage Modification, Equitable Subordination, and the Honest but Unfortunate Creditor*, 79 FORDHAM L. REV. 1599, 1633 (2011) (arguing courts could, on a case by case basis, remove special priority given to home mortgage creditors when their lending practices were abusive).

14 *See* Moringiello, *supra* note 13, at 1603-04 ("A debtor who wishes to keep her home in bankruptcy would likely file under Chapter 13 because generally a Chapter 13 debtor keeps all of her property and pays her creditors some portion of their claims ....").

15 *See* David T. Newton, Note, *Widespread Panic: Why the Mortgage Lending Industry Can Calm Down About Amending Cramdown*, 98 KY. L.J. 155, 155 (2009).

16 *See* Nobelman v. Am. Sav. Bank, 508 U.S. 324, 331 (1993) (stating debtors cannot modify unsecured portion of debt without modifying secured portion, which would require interest payments to be recalculated).

17 *See* 11 U.S.C. § 1322(b)(2) (2012).

18 *See* Levitin & Goodman, *supra* note 3, at 2-3 (listing types of property which can be used in modifiable loans).

19 *Id.* at 26.

20 *See* Zimmer v. PSB Lending Corp. (*In re* Zimmer), 313 F.3d 1220, 1221 (9th Cir. 2002) (upholding debtor's ability to strip-off wholly unsecured junior mortgage in chapter 13 cases); *accord* Lane v. W. Interstate Bancorp (*In re* Lane), 280 F.3d 663, 664 (6th Cir. 2002); McDonald v. Master Fin., Inc. (*In re* McDonald), 205 F.3d 606, 615 (3d Cir. 2000); Bartee v. Tara Colony Homeowners Ass'n (*In re* Bartee), 212 F.3d 277, 280 (5th Cir. 2000); Tanner v. FirstPlus Fin., Inc. (*In re* Tanner), 217 F.3d 1357, 1357 (11th Cir. 2000).

21 *See* 11 U.S.C. § 506(a) (2012).

22 *See* Levitin & Goodman, *supra* note 3, at 2.

23 210 B.R. 157 (Bankr. D. Minn. 1997).

24 *Id.* at 159.

25 *See* 11 U.S.C. § 506(a)(1).

26 11 U.S.C. § 1325(a)(5).

27 *See* ELIZABETH WARREN & JAY LAWRENCE WESTBROOK, THE LAW OF DEBTORS AND CREDITORS 284 (6th ed. 2008) (stating secured claim must be paid in full, with interest).

28 *Id.*

29 *Id.*

30 *See* 11 U.S.C. § 506(a), (d). The pertinent language in section 506 states:

(a)(1) An allowed claim of a creditor secured by a lien on property ... is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property, or to the extent of the amount subject to setoff, as the case may be, and is an unsecured claim to the extent that the value of such creditor's interest or the amount so subject to setoff is less than the amount of such allowed claim.
(d) To the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void, unless--
(1) such claim was disallowed only under section 502(b)(5) ... of this title; or
(2) such claim is not an allowed secured claim due only to the failure of any entity to file a proof of such claim under section 501 of this title.
Id.

31 WARREN & WESTBROOK, *supra* note 27, at 225.

32 *Id.* at 284.

33 David G. Epstein, *Don't Go and Do Something Rash About Cram Down Interest Rates*, 49 ALA. L. REV. 435, 464 (1998).

34 520 U.S. 953 (1997).

35 *See id.* at 955.

36 *See id.* at 964-65 (finding that "[s]ection 506(a) calls for the value the property possesses in light of the 'disposition or use' in fact 'proposed,' not the various dispositions or uses that might have been proposed").

37 *Id.* at 956.

38 *Id.* at 964-65.

39 Stacy L. Molison, Note, *A Look at Disparate Approaches to Valuation Under Section 506 and its Relationship to Section 1325*, 15 AM. BANKR. INST. L. REV. 659, 662 (2007).

40 *Id.*

41 *See* 11 U.S.C. § 1325(a)(5) (2012).

42 *See id.* The pertinent language in section 1325(a)(5) is:
(a) Except as provided in subsection (b), the court shall confirm a plan if ... (5) with respect to each allowed secured claim provided for by the plan ... (A) the holder of such claim has accepted the plan; (B)(i) the plan provides that (I) the holder of such claim retain the lien securing such claim until the earlier of the payment of the underlying debt ... or discharge under § 1328; and (II) if the case under this chapter is dismissed or converted without completion of the plan, such lien shall also be retained by such holder to the extent recognized by applicable non-bankruptcy law; (ii) the value, as of the effective date of the plan, of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim; and (iii) if property to be distributed ... is in the form of periodic payments, such payments shall be in equal monthly amounts; and
(iii) if ... the holder of the claim is secured by personal property, the amount of such payments shall not be less than an amount sufficient to provide to the holder of such claim adequate protection during the period of the plan; or (C) the debtor surrenders the property securing such claim to such holder.
Id.

43 *See In re* Hudson, 260 B.R. 421, 428 (Bankr. W.D. Mich. 2001) (citations omitted) (stating after debtors' plan was confirmed, secured creditor could not demand greater payment on secured portion of its claim).

44 *See id.* (explaining *res judicata* leads to binding effect of confirmed chapter 13 plans).

45 *See id.*

46 *See id.* at 429 (showing chapter 13 allows certain protections for debtor's "principal residence").

47 *See, e.g.*, Bellamy v. Fed. Home Loan Mortg. Corp. (*In re* Bellamy), 962 F.2d 176, 185 (2d Cir. 1992) (finding chapter 13 debtor may reinstate residential mortgage coming due beyond life of plan in its stripped down form).

48 *See In re* Nation, 352 B.R. 656, 666 (Bankr. E.D. Tenn. 2006); *In re* Strober, 136 B.R. 614, 623 (Bankr. E.D.N.Y. 1992) (assessing debtor's need for time beyond life of plan to pay off mortgage).

49 *See* Order Denying Debtor's Motion to Value and Denying Confirmation of First Amended Chapter 13 Plan at 5, *In re* Jozwiak, No. 11-13579-JKO (Bankr. S.D. Fla. Jul. 11, 2011) (denying debtor's motion); *In re* Elibo, 447 B.R. 359, 364 (Bankr. S.D. Fla. 2011) (holding if debtor wished to pay secured claim over more than five years, debtor must cure defaults within a reasonable time and maintain pre-petition payments at original interest rate until claim was paid in full); *In re* Valdes, No. 09-26712, 2010 WL 3956814, at *3 (Bankr. S.D. Fla. Oct. 4, 2010) (finding debtor's proposed cramdown would violate Bankruptcy Code)r; *In re* Santiago, No. 08-15360, 2009 WL 3515705, at *3 (Bankr. S.D. Fla. Oct. 29, 2009) (showing debtor may modify payment terms, in which case all payments must be completed during plan).

50 541 U.S. 465, 501, n.10 (2004) (incorporating two percent over prime rate into calculations of payment due on secured claim); Order Denying Debtor's Motion to Value and Denying Confirmation of First Amended Chapter 13 Plan, *supra* note 48, at 5.

51 There are two methods used to lien-strip a wholly unsecured mortgage in a chapter 13 case. The first method is for the chapter 13 debtor to file an adversary proceeding pursuant to Federal Rule of Bankruptcy Procedure 7001(2). The second method is to set the matter as a contested matter by motion. *See* David Lloyd & Ariane Holtschlag, *Chapter 13 Strip-Off of Junior Mortgages: Not Whether, but How under Current Law*, 28 AM. BANKR. INST. J. 12, 12 (July-Aug. 2009). The majority view is that the filing of an adversary proceeding is not necessary, and in most jurisdictions, the issue of whether a wholly unsecured mortgage can be lien-stripped in a c hapter 13 case may be raised and settled as a contested matter during motion practice. *See In re* Millspaugh, 302 B.R. 90, 97 (Bankr. D. Idaho 2003) (citing cases in which courts have concluded adversary proceeding is not required to strip off wholly unsecured mortgage from residence).

52 *See, e.g., In re* Millspaugh, 302 B.R. at 103 (allowing debtor to lien-strip second, wholly unsecured mortgage).

53 *See* Tanner v. FirstPlus Fin., Inc. (*In re* Tanner), 217 F.3d 1357, 1360 (11th Cir. 2000) ("Any claim that is wholly unsecured, however, would not be protected from modification under section 1322(b)(2).").

54 *See* First Mariner Bank v. Johnson, 411 B.R. 221, 224-25 (D. Md. 2009) (explaining courts have applied anti-modification provisions only to first or purchase-money mortgages).

55 *Id.* at 224 ("Justice Thomas' analysis in *Nobelman* clearly indicated that the proper starting point in this analysis is the valuation in § 506(a), *not* the exception in § 1322(b)(2).") (emphasis in original).

56 *See* Pond v. Farm Specialist Realty (*In re* Pond), 252 F. 3d 122, 125-26 (2d Cir. 2001) (holding that (1) if no portion of secured claim of mortgage loan is secured by value of collateral, *Nobelman* would not apply because no portion of the debt is secured; and (2) *Nobelman*'s "anti-modification exception is only triggered where there is sufficient value in the underlying collateral to cover some portion of a the creditor's claim").

57 *See First Mariner Bank*, 411 B.R. at 224 (stating *Nobelman* narrowed interpretation of section 1322(b)(2)).

58 *See id.* (explaining if lienholder's interest in collateral has economic value, then it is secured claim).

59 *See id.* (demonstrating unsecured claims may be modified by chapter 13 plan, pursuant to section 1322(b)(2)).

60 Moringiello, *supra* note 13 at 1605.

61 Susan Jill Rice, *Lien Stripping: An Ever Expanding Remedy?,* Amer. Bankr. Inst. Detroit Consumer Bankr. Conference 489, 491-92 (2010) ("Congress enacted the Bankruptcy Reform Act of 1978 ... against the 'pre-Code background that allowed debtors to strip a creditor's lien' in reorganization cases.").

62 *See* Moringiello, *supra* note 13, at 1606 (explaining prior to *Nobelman*, it was unclear prohibition on modifying home mortgages prohibited cramdown).

63 *See* Nobelman v. Am. Sav. Bank, 508 U.S. 324, 325-26 (1993).

64 Robert M. Zinman & Novica Petrovski, *The Home Mortgage and Chapter 13: An Essay on Unintended Consequences*, 17 AM. BANKR. INST. L. REV. 133, 135 (2009).

65 *See generally* JOHN C. MURRAY & BAXTER DUNAWAY, 3 THE LAW OF DISTRESSED REAL ESTATE 30?68 (2009); *see also* Zinman & Petrovski, *supra* note 64, at 135 (describing how plan confirmation under former chapter XIII of Bankruptcy Act required unanimous approval of secured creditors whose claims were addressed in plan).

66 *See* Jack Friedman, *What Courts Do to Secured Creditors in Chapter 11 Cram Down,* 14 CARDOZO L. REV. 1495, 1496 n.1 (1993).

67 *Id.*

68 *See* Richard E. Coulson, *Consumer Abuse of Bankruptcy: An Evolving Philosophy of Debtor Qualification for Bankruptcy Discharge*, 62 ALB. L. REV. 467, 493 (1998).

69 From the creation of chapter 13 by the Chandler Act in 1938 until the enactment of the Bankruptcy Code in 1978, debtors could modify a claim on their principal residence.

70 *See* H.R. 8200, 95th Cong. § 1322 (1977); S. 2266, 95th Cong. § 1322 (1977).

71 *See* Moringiello, *supra* note 13, at 1603.

72 *See Growing Mortgage Foreclosure Crisis: Identifying Solutions and Dispelling Myths: Hearing Before the Subcomm. on Commercial and Admin. Law of the H. Comm. on the Judiciary*, 110th Cong. 80 (2008) (statement of David G. Kittle, Chairman-Elect, Mortgage Bankers Association).

73 11 U.S.C. § 1322(b)(2) (2012). The pertinent language in section 1322(b)(2) is:
Contents of plan ... (b) Subject to subsections (a) and (c) of this section, the plan may--... (2) modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims.
Id.

74 *See* Susan E. Hauser, *Cutting the Gordian Knot: The Case for Allowing Modification of Home Mortgages in Bankruptcy*, 5 J. BUS. & TECH. L. 207, 218-19 n.79 (2010). These objectives stated in affirmation of enacting cramdown as it pertains to claims in general are contradictory to the legislative history that was used to justify the exemption of home mortgages under section 1322(b)(2), which stated that cramdowns would have a chilling effect on the free flow of capital in the mortgage markets.

75 *See* Adam J. Levitin, *Resolving the Foreclosure Crisis: Modification of Mortgages in Bankruptcy*, 2 WIS. L. REV. 565, 573 n.26 (2009) [hereinafter *Resolving the Foreclosure Crisis*].

76 *See id.*

77 *Id.*

78 *Hearings on S. 2266 and H.R. 8200 Before the Subcomm. on Improvements in Judicial Mach. of the Comm. on the Judiciary*, 95th Cong. 714-15 (1977) (statements of Edward J. Kulik, Senior Vice President, Real Estate Division, Massachusetts Mutual Life Insurance Co., accompanied by Robert E. O'Malley, Attorney, Covington Burling); *see Resolving the Foreclosure Crisis, supra* note 74, at 574; *see also* discussion in Part VI *infra* at 66-67 (discussing how home mortgage credit is affected by *Nobelman* and through enactment of section 1322(c)).

79 *See* Nina Liao, Note, *Cramming Down the Housing Crisis: Amending 11 U.S.C. § 1322(b) to Protect Homeowners and Create a Sustainable Bankruptcy System*, 93 MINN. L. REV. 2240, 2250 (2009) (presenting example of homeowner whose mortage could not be modified by judge in chapter 13 filing).

80 *See id.* (noting Supreme Court's conclusion in *Nobelman* that section 1322(b)(2) prohibits debtor from using section 506(a) to bifurcate and reduce undersecured homestead mortgage).

81 *See id.*

82 *See In re* Frost, 96 B.R. 804, 807 (Bankr. S.D. Ohio 1989) (noting if Congress intended distinction, then qualifiers would be included).

83 *See In re* Mitchell, 125 B.R. 5, 8 (Bankr. D.N.H. 1991).

84 *See* Liao, *supra* note 79, at 2250.

85 508 U.S. 324 (1993).

86 *See id.* at 332.

87 *Id.* at 328-29.

88 *Id.* at 329.

89 *Id.*

90 *Id.*

91 *Id.* at 329-30. The Supreme Court arrived at this conclusion by stating that it would be impossible to reduce the petitioners' outstanding mortgage principal to the current market value of the property without modifying the contractual rights of the mortgagee under state law with regard to monthly payments, interest rates and repayment terms

92 *See id.* at 328.

93 WARREN & WESTBROOK, *supra* note 27, at 301.

94 *See id.*

95 *Id.* at 300-01 (describing home-saving processes in absence of cramdown).

96 *See* description of lien-stripping, *supra* Part II(A).

97 Mark S. Scarberry & Scott M. Reddie, *Home Mortgage Strip Down in Chapter 13 Bankruptcy: A Contextual Approach To Sections 1322(b)(2) and (b)(5)*, 20 PEPP. L. REV. 425, 428-29 (1993) (discussing nature of mortage cures).

98 Although only 10.1%, or 26 of the 257 chapter 13 cases that were filed in April 2007 reflected homestead properties where loan-to-value ratios exceeded 100%, 55.3%, or 291 of the 526 chapter 13 cases that were filed in April 2009 reflected homestead properties where the loan-to-value ratios exceeded 100%. As I am a local bankruptcy practitioner in the Southern District of Florida and I know from first-hand experience how the mortgage market in this area has been severely adversely affected, I thought it appropriate to conduct my study here. Of course while the Southern District of Florida is not necessarily reflective of the nation, I believe that the behavior trends and effective rates of the subsamples discussed to be illustrative of my hypothesis. Also, a limitation of this study is that I only examined the month of April, which may not be indicative of the yearly trend. However, research demonstrates that there are not seasonal effects in chapter 13 filings. *See, e.g.*, Ronald J. Mann & Katherine Porter, *Saving up for Bankruptcy*, 98 GEO. L.J. 289, 318 (2010) (observing trends in filing data).

99 The study contemplated comparing the status of underwater homestead mortgage cures with non-homestead mortgage cramdowns. However, only nine cases sought cramdowns, and because there is often a difference in the sophistication and income levels of debtors owning investment properties compared to investors that do not and because the study focused on homestead properties, this sub-sample was not incorporated.

100 PACER is an acronym for Public Access to Court Electronic Records, the online system for accessing federal court records.

101 *But see* Joshua L. Boehm, Note, *Chapter 13 Debtors' Home Loss in the Foreclosure Crisis*, 3 HARV. BUS. L. REV. 185, 186 (2013) (finding three factors strongly predicted eventual home loss: whether debtor was in foreclosure at time of filing bankruptcy, higher loan-to-value (LTV) ratios and higher mortgage-to-income (MTI) ratios). Mr. Boehm's study found that as these variables increased, the probability that a debtor would lose his or her home increased substantially. *Id.* at 187.

102 A limitation to these findings, as well as to all the sample sets analyzed, is that debtors may have allowed their chapter 13 cases to be dismissed in order to more freely participate in lenders' loss mitigation options. These options include, but are not necessarily limited to, the voluntary modification of a mortgage, the acceptance of a deed in lieu of foreclosure, or participation in a short sale of the subject property. *See* Katherine Porter, *The Pretend Solution: An Empirical Study of Bankruptcy Outcomes*, 90 TEX. L. REV. 103, 146 (2011) (revealing in her study that over one-third of chapter 13 bankruptcy filers polled stated that they found a better solution outside of bankruptcy, often by negotiating loan modifications with their mortgage lenders). In this study, whether cases were voluntarily dismissed by debtors either affirmatively or by purposefully stopping to make payments in order to avail themselves of non-bankruptcy loss mitigation options cannot be gleaned by an analysis of the bankruptcy docket and filings.

103 A limitation of these findings that indicate that non-underwater homestead cures are largely ineffective is the relative small size of the sample studied. However, only 17 cases that were filed in the Southern District of Florida in April 2009 fit into this subcategory's case code.

104 Even though the vast majority of the cases that were proposing treatment of an underwater homestead in the plan proposed to lien-strip subordinate mortgages (74.3% = 63.4% lien-strip + 10.9% lien-strip in conjunction with mortgage cure), it is likely that many of the remaining cases (25.7%) that had subordinate mortgages encumbering their homes would have also proposed a lien-strip had it not been for an equity cushion securing some portion of the mortgage interest, thereby prohibiting bankruptcy court-ordered modification under 11 U.S.C. § 1322(b)(2).

105 *See supra* Part I(A).

106 *See id.*

107 *See* Scarberry & Reddie, *supra* note 97, at 430 (concluding strip down of home mortgages is only permissible if "(1) the undersecured mortgagee has taken other collateral for the loan in addition to the home, so that the 'other than' clause does not apply, and (2) the Chapter 13 plan does not utilize § 1322(b)(5) to cure a mortgage default").

108 *See, e.g., In re* Jackson, 136 B.R. 797, 800 (Bankr. N.D. Ill. 1992) (finding mortgagee's secured claim on debtor's residence outside protection of § 1332(b) where, based on language pledging rents and issue from property as additional security, claims of mortgagee were secured by property in addition to debtor's principal residence).

109 11 U.S.C. § 1327(a) (2012).

110 *See id.*

111 *See id.*; 8 COLLIER ON BANKRUPTCY ¶ 1327.02 (Alan N. Resnick & Henry J. Sommer eds., 16th ed. 2011).

112 11 U.S.C. § 1325(a)(5)(A).

113 11 U.S.C. § 506(a).

114 11 U.S.C. § 1325(a)(5)(A).

115 *See* § 506(a).

116 *See id.*

117 *See id.*

118 Nobelman v. Am. Sav. Bank, 508 U.S. 324, 328-29 (1993).

119 *See* 11 U.S.C. § 1325(a)(5)(A).

120 438 B.R. 428 (Bankr. D. Colo. 2010).

121 *Id.* at 429-30.

122 *Id.* at 430.

123 *Id.*

124 *Id.*

125 *See id.* at 431 (finding plan simply recites terms of mortgage modification just as if it was reciting terms of original mortgage).

126 *Id.* at 431-32.

127 *Id.* at 431.

128 *See id.* at 431.

129 WARREN & WESTBROOK, *supra* note 27, at 284-85.

130 520 U.S. 953 (1997).

131 *See* Adam Levitin, *The New Cramdown*, CREDIT SLIPS, (June 29, 2012, 8:01 PM), http://www.creditslips.org/creditslips/2012/06/the-new-cramdown.html#more (positing new cramdown legislation is unnecessary).

132 *Id.*

133 *See id.*

134 *See id.*

135 *See id.*

136 *Id.*

137 *See id.*

138 *Id.*

139 *See* 11 U.S.C. § 1307(a) (2012). Under this section a debtor may convert a chapter 13 case to chapter 7 at any time by filing a notice. *See id.* Pursuant to Rule 1017(f)(3), the bankruptcy court must convert a chapter 13 case to a chapter 7 case without court order when a notice of conversion is filed under section 1307(a). *See* FED. R. BANKR. P. 1017(f)(3) (2013).

140 *See* 11 U.S.C. § 1322(b)(2).

141 503 U.S. 638 (1992).

142 *See id.* at 643.

143 *See* COLLIER ON BANKRUPTCY, *supra* note 110, at ¶ 1327.02(1)(a) ("The binding effect of the confirmation order establishes the rights of the debtor and creditors as those that are provided in the plan. It is therefore incumbent upon creditors ... to review the plan and object to the plan if they believe it to be improper.").

144 *See* Ventura Tax Collector v. Brawders (*In re* Brawders), 325 B.R. 405, 407 (B.A.P. 9th Cir. 2005).

145 *See* Mullane v. Cent. Hanover Bank & Trust Co., 339 U.S. 306, 314 (1950).

146 *See* FED R. BANKR. P. 3015(d), (f) (2013).

147 *See* Factors Funding Co. v. Fili (*In re* Fili), 257 B.R. 370, 373-74 (B.A.P. 1st Cir. 2001) ("A creditor who disregards a procedurally proper and plain notice that its interests are in jeopardy does so at its own risk.").

148 559 U.S. 260 (2010).

149 *Id.* at 275.

150 *See id.* at 264.

151 *Id.*

152 *See id.* Rule 60(b)(4) provides that "the court may relieve a party or its legal representative from a final judgment, order, or proceeding [if] ... the judgment is void." FED. R. CIV. P. 60(b)(4) (2013).

153 *See Espinosa*, 559 U.S. at 272.

154 *See* COLLIER ON BANKRUPTCY, *supra* note 110, at ¶ 1327.02(1)(c).

155 Universal Am. Mortg. Co. v. Bateman (*In re* Bateman), 331 F.3d 821 (11th Cir. 2003).

156 *Id.* at 822 (finding section 1322(b)(2)requires amounts owed to secured creditor not satisfied in full by payments under plan survive discharge).

157 *Id.* at 830.

158 *See* 9D AM. JUR. 2D *Bankruptcy* § 3043 (2014); *see also In re* Hughes, 333 B.R. 360, 362 (Bankr. M.D.N.C. 2005) (stating loan documents should be examined to determine whether a creditor's claim was secured solely by the debtor's principal residence).

159 *In re Hughes*, 333 B.R. at 362.

160 27 F.3d 52 (3d Cir. 1994).

161 *Id.* at 57.

162 *Id.*

163 9D AM. JURIS. 2D *Bankr*. § 3043 (2004).

164 *See In re* French, 174 B.R. 1, 7 (Bankr. D. Mass. 1994).

165 *In re Hughes*, 333 B.R. at 362.

166 *See id.* at 363 (stating that section 1322(b)(2) does not require interest to be perfected, but interest must be secured by something other than real property).

167 259 B.R. 675 (Bankr. N.D. Ill. 2001).

168 *Id.* at 678.

169 *See In re* Spano, 161 B.R. 880, 887 (Bankr. D. Conn. 1993) (acknowledging courts may define what constitutes "additional security" based on applicable state law).

170 *See In re Hughes*, 333 B.R. at 364.

171 *See id.* at 363-64.

172 *See id.*

173 *Id.* at 362.

174 *Id.*

175 *See id.* at 363.

176 *See In re* Brown, 311 B.R. 282, 285 (Bankr. M.D. Fla. 2004) (listing courts which have concluded that security interest in an escrow account for taxes and insurance forfeits protection from modification in section 1322(b)(2)).

177 263 B.R. 728 (Bankr. W.D. Pa. 2001).

178 *See id.* at 733.

179 *Id.* at 732.

180 *See id.*

181 *See id.* at 733; *see also In re* Hughes, 333 B.R. 360, 363-64 (Bankr. M.D.N.C. 2005) (concluding the lender was not afforded the anti-modification provision of section 1322(b)(2) because "escrow funds or an escrow account are entirely separate from the debtor's real property and that a security interest in [this type of fund or account] is a separate and additional security interest").

182 *See In re* Bradsher, 427 B.R. 386, 389 (Bankr. M.D.N.C. 2010).

183 *See* Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. 109-8, 119 Stat. 23 § 306 (2005) (codified as amended in scattered sections of 11 U.S.C.); *see also In re Bradsher*, 427 B.R. at 389 (questioning whether new definitions from the BAPCPA require new result).

184 *See* 11 U.S.C. § 101(13A) (2012).

185 *Id.* § 101(27B).

186 344 B.R. 386 (Bankr. W.D. Pa. 2006).

187 *See id.* at 388.

188 *Id.* at 389.

189 *Id.*

190 *Id.* at 392.

191 Ennis v. Green Tree Servicing, LLC (*In re* Ennis), 558 F.3d 343 (4th Cir. 2009).

192 *See generally id.* at 345-46.

193 *Id.*

194 *See id.* at 346.

195 *See id.* (alterations in original).

196 427 B.R. 386 (Bankr. M.D.N.C. 2010).

197 *See id.* at 389.

198 *Id.* at 389-90.

199 *Id.* at 390.

200 *See id.* at 391-92.

201 *Id.*

202 1st 2nd Mortgage Co. Of NJ, Inc. v. Ferandos (*In re* Ferandos), 402 F.3d 147, 156 (3d Cir. 2005).

203 *Id.* at 155-56.

204 *Id.* at 156.

205 *See id.*

206 *See id.*

207 *See In re* Brown, 311 B.R. 282, 286 (Bankr. M.D. Fla. 2004).

208 *Id.* at 285.

209 *See id.* at 287.

210 *See id.* at 283.

211 *Id.* at 284.

212 *See id.* at 287 (concluding that property rights do not vest in non-existent property).

213 *See id.*

214 *See id.* (noting secured party must control escrow account to create security interest).

215 *See id.* at 283.

216 *See* Fla. Stat. § 679.1041 (2012).

217 *See In re Brown*, 311 B.R. at 287 (requiring escrow account be opened before section 1322 (b)(2) protection is lost).

218 *See, e.g., In re* Bradsher, 427 B.R. 386, 391 (Bankr. M.D.N.C. 2010) (noting deed of trust provided "[t]he Escrow Funds are pledged as additional security for all sums secured by the Security Instrument").

219 *Cf.* Hammond v. Commonwealth Mortg. Corp. of Am. (*In re* Hammond), 27. F.3d 52, 57 (3d Cir. 1994) (indicating escrow accounts and interest subject claims to modification).

220 *See, e.g., In re Bradsher*, 427 B.R. at 389.

221 *See id.* (positing surplus escrow funds act as additional collateral securing debtor's residence).

222 *See In re* Mobley, No. 11 B 34299, 2011 WL 5833976, at *1 (Bankr. N.D. Ill. Nov. 17, 2011). The court in *Mobley* noted the following courts have ruled that section 1322(b)(2) does not prohibit modification of a mortgage of a multi-unit property:
In re Picchi, 448 B.R. 870, 875 (1st Cir. 2011) (permitting cramdown of a multiunit dwelling where the debtor did reside); *Scarborough v. Chase Manhattan Mortgage Corp. (In re Scarborough)*, 461 F.3d 406, 408, 412?13 (3d Cir. 2006) (permitting strip-down on a two-unit property in which the debtor resided); *Chase Manhattan Mortgage Corp. v. Thompson (In re Thompson)*, 77 Fed. Appx. 57, 58 (2d Cir. 2003) (permitting strip-down on a three-unit property in which the debtor resided); *Lomas Mortgage, Inc. v. Louis*, 82 F.3d 1, 7 (1st Cir. 1996) (permitting strip-down on a three-unit property in which the debtor resided); *First Nationwide Mortgage Corp. v. Kinney (In re Kinney)*, No. 3:98CV1753 (CFD), 2000 U.S. Dist. LEXIS 22313, at *11?13 (D. Conn. Apr. 12, 2000) (permitting modification of a two-unit property in which the debtor resided*); In re Stivender*, 301 B.R. 498, 500 n.2 (Bankr. S.D. Ohio 2003) (permitting bifurcation on a two-unit property containing the debtor's residence); *In re Kimbell*, 247 B.R. 35, 38 (Bankr. W.D.N.Y. 2000) (permitting bifurcation on a two-unit property containing the debtor's residence); *Ford Consumer Fin. Co. v. Maddaloni (In re Maddaloni)*, 225 B.R. 277, 278 (D. Conn. 1998) (permitting bifurcation on a two-unit property containing the debtor's residence); *In re Del Valle*, 186 B.R. 347, 348?50 (Bankr. D. Conn. 1995) (permitting modification of a two-unit property, where the debtor lived in one unit and rented the other); *Adebanjo v. Dime Sav. Bank, FSB (In re Adebanjo)*, 165 B.R. 98, 100 (Bankr. D. Conn. 1994) (permitting bifurcation on a three-unit property containing the debtor's residence); *In re McGregor*, 172 B.R. 718, 721 (Bankr. D. Mass. 1994) (permitting modification of a mortgage of a four-unit apartment building in which the debtor resided); *Zablonski v. Sears Mortgage Corp. (In re Zablonski)*, 153 B.R. 604, 606 (Bankr. D. Mass. 1993) (holding that a mortgage encumbering a two-family home was not protected from modification).
Id.

223 461 F.3d 406 (3d Cir. 2006).

224 *Id.* at 414.

225 *Id.* at 411, 414.

226 *See In re* Zaldivar, 441 B.R. 389, 390 (Bankr. S.D. Fla. 2011) (noting minority approach that the anti-modification provision of section 1322(b)(2) "applies to any property that is used as a debtor's principal residence, notwithstanding other uses of the property securing the mortgage").

227 *See id.*; *see also In re* Brunson, 201 B.R. 351, 353 (Bankr. W.D.N.Y. 1996) (concluding courts examine totality of the circumstances to determine whether to strip down mortgage).

228 *In re Zaldivar*, 441 B.R. at 391 (finding that predominant character of transaction controls whether anti-modification provision applies).

229 327 B.R. 830 (Bankr. W.D. Mich. 2005).

230 *Id.* at 840 (citing *In* re *Brunson*, 201 B.R. at 353).

231 *See In re* Rosen, 208 B.R. 345, 350 (D.N.J. 1997).

232 *Id.*

233 *Id.* at 349 (emphasis in original).

234 *Id.* at 350 (quoting N.J.S.A. § 46:3-16 (1997)).

235 *Id.*; *see also* 1st 2nd Mortg. Co. of NJ, Inc. v. Ferandos (*In re* Ferandos), 402 F.3d 147, 155 (3d Cir. 2005) (looking to New Jersey state law and holding that definition of real property includes "rents" and thus protections of section 1322(b)(2) still apply to mortgage).

236 *See In re* Rolle, 281 B.R. 636, 639-40 (Bankr. S.D. Fla. 1998) (holding that under Florida law, rights to rents are incorporeal hereditaments that run with land and thus anti-modification protection still applies); *see also* Allied Credit Corp. v. Davis (*In re* Davis), 989 F.2d 208, 212-13 (6th Cir. 1993); *In re* Spano, 161 B.R. 880, 886 (Bankr. D. Conn. 1993); *In re* Dent, 130 B.R. 623, 628 (Bankr. S.D. Ga. 1991).

237 136 B.R. 797 (Bankr. N.D. Ill. 1992).

238 *See id.* at 802.

239 *Id.* at 799.

240 *Id.* at 802.

241 *See id.* at 803.

242 *See In re* Spano, 161 B.R. 880, 891 (Bankr. D. Conn. 1993) ("Most courts agree that a provision entitling a mortgagee to hazard insurance proceeds does not constitute an interest in collateral other than real property that is the debtor's principal residence.").

243 *See In re* Crystian, 197 B.R. 803, 806 (Bankr. W.D. Pa. 1996).

244 *Id.* at 805-06 (quoting Allied Credit Corp. v. Davis (*In re* Davis), 989 F.2d 208, 211 (6th Cir. 1993)).

245 *See In re* Jackson, 136 B.R. at 802.

246 *Id.*

247 106 B.R. 145 (W.D. Tenn. 1989).

248 *Id.* at 146.

249 *See id.* at 147 (affirming bankruptcy court's decision that "the optional credit life and disability insurance is additional security for the loan ... and therefore the loan was not a claim secured only by a security interest in real property ...") (citation omitted).

250 201 B.R. 371 (Bankr. D.N.J. 1996).

251 *See id.* at 376.

252 California Deed of Trust, Freddie Mac Uniform Instrument Form 3005, *available at* http://www.freddiemac.com/uniform/unifsecurity.html (emphasis added).

253 *See, e.g.*, Florida Mortgage, Freddie Mac Uniform Instrument Form 3010, *available at* http://www.freddiemac.com/uniform/unifsecurity.html ("Property Insurance. All insurance policies ... shall include a standard mortgage clause, and shall name Lender as mortgagee and/or as an additional loss payee .... [T]he insurance proceeds shall be applied to the sums secured by this Security Instrument, whether or not then due .... Borrower hereby assigns to lender ... Borrower's rights to any insurance proceeds .... Lender may use the insurance proceeds either to repair or restore the Property or to pay amounts unpaid under the Note or this Security Agreement, whether or not then due."). A complete list of the Fannie Mae/Freddie Mac Security Instruments used in all states can be found at http://www.freddiemac.com/uniform/unifsecurity.html.

254 Because of the characteristics of large securitized loan transactions, Fannie Mae and Freddie Mac have developed these standard forms. *See* Ronald J. Mann, *Searching for Negotiability in Payment and Credit Systems*, 44 UCLA L REV. 951, 971 (1997). However, by doing so, they have effectively made promissory notes on a home mortgage non-negotiable under the

U.C.C. in many aspects. *See id.* at 972. Arguably, the standardization of forms has muddled the application of section 1322(b)(2) in favor of the practical operation of securitizations. *See id.* at 972-73.

255 *See* Hutchins v. Commonwealth Mortg. Corp., 165 B.R. 401, 402, 404 (E.D. Pa. 1994).

256 Hammond v. Commonwealth Mortg. Corp. of America (*In re* Hammond), 27 F.3d 52 (3d Cir. 1994).

257 *Id.* at 53-54.

258 *Id.* at 58.

259 165 B.R. 401 (E.D. Pa. 1994).

260 *Id.* at 402, 404 (agreeing with Bankruptcy Court's reliance on *In re Hammond* that mortgagee's claim was removed from anti-modification clause).

261 *In re* Jones, 201 B.R. 371, 375-76 (Bankr. D. N.J. 1996).

262 No. 08-17239-BKC-AJC, 2009 Bankr. LEXIS 3206 (Bankr. S.D. Fla. July 22, 2009).

263 *Id.* at *6.

264 *Id.* at *7.

265 *Id.* at *8.

266 Florida Mortgage, Freddie Mac Uniform Instrument Form 3010, *available at* http://www.freddiemac.com/uniform/unifsecurity.html. A survey of the uniform forms of all states and U.S. territories shows that all of these documents include easements, appurtenances and fixtures as part of the secured property.

267 *See id.*

268 400 So. 2d 117 (Fla. Dist. Ct. App. 1981).

269 *See id.* at 119 (determining fixture refers to personal property either constructively or actually attached to soil or structure).

270 *Id.*

271 *Id.* at 118.

272 *See, e.g.*, Cmty. Bank of Homestead v. Barnett Bank of the Keys, 518 So. 2d 928, 930 (Fla. Dist. Ct. App. 1987).

273 *See* First Fed. Sav. & Loan Ass'n v. Stovall, 289 So. 2d 32, 33 (Fla. Dist. Ct. App. 1974)

274 *See In re* Herrin, 376 B.R. 316, 318 (S.D. Ala. 2007) (questioning whether mobile home was real property under section 1322(b) even though Alabama law deems mobile home as personal property).

275 *See Ennis v. Green Tree Servicing, LLC* (*In re* Ennis), 558 F.3d 343, 345-46 (4th Cir. 2009); *In re* Herrin, 376 B.R. at 319.

276 *In re* Herrin, 376 B.R. at 320.

277 8 COLLIER ON BANKRUPTCY, ¶ 1322.06[1][a], at 1322?29 (Alan N. Resnick & Henry J. Sommer eds., 16th ed. 2013) (asserting only if mobile home is real property would limitations on modification apply).

278 *See, e.g., In re* Ennis, 558 F.3d at 346 (noting it is undisputed that mobile home was debtor's principal residence).

279 *See, e.g., In re* Cole, No. 11-12245, 2012 Bankr. LEXIS 21, at *6 (Bankr. S.D. Ohio Jan. 9, 2012).

280 *Nobelman v. Am. Sav. Bank*, 508 U.S.324, 329 (1993) (quoting Butner v. United States, 440 U.S. 48, 54-55 (1979)).

281 *See In re* Ennis, 558 F.3d at 346.

282 558 F.3d 343 (4th Cir. 2009).

283 *Id.*

284 *Id.* at 345.

285 *Id.* at 346.

286 *See id.* at 346-47.

287 *See In re* Herrin, 376 B.R. 316, 321-22 (S.D. Ala. 2007) (declaring section 101(13A) does not authorize courts to expand scope of definition for "debtor's principal residence").

288 Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23, 81 (codified as amended at 11 U.S.C. § 101(13A) (2005)).

289 *See In re* Jordan, 403 B.R. 339, 346 (Bankr. W.D. Pa. 2009).

290 *See In re* Herrin, 376 B.R. at 321 (stating the majority of bankruptcy courts have similarly held section 1322(b)(2) continues to be limited to security interests in real property).

291 378 B.R. 789 (Bankr. E.D. Tex. 2007).

292 *See id.* at 790.

293 *Id.* at 791.

294 *Id.*

295 *See id.* at 791-92.

296 *Id.* at 792-93 (rejecting creditor's argument as logically flawed and in contrast with principles of statutory construction).

297 Craig R. Bucki, *Cracking The Code: The Legal Authority Behind Extrastatutory Debtor-InPossession Financing Mechanisms and Their Prospects for Survival*, 2005 COLUM. BUS. L. REV. 357, 362 (2005) (explaining cross-collateralization permits transformation of undersecured claims against a DIP into secured debt).

298 *See In re* Kain, 86 B.R. 506, 520 (Bankr. W.D. Mich. 1988) (stating creditor's indebtness was cross-collateralized and indebtness was not soley secured by debtor's principal residence).

299 86 B.R. 506 (Bankr. W.D. Mich. 1998).

300 *Id.* at 508.

301 *Id.* at 520.

302 197 B.R. 803 (Bankr. W.D. Pa. 1996).

303 *Id.* at 804.

304 11 U.S.C. § 1123(b)(5) (2012).

305 *In re* Crystian, 197 B.R. at 806.

306 *Id.* at 806-07.

307 *See id.* at 807 (finding prior checking account agreement permitted any claim acquired by creditor to be "secured by the proceeds in the account").

308 *See id.* (holding creditor's claim can be modified).

309 A "deposit account" is "a demand, time, savings, passbook or similar account maintained with a bank. The term does not include investment property or accounts evidenced by an instrument." U.C.C. § 9-102(29) (2003). *See also* James I. Black, III et al., *Proposed FinCEN Regulations and IRS Guidance on Foreign Bank and Financial Account Reporting*, 127 BANKING L.J. 301, 304-05 (2010); Kevin E. Packman, *Reporting Foreign Accounts: Treasury Applies the Carrot and the Stick*, 112 J. TAX'N. 334, 336 (2010).

310 Florida Mortgage, Freddie Mac Uniform Instrument Form 3010, *available at* http://www.freddiemac.com/uniform/unifsecurity.html (emphasis added). A survey of the uniform forms of all states and U.S. territories shows that all of these documents include identical language.

311 *Id.*

312 FLA. STAT. § 697.04(1)(a) (2011). A similar provision is contained in the Kentucky Revised Statutes, KY. REV. STAT. § 382.520(2) ("The mortgage ... may secure any additional indebtedness, whether direct, indirect, existing, future, contingent, or otherwise, to the extent expressly authorized by the mortgage, if the mortgage by its terms stipulates the maximum additional indebtedness which may be secured thereby.").

313 FLA. STAT. § 697.04(1)(a) (2013).

314 11 U.S.C. § 1322(b)(2) (2012).

315 11 U.S.C. § 101(13A).

316 11 U.S.C. § 101(27b).

317 370 B.R. 649 (Bankr. M.D. Pa. 2007).

318 *Id.* at 650.

319 *Id.*

320 *Id.* at 651.

321 *Id.*

322 440 U.S. 48 (1979).

323 *Lunger*, 370 B.R. at 651.

324 *See id.*

325 354 B.R. 505 (Bankr. E.D. Tenn. 2006).

326 *Id.* at 513.

327 *Id.* at 511; *see also In re* Shepherd (*Shepherd II*), 381 B.R. 675, 678 (E.D. Tenn. 2008).

328 *See generally Shepherd II*, 381 B.R. 675. Note that bankruptcy court decisions are appealed to the federal district courts, which is why the district court is revisiting the *Shepherd I* decision and not the 6th Circuit Court of Appeals.

329 *See id.*

330 *Id.* at 678.

331 *Shepherd II*, 381 B.R. at 679 (quoting Herrin v. GreenTree-- Al, LLC, 376 B.R. 316, 320 (S.D. Ala. 2007)).

332 *Id.*

333 *Id.* (noting it is unnecessary to examine legislative history where plain meaning of statute is clear).

334 *Id.*

335 *Id.* at 679-80 (concurring with majority of courts).

336 *Id.* at 680.

337 *In re* Herrin, No. 06-12249-WSS-13, 2007 WL 1975573, at *1 (Bankr. S.D. Ala. July 3, 2007) (concluding Congress did not intend to change section 1322(b)(2) by adding section 101(13A)).

338 *Id.*

339 *See* 11 U.S.C. § 506(a) (2012).

340 *See* 11 U.S.C. § 1322(b)(2).

341 *See* Liao, *supra* note 79, at 2250 (noting Supreme Court has held "the valuation of a secured claim, determined by § 506(a), does not limit a creditor's protected rights").

342 Nobelman v. Am. Sav. Bank, 508 U.S. 324, 328-29 (1993).

343 11 U.S.C. § 1322(b)(5).

344 *Id.*

345 *See* 11 U.S.C. § 1322(b)(2) (allowing for modification of rights of secured creditors).

346 *See In re Nobelman*, 508 U.S. at 329 (concluding "[i]n the absence of a controlling federal rule[,]" property rights in a bankruptcy estate are determined by state law).

347 *See id.* (concluding state law also determines security interests, such as interest of mortgagees).

348 11 U.S.C. § 1322(c)(2).

349 11 U.S.C. § 1322(b)(5).

350 *See id.*

351 *See* Fed. Mortg. Ass'n v. Miller, 473 N.Y.S.2d 743, 744 (Sup. Ct. 1984) (explaining acceleration results in maturation because "the debt has been changed from one payable in the future ... to one payable immediately"); BLACK'S LAW DICTIONARY 12 (8th ed. 2004) (acceleration defined as "the advancing of a loan agreement's maturity date so that payment of the entire debt is due immediately").

352 11 U.S.C. § 1322(c)(2).

353 *In re* Nepil, 206 B.R. 72, 74 (Bankr. D.N.J. 1997).

354 *See id.*

355 *Id.*

356 *See* Witt v. United Companies Lending Corp. (*In re* Witt), 113 F.3d 508, 514 (4th Cir. 1997).

357 *See In re* Nepil, 206 B.R. at 77 (finding wide support for applicability of section 1322(c)(2) to balloon payments).

358 *See In re* Williams, 109 B.R. 36, 41 (Bankr. E.D.N.Y. 1989).

359 H.R. 5116, 103rd Cong. (1994).

360 *Id.* (emphasis added).

361 *See* H.R. REP. NO. 103-835, at 52 (1994), *reprinted in* 1994 U.S.C.C.A.N. 3340, 3361.

362 *See In re Nepil*, 206 B.R. at 77.

363 *See In re* Lobue, 189 B.R. 216, 218 (Bankr. S.D. Fla. 1995) (describing broad language of §1322(c)(2)).

364 *See id.*

365 *See* H.R. REP. NO. 103-835, at 52 (1994), *reprinted in* 1994 U.S.C.C.A.N. 3340, 3361(explaining purpose of section 1322(c)(2)).

366 *See* Moringiello, *supra* note 13, at 1612 (discussing administrative punishment of creditors).

367 *See id.* at 1616.

368 *See id.* at 1617 n.119.

369 *See id.* at 1617.

370 *See id.*

371 *See id.*

372 *Id.* (explaining dischargeablity provisions incorporate ideas of "creditor worthiness"); *see also* 11 U.S.C. §§ 523(a)(1)-(19) (2012) (highlighting exceptions to discharge).

373 Moringiello, *supra* note 13, at 1620-21 (describing "super priority" status granted to home mortgage creditors).

374 "Predatory lending" has been defined in an advisory opinion by the Massachusetts Commissioner of Banks as "'extending credit to a consumer based on the consumer's collateral if, considering the consumer's current and expected income ... the consumer will be unable to make the scheduled payments to repay the obligation.'" Commonwealth v. H&R Block, Inc., No. 08-2474- BLS1 *6 -7 (Mass. Super. Ct. Nov. 24, 2008) (internal citations omitted). *See generally* Federal Deposit Insurance Corp., Office of Inspector General, CHALLENGES AND FDIC EFFORTS RELATED TO PREDATORY LENDING, REP. NO. 06-011 (June 2006), *available at* http://www.fdicoig.gov/reports06/06-011.pdf (identifying risks of predatory lending and issuing guidance to FDIC-supervised financial institutions).

375 *See* Moringiello, *supra* note 13, at 1609 (indicating preferable home mortgage loan practices when chapter 13 was enacted).

376 *See id.* at 1609-11 (explaining recent abusive mortgage underwriting practices).

377 *See id.* at 1620 (urging judicial application of equitable subordination when "the creditor's conduct begs an equitable remedy").

378 *Id.* at 1621.

379 *Id.*

380 *See id.* at 1633-34 (urging courts to cram down home mortgage claims and use equitable subordination to re-prioritize bifurcated unsecured claims).

381 *See id.* at 1599.

382 *See id.* at 1620.

383 11 U.S.C. § 510(c)(1) (2012) (allowing claim priority reorganization).

384 *See* 11 U.S.C. § 510(a).

385 11 U.S.C. § 510(c)(1).

386 11 U.S.C. § 510(c)(2).

387 Legislative Statement to 11 U.S.C. § 510(c)(1) (emphasis added) (indicating Congress's intent allowing principles equitable subordination to secured and unsecured claims).

388 11 U.S.C. § 510(c)(2); *see also id.*

389 Moringiello, *supra* note 13, at 1622-23 (describing equitable subordination's goals to prevent unfair distribution of estate assets).

390 *See id.* at 1622.

391 *Id.*

392 *See id.* at 1623.

393 *Id.*

394 *Id.*

395 *See id.* at 1625.

396 *See, e.g., In re* Lifschultz Fast Freight, 132 F.3d 339, 344 (7th Cir. 1997) (describing courts' use of equitable subordination to eradicate bad-faith conduct during reorganization).

397 563 F.2d 692 (5th Cir. 1977).

398 *Id.* at 699-700 (internal citations omitted).

399 *See, e.g., In re Lifschultz Fast Freight*, 132 F.3d at 344; Feder v. Lazar (*In re* Lazar), 83 F.3d 306, 309 (9th Cir. 1996); Lemco Gypsum, Inc. v. Miller (*In re* Lemco Gypsum, Inc.), 911 F.2d 1553, 1556 (11th Cir. 1990); *In re* 1236 Dev. Corp., 188 B.R. 75, 81 (Bankr. D. Mass. 1995); *In re* Octagon Roofing, 141 B.R. 968, 980 (Bankr. N.D. Ill. 1992).

400 *See In re Mobile Steel Co.*, 563 F.2d at 695 (describing additional fiduciary relationship among corporate officers and shareholders).

401 *See* 11 U.S.C. § 101(31) (2012).

402 *See In re* Chira, 378 B.R. 698, 712 (S.D. Fla. 2007) (discussing court's higher standard for insiders during equitable subordination discussion); *see also* Moringiello, *supra* note 13, at 1629.

403 Capital Bank v. MVB, Inc., 644 So. 2d 515, 518 (Fla. Dist. Ct. App. 1994) (describing typical bank-borrower relationship).

404 *Id.* at 519 (*quoting* Klein v. First Edina Nat'l Bank, 196 N.W.2d 619, 623 (Minn. 1972)).

405 *Id.*

406 *See* Gramm-Leach-Bliley Act, Pub. L. No. 106-102, 113 Stat. 1338 (1999).

407 *See id.* at § 103(a)(k)(4).

408 *Id.*

409 Moringiello, *supra* note 13, at 1626.

410 *Id.* at 1627; *see, e.g., In re* Lifschultz Fast Freight, 132 F.3d 339, 345 (7th Cir. 1997).

411 *See In re Lifschultz Fast Freight*, 132 F.3d at 345 ("Most often undercapitalization signifies nothing more than business failure, poor access to capital, or both."); *see also In re* 1236 Dev. Corp., 188 B.R. 75, 83 (Bankr. D. Mass. 1995) (citing multiple cases where undercapitalization alone was not enough for subordination of claims).

412 *See In re* Yellowstone Mountain Club, LLC, No. 08-61570-11, 2009 Bankr. LEXIS 2047, at *22 (Bankr. D. Mont. May 13, 2009) (quoting Henry v. Lehman Commercial Paper, Inc. (*In re* First Alliance Mortg. Co.), 471 F.3d 977, 1006 (9th Cir. 2006)).

413 *See In re Yellowstone Mountain Club, LLC*, 2009 Bankr. LEXIS 2047, at *24 (noting difficulty in articulating levels of misconduct required to subordinate non-insider claims).

414 *In re* Felt Mfg. Co., Inc., 371 B.R. 589, 5624 (Bankr. D.N.H. 2007).

415 2009 Bankr. LEXIS 2047.

416 *See id.* at *7-10.

417 *See id.* at *11-12.

418 *See id.* at *27.

419 *See id.* at *25.

420 *Id.* at *31.

421 *See id.* at *22?31 (showing absence of third prong analysis).

422 *See id.* (providing lack of third prong analysis but Credit Suisse's lien must be subordinated anyway due to gross misconduct in lending practices).

423 *See* Jo Ann J. Brighton & Felton E. Parrish, Yellowstone*: New Standards for Lender Ability in Today's Economic Climate*, 28 AM. BANKR. INST. J., Sept. 2009 at 28, 28 (Sept. 2009) (citing to *In re* Yellowstone Mountain Club, LLC as depicting court willingness to look "at lending transactions with greater scrutiny than ever before").

424 No. 3:10-bk-667-PMG (Bankr. M.D. Fla. 2011).

425 *See id.* at *6.

426 *See id.* at *2.

427 *See id.*

428 *See id.* at *2?3 (showing lender's filing of secured proof of claim followed by debtor's filing to equitably subordinate it).

429 *Id.* at *4. (stating all three conditions from *In re Mobile Steel Co.* "must be satisfied before a claim is equitably subordinated").

430 *See id.* at *6.

431 *See id.*

432 *Id.* at *7.

433 *Id.* at *9.

434 *Id.*

435 *Id.* at *9-10 (*citing In re* AtlanticRancher, Inc., 279 B.R. 411, 441 (Bankr. D. Mass. 2002).

436 *Id.* at *10.

437 *Id.*

438 *Id.* at *11 (revealing effect of relief sought by debtors is to bifurcate HSBC's claim).

439 *In re* Downer, No. 3:10-bk-667-PMG, at *11-12 (presenting subordination of HSBC's claim by debtors as inconsitent with Code).

440 *Id.* at *14.

441 *In re* Felt Mfg. Co., Inc., 371 B.R. 589, 624 n.6 (Bankr. D.N.H. 2007).

442 *See* Law Office of David J. Stern, P.A. v. Sec. Nat'l Servicing Corp., 969 So. 2d 962, 968 (Fla. 2007).

443 *Id.* (quoting State v. Family Bank of Hallandale, 667 So. 2d 257, 259 (Fla. Dist. Ct. App. 1995).

444 *See* Shaw v. State Farm Fire & Cas. Co., 37 So. 3d 329, 333 (Fla. Dist. Ct. App. 2010).

445 *Id.*

446 *See In re* Yellowstone Mountain Club, LLC, No. 08-61570-11, 2009 Bankr. LEXIS 2047, at *25 (Bankr. D. Mont. May 13, 2009).

447 *See id.*

448 *See* Adam J. Levitin, *Finding Nemo: Rediscovering the Virtues of Negotiability in the Wake of Enron*, 2007 COLUM. BUS. L. REV. 83, 88-89 (2007).

449 333 B.R. 205 (Bankr. S.D.N.Y. 2005).

450 *Id.* at 219.

451 *Id.* at 223.

452 *See id.*

453 *Id.* at 226.

454 *Id.* at 231.

455 *See id.* at 211.

456 11 U.S.C. § 510(c) (2012).

457 *See In re Enron Corp.*, 333 B.R. at 230 (looking to Congress to provide “special protection” to certain claims' transferees).

458 WARREN & WESTBROOK, *supra* note 27, at 301.

459 *See id.*; *see also* Mann & Porter, *supra* note 98 at 337 (considering social losses that may result from deferral of a bankruptcy filing).

460 *See* Mann & Porter, *supra* note 98, at 310.

461 *See* Porter, *supra* note 102, at 125.

462 *See supra* Table 1, Part II (discussing effectiveness of cures on underwater homestead mortgages in study analyzing chapter 13 cases filed in Southern District of Florida in April 2009).

463 *See id.* Note this percentage is for lien-strips only (i.e. case code 3), and this percentage is not applicable to cures in conjunction with lien-strips (i.e. case code 4).

464 *See id.*

465 Stephen Spruiell, *Republicans Win a Big One-For a Change*, CBS NEWS (Sept. 22, 2009), http://www.cbsnews.com/stories/2009/06/09/opinion/main5075109.shtml?tag=contentMain;contentBody.

466 *Id.*

467 *See* Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555, 601-02 (1935) (discussing how refinancing of farm mortgages and relief under contracts are matters for Congress).

468 *See Helping Families Save Their Homes in Bankruptcy Act of 2009 and Emergency Homeownership and Equity Protection Act: Hearing on H.R. 200 and H.R. 225 Before the H. Comm. on the Judiciary*, 111th Cong. 35 (2009) (statement of Adam J. Levitin, Associate Professor of Law, Georgetown University Law Center) (discussing importance of bankruptcy as method for addressing financial issues).

469 *See id.* (stating bankruptcy modification "is truly the only serious option on the table" for dealing with the foreclosure crisis).

470 Zinman & Petrovski, *supra* note 64, at 139.

471 Levitin & Goodman, *supra* note 3, at 4.

472 *Id.*

473 *Straightening Out the Mortgage Mess: How Can We Protect Home Ownership and Provide Relief to Consumers in Financial Distress? (Part II): Hearing Before the Subcomm. on Commercial and Admin. Law of the H. Comm. on the Judiciary*, 110th Cong. 113 (2007) (statement of David G. Kittle, CMB, Chairman-Elect, Mortgage Bankers Association).

474 Hauser, *supra* note 74, at 230.

475 *Straightening Out the Mortgage Mess: How Can We Protect Home Ownership and Provide Relief to Consumers in Financial Distress? (Part II), supra* note 471.

476 Adam J. Levitin & Joshua Goodman, *Mortgage Market Sensitivity to Bankruptcy Modification*, 48 Third Annual Conference on Empirical Legal Studies Papers (April 15, 2008), *available at* SSRN: http://ssrn.com/abstract=1121054 or http://dx.doi.org/10.2139/ssrn.1121054.

477 *See id.*

478 *See id.* at 16 (discussing tenant risks that accompany investor properties).

479 *See* Levitin & Goodman, *supra* note 3, at 5.

480 *Id.*

481 *See id.* at 7 (finding it "unsurprising that vacation homes have the same rates as single-family principal residences" because tenancy risk factors are not present and "they are typically well-maintained").

482 *Id.*

483 *See id.*

484 *Id.* at 40.

485 *Id.*

486 *Id.*

487 *Id.* (suggesting if anything bankruptcy modification will have a *de minimis* effect on interest rates).

488 *See* Hauser, *supra* note 74, at 231 ("By definition, creditors exposed to the risk of cramdown are undersecured[.]").

489 *See id.*

490 *Id.* (arguing that "risks associated with ... underperforming mortgages, [in which the borrowers are seeking cramdown,] will already have been realized before bankruptcy is filed").

491 *See* John Eggum, Katherine Porter & Tara Twomey, *Saving Homes in Bankruptcy: Housing Affordability and Loan Modification*, 2008 UTAH L. REV. 1123, 1158 (2008).

492 *Id.* at 1158-59.

493 *Id.* at 1159.

494 *See supra* Part II (discussing the effectiveness of cures on underwater homestead mortgages in the study analyzing chapter 13 cases filed in the Southern District of Florida in April 2009). Note also this percentage pertains only to case code 1, i.e. pure underwater homestead cures, and not underwater homestead cures in conjunction with lien-strips.

495 *See* BAXTER DUNAWAY, 3 LAW OF DISTRESSED REAL ESTATE 30-133 (2013).

496 *See id.*

497 *State of the Housing Market: Removing Barriers to Economic Recovery, Hearing Before the S. Comm. on Banking, Housing, and Urban Affairs*, 112th Cong. 5-6 (2012) (testimony of Phillip L. Swagel, Professor, University of Maryland, School of Public Policy).

498 Mann & Porter, *supra* note 98, at 297 (citing an Australian study which found that bankruptcy is viewed by debtors as a last resort).

499 *See* Zinman & Petrovski, *supra* note 64, at 150 (discussing the Supreme Court's decision in *Louisville Joint Stock Land Bank v. Radford*).

500 459 U.S. 70 (1982).

501 *Id.* at 75.

502 *See* Zinman & Petrovski, *supra* note 64, at 152.

503 311 U.S. 273 (1940).

504 *Id.* at 278-79.

505 *See* Zinman & Petrovski, *supra* note 64, at 153.

506 *See id.* at 154.

507 Epstein, *supra* note 33, at 468.

508 *See id.* (noting that this applies to cram down interest rate).

509 *See generally* Zinman & Petrovski, *supra* note 64, at 156-58.

510 *See id.* at 157.

511 Epstein, *supra* note 33, at 464.

512 *Id.* at 464-65 (describing investment technique where cram down loans are divided into senior loans and junior loans).

513 *See id.* at 465.

514 Nobelman v. Am. Sav. Bank, 508 U.S. 324, 332 (1993) (Stevens, J. concurring).

515 *Id.*

516 *Id.*

517 *In re* Shaffer, 84 B.R. 63, 65 (Bankr. W.D. Va. 1988) ("[S]hort term, non-home related, finance company loans are not within the Congressional intended scope of [s]ection 1322(b)(2).").

518 *See* 11 U.S.C. § 1322(c)(2) (2012).

519 Hauser, *supra* note 74, at 213.

520 *Id.*

521 *See id.* at 215-16 (describing rule that allows junior mortgage undersecured under section 506 to be stripped down to unsecured claim despite anti-modification language).

522 *See id.* at 222.

523 *Id.* at 223-24.

524 *Id.* at 224.

525 *See id.*

526 *See id.* at 224-25 (requiring responsible budgeting and avoiding substantial new debts without court permission).

527 *See id.* at 225; *see also supra* Part II (discussing how in a study of all the chapter 13 cases filed in the Southern District of Florida in April 2009, proposed lien-strips on unsecured mortgages of underwater homestead properties were almost seven times as effective a home-saving device as proposed cures on underwater homestead properties, likley in part because of the incentiving effect the lien-strip had on the debtor to complete his chapter 13 plan).

528 *See supra* Part II (discussing author's empirical study).

529 *See* Hauser, *supra* note 74, at 225 (noting mandatory loan modification eliminates risk of investors suing lenders for financial injury).

530 *See id.*

531 *Id.* at 226-27 (indicating individual and community property values decrease when foreclosures occur).

532 *See id.* at 226.

533 *See id.* (noting chapter 13 spares creditors from paying foreclosure and resale costs).

534 *See id.* (discussing creditors' ability to recapture appreciation in property value if debtor sells property before plan completion, or if debtor defaults on plan).

535 *See* Zinman & Petrovski, *supra* note 64, at 162 (suggesting addition of subsection to 1322 allowing payment of allowed secured claims up to the remaining term of mortgage).

536 *See Helping Families Save Their Homes in Bankruptcy Act of 2009 and Emergency Homeownership and Equity Protection Act: Hearing on H.R. 200 and H.R. 225 Before the H. Comm. on the Judiciary, supra* note 466, at 26.

537 Levitin, *supra* note 75, at 568.

538 Levitin & Goodman, *supra* note 3, at 27.

539 *Id.*

540 *Id.*

541 *Id.*

542 *Id.* at 32.

543 *See* Rod Dubitsky, et al., *Bankruptcy Law Reform--A New Tool for Foreclosure Avoidance*, FIXED INCOME RESEARCH 9 (Jan. 26, 2009) http://www.bankruptcylawnetwork.com/wpcontent/uploads/2009/01/credit_suisse_bankruptcy_law_reform.pdf ("Our review of the bankruptcy filing of securitized subprime loans shows that the average failure rate is about 54%.").

544 Levitin & Goodman, *supra* note 3, at 32.

545 *Id.*

546 *Id.*

547 *See The Worsening Foreclosure Crisis: Is It Time to Reconsider Bankruptcy Reform?: Hearing Before the Subcomm. on Admin. Oversight & the Courts, of the S. Comm. on the Judiciary*, 111th Cong. 9 (2009) (written testimony of Adam J. Levitin, Associate Professor of Law, Georgetown University Law Center).

548 *See id.*

549 Levitin & Goodman, *supra* note 3, at 38 ("The 2007 Riverside data confirms what the 2001 CBP data indicated: that mortgage markets are indifferent to strip-down risk because it is small in magnitude and likelihood, and may represent lesser losses than lenders would incur in foreclosure.").

550 *See* Kathleen Munden, *Failure By Mortgage Companies to Modify Mortgages May Reawaken Bankruptcy Cramdown Legislation*, 1-2 KRAFT & ASSOC.(WHITE PAPER)))) (Oct. 15, 2009), *available at* http://www.jdsupra.com/post/documentViewer.aspx?fid=441e8d06-1347-4bce-9fac-a53dfc62f180.

551 *Id.* at 1.

552 *See The Worsening Foreclosure Crisis: Is It Time to Reconsider Bankruptcy Reform?: Hearing Before the Subcomm. on Admin. Oversight & the Courts, of the S. Comm. on the Judiciary, supra* note 545, at 5.

553 *See id.* ("[A]fter 2 years of effort that relies on banks to volunteer ... it is time to admit that is not working.").

554 *See id.* at 7-8.

555 *See* U.S. DEP'T OF TREAS., PROGRAM PERFORMANCE REPORT THROUGH DECEMBER 2011: MAKING HOME AFFORDABLE, 12 (2011), *available at* http://www.treasury.gov/initiatives/financial-stability/reports/Documents/Dec%202011%CC20MHA%CC20Report%20FINAL.PDF.

556 *See The Worsening Foreclosure Crisis: Is It Time to Reconsider Bankruptcy Reform?: Hearing Before the Subcomm. on Admin. Oversight & the Courts, of the S. Comm. on the Judiciary, supra* note 545, at 8.

557 *Id.* at 1.

558 *See* Peter Wallison, *Hey, Barney Frank: The Government Did Cause the Housing Crisis*, THE ATLANTIC (Dec. 13, 2011, 11:20 AM), http://www.theatlantic.com/business/archive/2011/12/hey-barney-frank-the-government-did-cause-the-housing-crisis/249903/.

559 *See* Hauser, *supra* note 74, at 226.

560 *See id.* at 232.

561 *See id.*

562 *See id.* at 227.

563 *See id.*

564 *Id.* at 228.

565 *See id.*

566 *Id.* (quoting Press Release, Mortgage Bankers Ass'n, MBA's Kittle Challenges Bankruptcy Myths at Hearing (Jan. 29, 2008), http://www.mortgagebankers.org/NewsandMedia/PressCenter/59656.htm).

567 *See id.* at 212.

568 *See id.* at 225 (noting debtors need discipline to complete plan).

569 *See id.* at 229.

570 *See id.*

571 *See id.* (concluding lenders need accountability).

572 Anne Flaherty, *Senate Defeats Anti-Foreclosure Bill*, ASSOCIATED PRESS, Apr. 30, 2009, http://abclocal.go.com/wpvi/story?section=news/politics&id=6789561 (last visited Mar. 18, 2014).

573 *See generally* International Monetary Fund, Concluding Statement of the 2012 Article IV Mission to the United States of America, July 3, 2012, *available at* http://www.imf.org/external/np/ms/2012/070312.htm (last visited Mar. 18, 2014).

574 *See id.*

575 *See id.* (recommending implementation of new regulatory framework and systemic risk monitoring).

576 *Id.* at 7.

577 *See id.*

578 *See id.* (noting additional steps must be taken to strengthen housing recovery).

579 *See Foreclosures to Affect 6.5 Mln Loans by 2012*, Report, REUTERS (Apr. 22, 2008), *available at* http://www.reuters.com/article/bondsNews/idUSN2233380820080422.

580 *See supra* Part II (discussing Author's empirical study).

581 *See* Stellwagen v. Clum, 245 U.S. 605, 617 (1918).

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