Too Close to Call –
Confirmation Requirements of a Chapter 13 Plan

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Adequate Protection in the Chapter 13 Context

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It is well settled that a secured party is secured to the extent of the value of the collateral. And the holder of a secured claim is only as "protected" as the value of the collateral in which that party has a position, in the order of priority.

A Chapter 13 debtor who wants to keep and use property of the estate which is subject to the claim of a secured party must provide adequate protection to and for the benefit of that secured party, to the extent of any depreciation in the value of the collateral. The concept is simple: keep the secured party in at least as good a position with respect to the underlying collateral, as relates to the claim, as that party enjoyed at the beginning of the case.

In **United Savings Association of Texas v. Timbers of Inwood Forest Associates**, Ltd 484 US 365, 108 S. Ct. 626 Argued Dec. 1, 1987 and decided Jan. 20, 1988), the United States Supreme Court, citing the Bankruptcy Code, said "Section 506 of the Code defines the amount of the secured creditor's allowed secured claim… In relevant part it reads as follows: "(a) An allowed claim of a creditor secured by a lien on property in which the estate has an interest… is a secured claim 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…"

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The Court was dealing specifically with the issue of interest (as well as any reasonable fees, costs or charges) that might be payable to the holder of a secured claim. The petitioner in that case was undersecured and, as a result, the Court found that "the undersecured petitioner is not entitled to interest on its collateral during the stay to assure adequate protection under 11 USC 362(d)(1)"

Of course, the value of the underlying collateral is a critical issue in both the determination of secured status, as well as the determination of entitlement to post-petition interest or any form of adequate protection. In 2005, BAPCPA amended section 506 by adding new section 506(a)(2) in relevant part as follows: "If a debtor is an individual in a case under Chapter 13, such value with respect to personal property securing an allowed claim shall be determined based on the replacement value of such property as of the date of the filing of the petition without deduction for costs of sale or marketing. With respect to property acquired for personal, family, or household purposes, replacement value shall mean the price a retail merchant would charge for property of that kind considering the age and condition of the property at the time value is determined."

So, the value needs to be determined as of the filing date and that value will determine the extent of the secured party's claim. The addition of new Code section 506(a)(2) appears to be a reaction by Congress to the interests of parties who hold claims secured by interests in ***personal property,*** since the issue and importance of adequate protection prior to the 2005 amendments

most often would come up in matters regarding real property and the interests of mortgagees and other lienholders.

Chapter 13 of the Code also added new section 1325 (a)(5)(B)(iii)(II), (Confirmation of plan) saying: “(a)… the court shall confirm a plan if …(5)with respect to each allowed secured claim provided for by the plan – (B)(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—(II) 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;”

As a result of BAPCPA, Congress also made additions to the Payments (section 1326) section of the Code, by replacing 1326(a)(1) as follows: “Unless the Court orders otherwise, the debtor shall commence making payments…in the amount—(C)that provides adequate protection directly to a creditor holding an allowed claim secured by personal property to the extent the claim is attributable to the purchase of such property by the debtor for that portion of the obligation that becomes due after the order for relief, reducing the payments under subparagraph (A) by the amount so paid and providing the Trustee with evidence of such payment, including the amount and date of payment,

It appears that the interests of creditors who hold purchase money security interests in personal property have been newly addressed by Congress. Prior to the enactment of BAPCPA, a debtor would typically pay regular monthly lease and secured (on personal property such as an

automobile) payments to the lessor or the secured party, as the case may be, on a post-petition basis. The Chapter 13 plan would permit the debtor to deal appropriately with the arrears or permit other treatment of the claim of the secured party. Now, the debtor appears obligated to provide, to the holder of a claim secured by a security interest in personal property that the debtor intends to retain, adequate protection payment(s) to that secured party.

Typically, those adequate protection payments must be sufficient to accommodate the secured party with respect to the amount of any depreciation in the value of the collateral over the applicable term. The debtor receives a credit, as against payments due under the plan to be paid to the Trustee, for the amount of payment so made.

Since the value of some (much) personal property depreciates faster than the loan balance reduces, even when regular payments are made on a timely basis, this section can have significant benefit to such creditors as car lenders. In an article in the Wall Street Journal on May 22, 2007, the author indicated that as to buyers with negative equity who are trading in their cars, the amount of negative equity has risen steadily over the years. As a result, car buyers are purchasing new cars and extending the financing for six, seven and even up to nine years, to make the monthly payment conform to their monthly budget.

So, one can envision a Chapter 13 debtor whose vehicle is worth considerably less than the balance on the pmsi loan, and the lender expecting adequate protection payments as required by 1326(a)(1)(c) to protect as against any further depreciation as compared to the value/loan ratio as of the filing date. Query how this will sort out in light of the new prohibition (at the end of 1325

(a) regarding motor vehicles acquired for the personal use of the debtor and purchase money loans incurred within 910 days of the petition date.

In Chapter 13, adequate protection has historically been raised as an issue with respect to Motions for Relief from Stay, usually filed by mortgagees as a result of post-petition nonpayment by a debtor. Lack of adequate protection is often pled as a reason for the granting of the Motion for Relief from Automatic Stay. Of course, this depends on "value," and whether or not there is an "equity cushion" to provide some comfort to the holder of the secured claim. In an appreciating real estate market, adequate protection payments may be unnecessary. Of course, in a depressed market where real estate values are depreciating, regular monthly payments on a post-petition basis may not satisfy the holder of the secured claim.

For example, in the case of **In re Lemieux**, 347 B.R.460 (Bankr. D. Mass. 2006), Judge Feeney refused to approve the Chapter 13 debtor's proposed Plan, observing "the importance of maintaining the creditor's lien rights." Unlike the previous section 1325, the new language seems to require that payments made after confirmation be in equal amounts and keep pace with depreciation during the term of the Plan. "Americredit Financial Services Inc. v. Nichols (In re: Nichols), 440 F.3d 850, 857 n. 6 (6th Cir.2006).

In **Sarafoglou**, (345 B.R. 19 (2006)) Judge Robert Somma held for the Chapter 13 debtor, with monthly net disposable income of more than $6,700, and more than $400,000 of equity in her residence satisfied the burden of showing that her current bankruptcy case, filed close on the heels of two prior bankruptcy cases, was filed in good faith. In addition, the Judge held that the

mortgagee was not entitled to relief from the automatic stay based upon alleged lack of adequate protection for its interest. At trial, the debtor had offered unrebutted testimony that the residence had a value significantly higher than the mortgage debt owed to Wachovia. The Court found that Wachovia was more than adequately protected by a substantial equity cushion.

In **In re Beaver**, (337 B.R. 281 (Bankr. D.N.C. 2006)) the petitioner creditor filed a Motion for pre-confirmation adequate protection of its security interests in vehicles owned by one of the respondent debtors. The debtors objected that adequate protection could be provided by means other than the direct payments requested. The Court approved the parties' agreement that the Chapter 13 Trustee would make pre-confirmation payment to the creditor, on a monthly basis. Further, the Court found that "even if Coastal's interpretation of 1326 (a)(1)(C) is correct, section 1326(a)(1), which begins "unless the Court orders otherwise", gives the Court the discretion to alter a requirement that the debtor make direct pre-confirmation adequate protection payments to a secured creditor."

The Court went further to state that "it is well established bankruptcy law, and practice that when adequate protection is required to protect an interest of an entity in property, it may be provided by a variety of methods. Providing cash payments directly to the entity holding the interest in property is one of those methods, but it is not the exclusive method. Section 361 provides that **adequate protection** may be provided by cash payments, replacement liens, or "such other relief" as would "result in the realization by such entity of the indubitable equivalent of such entity's interest in such property." Adequate protection can take many forms, and may even be

the status quo where the value of the creditor's collateral is sufficient to provide an "equity cushion."

That same Court also suggests that "a plan that provides for the payment of the secured claim over the life of the Plan, and also provides that a portion of each pre-confirmation payment will be distributed to the secured creditor in the event that the Plan is not confirmed and the case is dismissed may provide adequate protection without the necessity of pre-confirmation payments to the secured creditor." This is simply because payments made with respect to a Plan that is not confirmed are returned to the debtor when the case is dismissed.

An interesting twist was addressed in the matter of **In re Eric G. DeSardi, Jr. (and others)** where Judge Marvin Isgur held that adequate protection payments awarded to creditors whose claims were secured by interest in Chapter 13 debtor's motor vehicles, in the absence of an objection, are payable on a priority basis as administrative expense and the administrative expense claims held by these creditors were payable ahead of administrative claims held by debtor's attorneys. Judge Isgur also found that adequate protection payments to which creditors were entitled had to be calculated based on the value of the motor vehicle, rather than upon the amount of the creditor's allowed claims. Finally, Judge Isgur attached a series of charts to his opinion (attachments a,b, and c) which provided insightful detail and calculated information regarding the principal owed, the Till interest rate, plan payments, interest, principal, and ending balances, as well as calculations for payments to car lenders and payments to debtor's counsel.

In **In re Edekawa Brown** (Drive Financial Services, Movant vs. Edekawa Brown and James H. Bone, Trustee as respondents) Judge Joyce Bihary found that the clause "unless the Court orders otherwise" gave the Court discretion, not just to alter the timing of the debtor's payments, but to allow the debtor to make payments to the Trustee for disbursement to the creditor. In addition, Judge Bihary found that a secured creditor could not apply pre-confirmation adequate protection payments that it received first to interest, and then to principal, but could apply such payments only to principal. The Judge further indicates "past bankruptcy practice supports the conclusion, and the Court holds that these pre-confirmation adequate protection payments are to compensate for any depreciation in the collateral, and should be applied to principal only."

In summary, issues regarding adequate protection in the context of the Chapter 13 case have changed significantly with the implementation of BAPCPA. A lender with a purchase money security interest, typically in a motor vehicle, can require a debtor to make adequate protection payments to effectively make up for future depreciation with respect to the value of the vehicle, during the course of the Chapter 13 Plan. How this may be done, as a practical matter, will likely depend on the interpretation of individual Judges, but it is clear that dealing with a car loan in a Chapter 13, even if the payments are current at the time of filing, will be different from prior practice. It does, however, appear that the concept of adequate protection is still designed to provide protection in the event the value of the collateral depreciates at a faster rate than the balance on the underlying obligation. The book keeping and record keeping can become complicated, and there is no question that the burden is now on a Chapter 13 debtor to make adequate protection payments where that burden did not previously exist under prior law.

DID BAPCPA BURST BALLOON PAYMENT PLANS?

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Consumers facing a home mortgage foreclosure may find bankruptcy is the most effective option for saving their home. Chapter 13 is the most commonly used form of bankruptcy in consumer home defense. It provides a powerful right generally unavailable under state law namely, the right to de-accelerate a mortgage default and cure the default by paying the arrearage over a period not exceeding five years. For some debtors, particularly those with large arrearage amounts, balloon payment plans have been an important home saving device. Under such plans, debtors typically make relatively small monthly payments[1] throughout the plan followed by a large lump sum payment in the final month. Debtors commonly intend to fund the final payment through the sale of the home or refinancing of their mortgage loan.

Prior to BAPCPA, the question of whether a balloon payment plan in chapter 13 could be confirmed focused on feasibility.[2] Post-BAPCPA balloon plan cases have turned their attention to the "equal monthly payment" provision added in 2005.

Section 1325 provides that the court "shall" confirm a chapter 13 plan if certain requirements are met. Section 1325(a)(5) gives the debtor three options for dealing with allowed secured claims provided for by the plan: (1) the creditor may accept the plan, § 1325(a)(5)(A); (2) the debtor may surrender the collateral to the secured creditor § 1325(a)(5)(C); or (3) the plan may provide for treatment of the allowed secured claim in accordance with section 1325(a)(5)(B). In turn, section 1325(a)(5)(B)(iii) states that:

"(iii) if

(I) property to be distributed pursuant to this subsection is in the form of periodic payments, such payments shall be in equal monthly amounts, and

(II) 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 the holder of such claim adequate protection during the

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[1] In some cases, the monthly payments represent the monthly post-petition payment due on the mortgage loan plus a small fraction of the arrears with the majority of the arrears being paid through the lump sum payment at the end of the plan.

[2] 11 U.S.C. 1325(a)(6); *See In re* Wagner, 259 B.R. 694 (B.A.P. 8th Cir. 2001); *In re* Fanatasia, 211 B.R. 420 (B.A.P. 1st Cir. 1997); *In re* Endicott, 157 B.R. 255 (W.D. Va. 1993); *In re* Cloud, 209 B.R. 801 (Banknr. D. Mass. 1997); *In re* Harris, 199 B.R. 344 (Bankr. N.H. 1996); *In re* Gregory, 143 B.R. 424 (Bankr. E.D. Tex. 1992); *In re* Groff, 131 B.R. 703 (Bankr. E.D. Wis. 1991); *In re* Brunson, 87 B.R. 304 (Bankr. D.N.J. 1988).

period of the plan.

Several courts have already been called upon to decide whether this new language bans balloon payment plans used to cure defaults on mortgage loans. To date, no clear answer has emerged.

No Objection, No Problem.

As noted above, debtors are entitled to confirmation of their chapter 13 plans over the objections of secured creditors if the plan complies with the provisions of section 1325(a)(5)(B). However, obtaining a creditor's consent to a plan instead is just as good. Where creditors consent, failure to treat an allowed secured claim in accordance with section 1325(a)(5)(B) should not prohibit confirmation. Furthermore, it has long been held that courts may find creditor consent under section 1325(a)(5)(A) where the creditor fails to object to the confirmation of the proposed chapter 13 plan.[3] For example, in *In re Schultz*, 2007 WL 128827 (Bankr. E.D. Wis. Jan. 12, 2007), the court confirmed the debtor's balloon payment plan finding that the plan satisfied the requirements of section 1325(a)(5)(A). Despite the chapter 13 trustee's objection to confirmation, the court held that the plan was deemed accepted by the creditor because it did not object.

In some cases, a balloon payment plan might be viewed more favorably by a secured creditor than an alternative treatment that is clearly permissible under the Code. It is not surprising then that creditors sometimes choose not to object to balloon plans.[4] Where creditors have not objected to balloon provisions, the new equal monthly payment provision should not present a barrier to confirmation.

Real Property, Personal Property or Both?

Under the new language of 1325(a)(5)(B)(iii), whenever a plan proposes periodic payments, they must be in equal amounts and adequately protect the creditor's interest in the collateral if the claim is secured by personal property. Section 1325(a)(5)(B)(iii)(I) does not differentiate among types of secured claims. Rather, it refers only to "property to be distributed pursuant to this subsection." If the term "this subsection" refers generally to subsection (a)(5) of 1325 then the equal monthly payment provision applies to claims secured by both real property and personal property. However, if the phrase "this subsection" refers only to subsection (a)(5)(iii) then the requirements of (I) and (II) could be viewed as cumulative and applicable only to claims secured by personal

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[3] *See, e.g., In re* Andrews, 49 F.3d 1404, 1409 (9th Cir. 1995)(Here, § 1325(a)(5) is fulfilled because subsection (A) was satisfied when the holders of the secured claims failed to object. In most instances, failure to object translates into acceptance of the plan by the secured creditor."); *In re* Szostek, 886 F.2d 1405 (3d Cir. 1989).

[4] *See In re* Schultz, 2007 WL 128827 (Bankr. E.D. Wis. Jan. 12, 2007)(noting the lack of objection no great surprise since creditor would receive money sooner under balloon plan than it would under an alternative confirmable plan).

property.

The court in *In re Lemieux*, 347 B.R. 460 (Bankr. D. Mass. 2006), appears to have considered and rejected such an argument. In particular, the court stated because the word "if" precedes both subsection (I) and (II), the two clauses are independent of one another. Therefore, the explicit reference to personal property in section 1325(a)(5)(B)(iii)(II) did not serve to exclude claims secured by real property from treatment under section 1325(a)(B)(iii)(I).[5]

While this argument is not likely to win the day for debtors seeking to cure mortgage arrears through a balloon payment plan, it is nevertheless interesting to note that section 309(c) of BAPCPA, which adds section 1325(a)(5)(B)(iii)(I) is entitled "ADEQUATE PROTECTION OF LESSORS AND PURCHASE MONEY SECURED CREDITORS." Additionally, section 309 of BAPCPA deals almost exclusively with personal property. While there is little legislative history to clarify whether equal monthly payments applies to claims secured by real property, the pre-BAPCPA practices that were seen, by many, as abusive and for which 1325(a)(5)(B)(iii) was intended to remedy relate to car creditor payments, not mortgage lenders.[6]

<u>Obligations Maturing Before the End of Plan</u>

Section 1322(b)(2) permits debtors to modify the rights of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence. One exception to this anti-modification provision, however, can be found in section 1322(c)(2), which allows for the curing of mortgage loans that mature before the final payment on the plan is due.[7] Treatment of a secured claim under section

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[5] *See also In re* Hill, 2007 WL 499622 (Bankr. M.D.N.C. Feb. 12, 2007)("When the collateral in question is "personal property," these subsections must be read together; they require "equal monthly payments" to be made monthly, in equal amounts, and at the minimum level necessary to afford the secured creditor adequate protection. When the collateral is real property, subsection (II) does not apply and no adequate protection payments are required by Section 1325(a)(5)(B)").

[6] *See In re* DeSardi, 340 B.R. 790, 809 (Bankr. S.D. Tex. 2006); Richardo Kilpatrick, *Selected Creditor Issues Under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 79 Am. Bankr. L.J. 817, 835-36 (2005)(" In many instances, creditors with a security interest have been required to await payment on their secured claims until after payment of administrative expenses which include unpaid attorneys' fees. Further, Chapter 13 plans often provided for payment of the current mortgage, payment of the mortgage arrearages, and payments made pursuant to a lease and lease arrearages prior to payments on secured claims. This often resulted in uncompensated depreciation of collateral during the pendency of a Chapter 13 case. In the worst-case scenario, a creditor could wait as long as twenty-four months before receiving any distributions on an allowed secured claim.").

[7] In relevant part section 1322(c)(2) states:

> Notwithstanding subsection (b)(2) and applicable nonbankruptcy law…
>
> (2) in a case in which the last payment on the original payment schedule

1322(c)(2) is explicitly conditioned on compliance with section 1325(a)(5). As a result, the equal monthly payment provision applies to such a claim. In *In re Lemieux*, 347 B.R. 460 (Bankr. D. Mass. 2006), the court concluded, after considering this relationship between 1322(c) and 1325(a)(5), that the plain language of the statute precluded confirmation of a debtor's plan that proposed unequal periodic payments.

In *Lemieux*, the debtors used section 1322(c) to deal with two junior mortgages that would become payable during the term of the plan. In order to satisfy these secured claims, the debtors proposed a 36-month plan under which they would pay $1081 per month for the first 35 months with a final payment of $95,853 in the 36th month. Debtors stated that the final balloon payment would come from a refinancing. Finding the debtors' proposed plan violated the equal monthly payment provision of 1325(a)(5), the court denied confirmation. The court, however, specifically distinguished the facts presented in *Lemieux* from situations in which debtors might propose a single lump-sum payment or seek to cure arrears and maintain payments under section 1322(b)(5).

The One Payment Alternative

Notably, section 1325(a)(5)(B)(iii)(I) does not mandate periodic payments. It merely states that "if" periodic payments are provided for in the plan, they must be in equal monthly amounts. It would appear then that the new language does not preclude a plan providing for a single lump sum payment to a creditor.[8] While no court has addressed this issue directly, the *Lemieux* court did not rule out such a provision. The *Schultz* court also did not rule directly on the propriety of a single payment plan but suggests that such plans are incompatible where the debtor seeks to cure and maintain payments under section 1322(b)(5). The *Schultz* court noted that where ongoing monthly mortgage payments are required by the mortgage loan contract, a one-payment proposal would not result in the "maintenance of payments." Under both *Lemieux* and *Schultz* then, it appears that a debtor may be able to propose a single lump sum payment plan to address short-term obligations that become due before the end of the plan.

By contrast, the court in *In re Wagner*, 342 B.R. 766 (Bankr. W.D. Tenn. 2006), implicitly rejected the possibility of a one-payment plan altogether when it held that section 1325(a)(5)(B)(iii)(I) required equal monthly payments over the life of the plan. The *Wagner* court denied confirmation of the debtor's plan in which she proposed bi-weekly payments for 60 months to the trustee of $420.00, monthly "maintenance installments" on her mortgage for 23 months in the amount of $728.00, and a balloon payment for the balance due on the mortgage in month 24.

The *Wagner* court holding--that equal monthly payments must commence

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> 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 section 1325(a)(5) of this title.

[8] *See* 8 Collier on Bankruptcy ¶ 1325.06[3][b][ii][A]. Another possible view is that a balloon payment is not one of the "periodic payments," but rather comes after the periodic payments and therefore does not need to be equal.

immediately upon confirmation and continue until the allowed secured claim is paid in full--has been rejected by several other courts. For example, in *In re DeSardi*, 340 B.R. 790 (Bankr. S.D. Tex. 2006), the court held that section 1325(a)(5)(B)(iii)(I) required payments to be equal once they begin, and to continue to be equal until they cease. [9]

Must Cure and Maintenance Payments Be Equal?

A second exception to the anti-modification provision of section 1322(b)(2) is contained in section 1322(b)(5), which provides that the debtor's plan may "provide for the curing of any default within a reasonable period of time and maintenance of payments while the case is pending on any…secured claim on which the last payment is due after the date on which the final payment under the plan is due." This section allows debtors to cure a default on a long-term obligation without having to pay the entire debt balance before the end of the plan term. Unlike section 1322(c), section 1322(b)(5) does not specifically require compliance with section 1325(a)(5). The question then is whether secured claims dealt with under section 1322(b)(5) must nevertheless provide equal monthly payments.

In re Davis, 343 B.R. 326 (Bankr. M.D. Fla. 2006), the only decision that directly addresses the issue, holds that subsection 1325(a)(5)(b)(iii)(I) is inapplicable and that equal monthly payments are not required for the cure and maintenance of long-term debts. In *Davis*, the debtor relied upon subsection 1322(b)(5) to cure and maintain payments on her mortgage, the last payment for which was due after the due date of the final plan payment. Her plan proposed to pay the mortgage arrearage at the rate of $0.00 per month for months one through 10, and $122.23 per month for months 11 through 57.[10] After examining the interplay between section 1325(a)(5) and section 1322(b), the court held that section 1322(b)(5) provides an independent basis for treatment of long-term secured debt. The *Davis* court also found that the addition of section 1322(e),[11] following the Supreme Court's decision of *Rake v. Wade*,[12] had the effect of overriding section 1325(a)(5) when arrears on long-term debt are cured.[13] While the focus of

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[9] *See also In re* Hill, 2007 WL 499622, *5 (Bankr. M.D.N.C. Feb 12, 2007); *In re* Blevins, 2006 WL 2724153 (Bankr. E.D. Cal. Sept. 21, 2006)(equal monthly payments not required to be made over the life of the plan).
[10] Though the debtor in *Davis* did not propose a balloon payment plan, the reasoning of *Davis* would seem equally applicable where debtor proposes to cure a mortgage arrears in part through a balloon payment.
[11] Section 1322(e) provides that "Notwithstanding subsection (b)(2) of this section and section 506(b) and 1325(a)(5) of this title, if it is proposed in a plan to cure a default, the amount necessary to cure the default, shall be determined in accordance with the underlying agreement and applicable nonbankruptcy law."
[12] 508 U.S. 464, 113 S. Ct. 2187, 124 L. Ed. 2d 424 (1993).
[13] At least one commentator noted that in enacting section 1322(e), Congress appears to have adopted the reasoning of pre-*Rake* cases that distinguish between cure and modification. Baxter Dunaway, *Effect of the Bankruptcy Reform Act of 1994 on Real Estate*, 30 Real Prop. Prob. & Tr. J. 601, 612 (Winter 1996). *See also In re* Landmark

section 1322(e) was to eliminate the present value requirement of section 1325(a)(5)(B)(ii), the statute has been construed more broadly since the introductory language of the section is not limited to 1325(a)(5)(B)(ii) . Other courts, like *Davis*, have found that section 1325(a)(5) has no applicability in the cure situation.[14]

The court in *Schultz* reached the opposite conclusion relying on *Wagner* and finding that cure and maintenance payments are subject to the equal monthly payment provision of 1325(a)(5)(B)(iii)(I). Curiously, the court in *Schultz* engages in a lengthy discussion of the equal monthly payment requirement even though the creditor did not object to the debtor's plan, and the court found that section 1325(a)(5)(A) was satisfied. In *Schultz*, the debtor's plan provided for monthly payments of $533.24 per month representing principal and interest on a mortgage loan with the unpaid balance of $71,195.68 due at the end of 60 months. The final scheduled payment under the debtor's mortgage loan extended beyond the term of the plan, but the balloon payment proposed by the debtor would have paid the loan in full. Though the debtor's proposal to pay the mortgage loan in full differed from the facts of the *Davis* case, where the debtor proposed to simply cure and maintain payments, the *Schultz* court found this distinction without a difference. The *Schultz* court found that mortgage creditors' claims, regardless of whether the debtor intends to cure or pay in full, are still "allowed secured claims" entitled to treatment under section 1325(a)(5). The court did not address the fact that 1322(b)(5), unlike 1322(c)(2), does not explicitly require modification pursuant to section 1325(a)(5). Nor did the *Schultz* court address the effect of 1322(e) which clearly limits the applicability of 1325(a)(5) to secured claims dealt with under section 1322(b)(5).

Adjusting Mortgage Payments

No case has yet to address the applicability of the equal monthly payment provision to adjustable rate mortgage (ARM) loans or other mortgage loans that may have differing monthly payments over time. While preemptively delving into the equal monthly payment debate, the *Schultz* court chose not to wade into the quagmire created by an adjustable rate mortgage. The court concedes, however, that a mortgage note that provides for interest adjustments might make the payments "not equal."[15] The same could be true for mortgage loans that require escrow payments. For the majority of home loans escrow payment amounts are analyzed and adjusted annually.[16] Fluctuation in mortgage payments required by the underlying contract may not be a problem if 1322(b)(5) permits the debtor to cure and maintain payments independently of the

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Fin. Servs. V. Hall, 918 F.2d 1150, 1154 (4th Cir. 1990)("The cure of mortgage or other long term debt is a distinct means of treating the claim of some secured creditors. Like a cramdown, it may be imposed on creditors without their consent. It operates, however, in an entirely different manner."); Shearson Lehmon Mortg. Corp., v. Laguna, 944 F.2d 542 (9th Cir. 1991).

[14] *See In re* Harko, 211 B.R. 116 (B.A.P. 2d Cir. 1997)("the introductory language, which specifically references §§ 506(b) and 1325(a)(5), makes clear that these sections have no applicability in a cure situation").

[15] *In re Schultz*, 2007 WL 128827 (Bankr. E.D. Wis. Jan. 12, 2007).

[16] *See* 12 U.S.C. § 2609; Reg. X., 24 C.F.R. § 3500.17.

requirements of 1325(a)(5). However, if courts find that section 1325(a)(5)(B)(iii)(I) is applicable to cure and maintenance payments under 1322(b)(5), it would difficult, if not impossible, for debtors to propose a plan that satisfied the requirements of 1322(b) and 1325(a)(5).

Plan Modification

Another issue that has yet to be addressed by any court is the effect of the equal monthly payment requirement on plan modification. Section 1329(a)(1) permits a modified plan to "increase or reduce the amount of payments on claims of a particular class." Section 1329(a)(2) allows a modified plan to "extend or reduce the time for such payments…" However, section 1329(b)(1) requires compliance with section 1325(a). It seems unlikely that the addition of the equal monthly payment provision was intended to limit modification of plans pursuant to section 1329. A better interpretation of the relationship between sections 1325(a)(5)(B)(iii)(I) and 1329 is that where section 1325(a)(5)(B)(iii)(I) applies debtors may modify their plans to increase or reduce the amount of the equal monthly payment, but that the new payment amount must remain equal throughout the remainder of the plan.

Feasibility Still Matters.

Even if the equal monthly payment provision is found not to apply to a debtor's situation, a balloon payment plan will still scrutinized to determine whether it is feasible. Section 1325(a)(6) requires debtor to demonstrate that they are "able to make all payment under the plan and to comply with the plan." Under section 1325(a)(6), most courts have framed the feasibility inquiry with respect to balloon payments as one that looks to the totality of the circumstances. While the Bankruptcy Code does not require absolute certainty that a balloon payment will be made, the likelihood of such a payment must be based on more that pure speculation.[17] Courts have enumerated several factors to be considered in balloon payment cases:

1) the equity in the property at the time of filing;
2) the future earning capacity of the debtor;
3) the future disposable income of the debtor;
4) whether the plan provides for the payment of interest to the secured creditor over the life of the plan;
5) whether the plan provides for payment of recurring charges against the property, including insurance, local property taxes and utility charges; and
6) whether the plan provides for substantial payments to the secured creditor which will significantly reduce the debt and enhance the prospects for refinancing at the end of the plan.

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[17] *See In re* Wagner, 259 B.R. 694, 701 (B.A.P. 8th Cir. 2001); *In re* Fanatasia, 211 B.R. 420, 423 (B.A.P. 1st Cir. 1997).

If these factors weigh in the debtors favor, a balloon payment plan may still be viable under a number of different theories discussed above.