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Bankruptcy—Chapter 13—Bifurcation of Undersecured Claims Secured Only by Residential Real Estate Mortgages Is Not Allowed. *Nobelman v. American Savings Bank (In re Nobelman)*, 113 S. Ct. 2106 (1993).

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BANKRUPTCY—CHAPTER 13—BIFURCATION OF UNDERSECURED CLAIMS SECURED ONLY BY RESIDENTIAL REAL ESTATE MORTGAGES IS NOT ALLOWED. *Nobelman v. American Savings Bank (In re Nobelman)*, 113 S. Ct. 2106 (1993).

I. INTRODUCTION

In *Nobelman v. American Savings Bank (In re Nobelman)*,¹ the United States Supreme Court resolved a split among the United States Circuit Courts of Appeal concerning whether a debtor who files for bankruptcy protection under Chapter 13 of the Bankruptcy Code² can bifurcate a claim arising out of a mortgage secured only by her home into a secured claim for the amount of the collateral's fair market value and an unsecured claim for the excess of the amount due under the terms of the loan over the fair market value.³ In *Nobelman*, the Supreme Court held that section 1322(b)(2) of the Bankruptcy Code⁴ prohibits the bifurcation generally allowed by section 506(a)⁵ in a Chapter 13 plan if the claim the debtor seeks to bifurcate is secured only by an interest in residential real property that comprises her principal residence.⁶

In general, Chapter 13 allows an individual with regular income⁷ to obtain a discharge of nearly all her debts⁸ while retaining most

1. *Nobelman v. American Sav. Bank (In re Nobelman)*, 113 S. Ct. 2106 (1993). It should be noted for research purposes that the Nobelmans' name was misspelled in both the District Court's and the Fifth Circuit's decisions as "Nobleman."

2. "Bankruptcy Code" refers to the Bankruptcy Reform Act of 1978 as amended and codified in 11 U.S.C. §§ 101-1330 (1988). "Chapter 13" refers to 11 U.S.C. §§ 1301-1330 (1988).

3. *Nobelman*, 113 S. Ct. at 2109.

4. 11 U.S.C. § 1322(b)(2) (1988). Section 1322(b)(2) provides: "[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, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims. . . ." *Id.*

5. *Id.* § 506(a). Section 506(a) provides:

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.

Id. 11 U.S.C. § 103 (1988) provides that Chapters 1, 3, and 5 are applicable to Chapter 13 cases.

6. *Nobelman*, 113 S. Ct. at 2111.

7. "Only an individual with regular income . . . may be a debtor under Chapter 13 of this title. . . ." 11 U.S.C. § 109(e) (1988).

8. "As soon as practicable after completion by the debtor of all payments under the plan . . . the court shall grant the debtor a discharge of all debts provided

of her assets.⁹ To obtain such relief, a Chapter 13 debtor must voluntarily¹⁰ file a debt restructuring plan.¹¹ The plan must provide for payments out of the future earnings of the debtor for a period of three to five years.¹² Secured creditors are generally paid in full up to the value of their claims, and unsecured creditors are paid a sum at least equal to the amount they would receive under a Chapter 7 liquidation.¹³ If the bankruptcy court confirms the plan, then a debtor who makes all payments under the plan obtains a discharge of all debts provided for in the plan except for debts for which the last payment was due after the completion of the plan or debts owed for alimony, maintenance and support obligations, student loans, or injury to another from driving under the influence of intoxicants.¹⁴ For a Chapter 13 plan to be confirmed, the debtor must convince the holders of each allowed fully secured claim to accept the plan, provide for payments under the plan equal to the value of such claim, and allow the creditor to either retain her lien securing the claim, or surrender the property securing it to the creditor.¹⁵

In structuring her Chapter 13 plan, the debtor may generally bifurcate the claims of undersecured creditors. Bifurcation¹⁶ is the

for by the plan." *Id.* § 1328(a).

One of the incentives for filing a Chapter 13 plan as opposed to Chapter 7 or 11 is the so-called superdischarge available under Chapter 13. Under Chapters 7 and 11, many types of debt are nondischargeable. *See id.* § 502. In a Chapter 13 bankruptcy, however, virtually all of the debtor's debts are dischargeable. *See id.* § 1328.

9. Unless the plan or the order confirming the plan provides otherwise, the confirmation of a plan vests in the debtor all of the property of the estate free and clear of any claim or interest of any creditor provided for in the plan. *Id.* §§ 1306(b), 1327(b)-(c). However, a debtor may surrender secured property to a creditor in lieu of paying her the value of her claim. *Id.* § 1325(a)(5)(C).

10. Involuntary provisions are not possible under Chapter 13. *See id.* § 303(a).

11. *Id.* § 1321. "The debtor shall file a plan." *Id.*

12. *Id.* § 1322(a)(1), (c). Because a plan must be proposed in good faith to be confirmed, the debtor must usually specify that all her disposable income be applied to payment of the creditors under the plan. *Id.* § 1325(a)(3). Bankruptcy plans normally span a three year period, but the court may approve a plan for up to five years. *Id.* § 1322(c).

13. The plan may provide for the partial or full payment of unsecured creditors out of future wages or other income of the debtor over a three to five year period. *Id.* § 1322(a), (c). Under the Nobelmanns' plan, the unsecured creditors would have received nothing. *Nobelmann v. American Sav. Bank (In re Nobelmann)*, 113 S. Ct. 2106, 2109 (1993).

14. 11 U.S.C. § 1328 (1988). The key to a Chapter 13 bankruptcy is confirmation of the plan pursuant to 11 U.S.C. § 1325. Once a plan is confirmed, the provisions bind the debtor and each creditor regardless of whether the claim of the creditor is provided for in the plan, and whether or not the creditor has objected to, has accepted, or has rejected the plan. *Id.* § 1327(a).

15. *Id.* § 1325(a)(5).

16. While bifurcation is the terminology used by the Supreme Court, other

process described in section 506(a) through which a creditor's undersecured¹⁷ claim is split into two separate claims: a secured claim for the amount of the value of the collateral and an unsecured claim for the amount of the excess due under the note over the value of the collateral.¹⁸ The debtor's plan may then provide for a discharge of the unsecured portion of the debt for only a percentage of the amount due.¹⁹

Creditors whose claims are secured only by an interest in the debtor's primary residence, however, enjoy a measure of protection against bifurcation under section 1322(b)(2).²⁰ The interpretation of the scope of this protection resulted in a split among the circuits. Four circuits held that the scope of protection under section 1322(b)(2) was narrow and allowed bifurcation of the claims for undersecured home mortgages.²¹ In *Nobelman*, however, the Fifth Circuit held that the protection granted by that section was broad enough to prohibit the bifurcation of claims secured only by home mortgages.²² The Supreme Court agreed with the Fifth Circuit view and affirmed the circuit court's decision in *Nobelman* that the scope of protection provided by section 1322(b)(2) included protection from bifurcation under section 506.²³

courts have referred to the process as "cram down," "lien stripping," and "strip down."

17. "Undersecured" means that the market value of the collateral is less than the obligation that the collateral secures. See *United Sav. Ass'n v. Timbers of Inwood Forest Assoc. (In re Timbers of Inwood Assoc.)*, 793 F.2d 1380, 1381 (5th Cir. 1986).

18. 11 U.S.C. § 506 (1988).

19. *Id.* § 1322.

20. In his concurring opinion in *Nobelman v. American Exchange Bank (In re Nobelman)*, 113 S.Ct. 2106 (1993), Justice Stevens pointed out that:

At first blush it seems somewhat strange that the Bankruptcy Code should provide less protection to an individual's interest in retaining possession of his or her home than of other assets. The anomaly is, however, explained by the legislative history indicating that favorable treatment of residential mortgagees was intended to encourage the flow of capital into the home lending market.

Id. at 211-12. (Stevens, J., concurring) (citations omitted).

21. See *Bellamy v. Federal Home Loan Mortgage Corp. (In re Bellamy)*, 962 F.2d 176 (2d Cir. 1992); *Eastland Mortgage Co. v. Hart (In re Hart)*, 923 F.2d 1410 (10th Cir. 1991); *Wilson v. Commonwealth Mortgage Corp.*, 895 F.2d 123 (3d Cir. 1990); *Hougland v. Lomas & Nettleton Co. (In re Hougland)*, 886 F.2d 1182 (9th Cir. 1989); see also *Nobelman v. American Sav. Bank (In re Nobelman)*, 113 S. Ct. 2106, 2109 n.2 (1993).

22. *Nobleman v. American Sav. Bank (In re Nobleman)*, 968 F.2d 483, 489 (5th Cir. 1992).

23. *Nobelman*, 113 S. Ct. at 2111.

II. FACTS

Leonard and Harriet Nobelman borrowed \$68,250 from American Savings Bank (hereinafter "American") on July 21, 1984, to purchase a condominium in Dallas, Texas.²⁴ The note was secured by the condominium,²⁵ which was the Nobelmans' principal residence.²⁶ On August 6, 1990, the Nobelmans voluntarily filed a petition for bankruptcy under Chapter 13.²⁷ American filed a proof of claim²⁸ for \$71,355.04 with the bankruptcy court which included the principal, interest, and fees owed on the note.²⁹ The Chapter 13 plan proposed by the Nobelmans would have bifurcated American's claim into a secured portion equal to the fair market value of the property and an unsecured portion which, under the plan, would be discharged without payment.³⁰ Under the Nobelmans' plan, American would have received only \$23,500 plus prepetition arrearages as payment for its secured claim, but the Nobelmans would have kept their condominium and enjoyed a discharge of the remainder of the debt.³¹ The Nobelmans asserted that 11 U.S.C. § 506(a) authorized the reduction of American's secured claim to the fair market value of the property, \$23,500.³²

American and the Chapter 13 trustee objected to the Nobelmans' plan and argued that 11 U.S.C. § 1322(b)(2) prohibited the bifurcation since it impermissibly modified Americans' rights as a holder of a claim secured only by real property comprising the debtor's

24. *Id.* at 2108.

25. The note was also secured by a security interest in an undivided .67% interest in the common areas of the condominium complex, escrow funds, proceeds of hazard insurance, and rents. *Nobleman v. American Sav. Bank (In re Nobleman)*, 129 B.R. 98, 99 (Bankr. N.D. Tex. 1991). The Supreme Court, however, did not discuss this additional security, and therefore did not definitively establish whether a note such as this even qualifies for the protection § 1322(b)(2) offers. See *Hammond v. Commonwealth Mortgage Co. of Am.*, 156 B.R. 943 (Bankr. E.D. Pa. 1993), for a complete discussion of the effect of the *Nobleman* decision on Third Circuit precedents holding that any interest other than residential real property is sufficient to remove a claim from the ambit of § 1322(b)(2)'s protection.

26. *Nobleman*, 129 B.R. at 99.

27. *Id.*

28. A proof of claim is a sworn statement filed in a bankruptcy proceeding by a creditor that sets forth the amount of and basis for the claim. BLACK'S LAW DICTIONARY 1215 (6th ed. 1990).

29. *Nobleman*, 129 B.R. at 99.

30. *Id.*

31. *Nobleman v. American Sav. Bank (In re Nobelman)*, 113 S. Ct. 2106, 2108-09 (1993).

32. This amount was uncontroverted at trial. *Id.* at 2108-09.

principal residence.³³ The bankruptcy court agreed and refused to confirm the plan.³⁴ The District Court for the Northern District of Texas,³⁵ the United States Court of Appeals for the Fifth Circuit,³⁶ and the Supreme Court of the United States affirmed.³⁷

III. HISTORICAL DEVELOPMENT

The United States Constitution expressly grants Congress the power to establish Bankruptcy laws.³⁸ Pursuant to this power, Congress enacted the Bankruptcy Act of 1898.³⁹ When that Act proved insufficient to cope with emerging problems, Congress appointed the Commission on the Bankruptcy Laws of the United States.⁴⁰ After considering the advice of the Commission, Congress enacted the current version of the Bankruptcy Code in 1978.⁴¹

The language of section 1322(b)(2)⁴² of the Bankruptcy Code as enacted by Congress represents a compromise agreement between the House and Senate versions of this section.⁴³ The House's original version of section 1322(b)(2) would have allowed a Chapter 13 plan to modify the rights of holders of secured and unsecured claims.⁴⁴ The Senate's version would have prevented the modification of all claims secured only by mortgages on real property.⁴⁵ The version finally enacted and currently in effect is the result of a number of

33. *Nobleman*, 129 B.R. at 99.

34. *Id.* at 99.

35. *Id.* at 104.

36. *Nobleman v. American Sav. Bank (In re Nobleman)*, 968 F.2d 483, 489 (5th Cir. 1992).

37. *Nobelman v. American Sav. Bank (In re Nobelman)*, 113 S. Ct. 2106, 2111 (1993).

38. "The Congress shall have Power to . . . establish . . . uniform Laws on the subject of Bankruptcies throughout the United States." U.S. CONST. art. I, § 8, cl. 4.

39. The National Bankruptcy Act of 1898, ch. 541, 30 Stat. 544, amended by Act of June 22, 1938, ch. 575, 52 Stat. 840, repealed by Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549.

40. Klee, *Legislative History of the New Bankruptcy Law*, 28 DEPAUL L. REV. 941, 942-43 (1979).

41. *Id.*

42. *See supra* note 4.

43. H.R. REP. No. 595, 95th Cong., 1st Sess. (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963. ("Section 1322(b)(2) of the House amendment represents a compromise agreement between similar provisions in the House bill and Senate amendment. Under the House amendment, the plan may modify the rights of holders of secured claims other than a claim secured by a security interest in real property that is the debtor's principal residence.")

44. H.R. 8200, 95th Cong., 1st Sess. (1977).

45. S. 2266, 95th Cong., 2d Sess. (1978).

floor amendments agreed upon by both houses.⁴⁶ Although the legislative history clearly shows that section 1322(b)(2) was a compromise between sharply contrasting proposals, it does not clearly express the intent of Congress in enacting the current statutory language regarding bifurcation of claims secured by home mortgages.⁴⁷ It is this lack of clarity in both the statutory text and the legislative history that led to the split in the circuit courts of appeals⁴⁸ that the Supreme Court resolved in *Nobelman*.

A. *The Majority View: Bifurcation of Claims Arising Out of Undersecured Home Mortgages Was Allowed.*

Prior to *Nobelman*, the majority view was that bifurcation of claims arising from undersecured home mortgages was not prohibited by section 1322(b)(2).⁴⁹ This view was first adopted at the Court of Appeals level by the Ninth Circuit in *Houglan v. Lomas & Nettleton Co. (In Re Houglan)*.⁵⁰ The rationale behind the *Houglan* decision was followed by many of the courts adopting this view, and it accurately portrays what was the majority's stance.

The court in *Houglan* employed a technical, grammatical analysis in interpreting section 1322(b)(2).⁵¹ According to the *Houglan* court,

46. *Grubbs v. Houston First Am. Sav. Ass'n*, 730 F.2d 236, 246 (5th Cir. 1984).

47. *Nobleman v. American Sav. Bank (In re Nobleman)*, 129 B.R. 98, 103 (Bankr. N.D. Tex. 1991). For a complete discussion of the legislative history of § 1322(b)(2) and the possible interpretations thereof, see *Grubbs*, 730 F.2d 236; *Goins v. Diamond Mortgage Corp.*, 119 B.R. 156 (Bankr. N.D. Ill. 1990); 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 (1993); Erik D. Klingenberg, *Strip Down of Home Mortgages: Undressing 11 U.S.C. § 1322(b)(2)*, 66 ST. JOHN'S L. REV. 443 (1992).

48. The Fifth Circuit held that bifurcation of undersecured home mortgages was prohibited. *Nobleman v. American Sav. Bank (In re Nobleman)*, 968 F.2d 483 (5th Cir. 1992). Four other circuits had held that bifurcation of undersecured home mortgages was allowed. See *Bellamy v. Federal Home Loan Mortgage Corp. (In re Bellamy)*, 962 F.2d 176 (2d Cir. 1992); *Eastland Mortgage Co. v. Hart (In re Hart)*, 923 F.2d 1410 (10th Cir. 1991); *Wilson v. Commonwealth Mortgage Corp.*, 895 F.2d 123 (3d Cir. 1990); *Houglan v. Lomas & Nettleton Co. (In re Houglan)*, 886 F.2d 1182 (9th Cir. 1989).

49. The Second, Third, Ninth, and Tenth Circuits followed this approach. See *Bellamy*, 962 F.2d 176; *Wilson*, 895 F.2d 123; *Houglan*, 886 F.2d 1182; *Hart*, 923 F.2d 1410 (10th Cir. 1991). Several bankruptcy and district courts in other circuits also agreed with this position. See, e.g., *Richards v. Citicorp Mortgage, Inc.*, 151 B.R. 8 (Bankr. D. Mass. 1993); *In re Jones*, 152 B.R. 155 (Bankr. E.D. Mich. 1993); *Franklin v. Union Mortgage Co.*, 126 B.R. 702 (Bankr. N.D. Miss. 1991); *In re Gadson*, 114 B.R. 453 (Bankr. E.D. Va. 1990); *In re DeMoff*, 109 B.R. 902 (Bankr. N.D. Ind. 1989).

50. *Houglan v. Lomas & Nettleton Co. (In re Houglan)*, 886 F.2d 1182 (9th Cir. 1989).

51. *Id.* at 1183-84.

it is the textual language of the statute itself that defines the search for statutory meaning.⁵² The court noted that there was no real need to consult the legislative history because the statute is internally consistent and can be interpreted without extrinsic aids.⁵³ The *Hougland* court also determined that, even if the legislative history is consulted, it only warrants the narrow and ambiguous inference that Congress intended to provide some benefit to residential real estate lenders.⁵⁴

In interpreting the language of section 1322(b)(2), the first step the *Hougland* court took was to try to define "secured claim" and "unsecured claim" since these terms were at the heart of the controversy.⁵⁵ The court held that the terms "secured claim" and "unsecured claim" in section 1322(b)(2) should carry the meaning ascribed to them by section 506(a)⁵⁶ because section 506 is a definitional section that applies to Chapter 13 cases.⁵⁷ Section 506(a) limits a secured claim to the value of the collateral securing the lien and treats the remainder as an unsecured claim.⁵⁸ The court then applied these definitions to the terms as they are used in section 1322(b)(2) and concluded that the clear language of the statute allows bifurcation of claims arising from home mortgages.⁵⁹

According to the *Hougland* court, the clause in section 1322(b)(2) that provides "other than a claim secured only by a security interest in real property that is the debtor's principal residence" (hereinafter the "other than" clause)⁶⁰ logically modifies "secured claim" since that is the closest referent.⁶¹ The court determined that, given the structure of the section, it would be most unusual if the "other

52. "[T]he quest for meaning should begin and end 'with the language of the statute itself.'" *Id.* at 1183 (quoting *United States v. Ron Pair Enter.*, 109 S. Ct. 1026, 1030 (1989)).

53. "[S]ince . . . the statute is internally consistent and can be construed without the use of outside aids, there is no real need to concentrate on the legislative history." *Hougland*, 886 F.2d at 1185. It should be noted that some of the other courts of appeals' decisions addressing this issue did look to the legislative history to determine legislative intent, but found no indication of the proper interpretation from that history. *See, e.g., Bellamy*, 962 F.2d at 181-82.

54. *Hougland*, 886 F.2d at 1185.

55. *Id.* at 1183.

56. *Id.* at 1183 (quoting *United States v. Ron Pair Enter.*, 109 S. Ct. 1026, 1029 (1989)). Section 506(a) applies to Chapter 13 proceedings. *See* 11 U.S.C. § 103(a) (1988).

57. *Hougland*, 886 F.2d at 1183-84.

58. 11 U.S.C. § 506(a) (1988).

59. For the text of § 1322(b)(2) *see supra* note 4.

60. 11 U.S.C. § 1322(b)(2) (1988).

61. *Hougland*, 886 F.2d at 1184.

than" clause modified either "unsecured claim" or the whole sentence.⁶² The court held that the use of commas to set apart the "other than" clause did not affect its decision.⁶³

The *Houglund* court also found support for its interpretation in reading the statute as a whole.⁶⁴ According to the court, its interpretation avoids the conflict that inevitably arises between section 1322(b)(2) and section 506(a) from any other interpretation.⁶⁵ In fact, the court held that it was bound to read the sections in such a way that, if possible, they would be harmonious when read in the context of the whole statute.⁶⁶

While the *Houglund* court did not address public policy issues, it is possible that policy considerations influenced its decision. Other courts adopting the majority view were also, presumably, motivated by policy concerns. Although the circuit courts' decisions did not specifically discuss these policy concerns, the courts hinted at such concerns by discussing the broad policy of the "fresh start" goals of Chapter 13.⁶⁷ These policy concerns are grounded in the idea that it simply is not fair to deny bifurcation since it will result in the secured creditor being paid as much or more than she would receive in a Chapter 7 liquidation.⁶⁸ In fact, if bifurcation were not allowed, it is possible that the Chapter 13 debtor would simply abandon her homestead.⁶⁹ The creditor would then have to obtain relief from the automatic stay and foreclose on the property.⁷⁰ The creditor would, presumably, only be able to sell the property for, at most, its fair market value, and the resulting deficiency would be unsecured.⁷¹ The debtor would then include the unsecured claim in his Chapter 13 bankruptcy plan and obtain a discharge.⁷² Under this scenario, the creditor would receive the same payment as if

62. *Id.* at 1184.

63. *Id.*

64. *Id.*

65. *Id.*

66. *Id.*

67. *See, e.g.,* Bellamy v. Federal Home Loan Mortgage Corp. (*In re Bellamy*), 962 F.2d 176, 181 (2d Cir. 1992).

68. *See* David A. Wisniewski, Note, *Residential Mortgages Under Chapter 13 of the Bankruptcy Code: The Increasing Case Against Cramdown After Dewsnup v. Timm*, 46 VAND. L. REV. 1031 (1993).

69. Brief on the Merits for Petitioners, Leonard Nobelman and Harriet Nobelman at 1, Nobelman v. American Sav. Bank (*In re Nobelman*), 113 S. Ct. 2106 (1993) (No. 92-641).

70. *Id.*

71. *Id.*

72. *Id.*

bifurcation were allowed, but the debtor loses his home.⁷³ Undoubtedly, many courts found this result unpalatable.

B. *The Minority View: Section 1322(b)(2) Prohibited the Bifurcation of Claims Arising From Undersecured Home Mortgages into Secured and Unsecured Claims.*

Until *Nobleman*,⁷⁴ no court of appeals had adopted the view that section 1322(b)(2) prohibited the bifurcation of a claim arising from an undersecured home mortgage into secured and unsecured components. Several bankruptcy courts, however, had adopted this interpretation.⁷⁵ These courts rejected the majority position as an "overly technocratic" approach to analyzing the text of sections 1322(b)(2) and (b)(5), and relating it to section 506(a).⁷⁶ In *In re Kaczmarczyk*,⁷⁷ the court discussed four basic rationales used by the courts adopting the minority's interpretation of section 1322(b)(2).

One rationale, employed by the court in *Kaczmarczyk*, is that the non-bifurcation construction is more consistent with the Bankruptcy Code's historical treatment of secured claims.⁷⁸ Under the Bankruptcy Code's predecessor, the Bankruptcy Act, a Chapter 13 plan could not deal with any claim secured by an estate in real property.⁷⁹ Because the Bankruptcy Code was enacted against this background, the court concluded that the basic rule that a claim

73. *Id.* See also Wisniewski, *supra* note 68.

74. *Nobleman v. American Sav. Bank (In re Nobleman)*, 968 F.2d 483 (5th Cir. 1992).

75. See, e.g., *In re Hernandez*, 149 B.R. 441 (Bankr. E.D. Tex. 1993); *In re Vines*, 153 B.R. 345 (Bankr. M.D. Ala. 1993); *In re Strober*, 136 B.R. 614 (Bankr. E.D.N.Y. 1992); *United Co. Fin. Corp. v. Davis*, 148 B.R. 16 (Bankr. W.D. La. 1992); *In re Doss*, 143 B.R. 952 (Bankr. E.D. Okla. 1992); *In re Davidoff*, 136 B.R. 567 (Bankr. M.D. Fla. 1992); *In re Burgess*, 138 B.R. 56 (Bankr. W.D. Wis. 1991); *In re Etchin*, 128 B.R. 662 (Bankr. W.D. Wisc. 1991); *In re Hynson*, 66 B.R. 246 (Bankr. D.N.J. 1986). This view seems to be the approach taken by the bankruptcy courts in the Eighth Circuit. See *In re Hussman*, 133 B.R. 490 (Bankr. D. Minn. 1991); *In re Sauber*, 115 B.R. 197 (Bankr. D. Minn. 1990); *In re Kaczmarczyk*, 107 B.R. 200 (Bankr. D. Neb. 1989); and *In re Russell*, 93 B.R. 703 (Bankr. D.N.D. 1988).

76. *Sauber*, 115 B.R. at 199. The court also criticized the approach taken by the Ninth Circuit in *Houglund* saying, "[a]lthough ostensibly undertaken in search of the plain meaning of these statutes, that meaning, and the proper setting of the statutes in the context of the overall scheme of the Code, is as clearly missed as the proverbial forest might be missed in examining the trees." *Id.*

77. *In re Kaczmarczyk*, 107 B.R. 200 (Bankr. D. Neb. 1989).

78. *Id.* at 202.

79. *Id.* at 202-03.

secured by real property cannot be dealt with under the plan continues except as explicitly changed by the Bankruptcy Code.⁸⁰ Because Congress did not explicitly change the treatment of claims secured by a mortgage on the debtor's principal residence, the court concluded that Congress intended a continuity of treatment.⁸¹ This led the court to the conclusion that section 1322(b)(2) prohibits the bifurcation of home mortgages.⁸²

A second rationale used by some courts in holding that the bifurcation of claims secured only by home mortgages is forbidden is that the legislative history indicates that Congress intended to prohibit such bifurcation.⁸³ These decisions focus on the compromise between the House and Senate bills.⁸⁴ They hold that the compromise prohibits a Chapter 13 plan from modifying claims secured only by the debtor's principal residence, but does not specifically limit the protection to a secured claim.⁸⁵

A third rationale is that the plain meaning of section 1322(b)(2) prohibits the bifurcation.⁸⁶ The plain language of the statute prohibits the modification of a claim secured only by a debtor's principal residence.⁸⁷ The Bankruptcy Code, in section 101(5)(a),⁸⁸ defines a claim as the right to payment whether secured or unsecured.⁸⁹ Since the claim referred to in section 1322(b)(2) can be either secured or unsecured, the protection extends to even undersecured mortgages.⁹⁰

The fourth rationale employed by courts in holding that section 1322(b)(2) controls over section 506(a) is *ejusdem generis*, a tenet of statutory construction.⁹¹ The application of this tenet to section 506(a), which is general in nature, and section 1322(a)(2), which is specific, would dictate that, if there is a conflict between the two sections, section 1322(b)(2) controls.⁹² Therefore, bifurcation of the claim secured by the debtor's home mortgage is prohibited.⁹³

80. *Id.* at 203.

81. *Id.*

82. *Id.*

83. *Id.* at 202.

84. *Id.*

85. *Id.*

86. *Id.*

87. *In re Russell*, 93 B.R. 703, 705 (Bankr. D.N.D. 1988).

88. 11 U.S.C. § 101(5)(a) (1994).

89. *Russell*, 93 B.R. at 705.

90. *Id.*

91. See *Kaczmarczyk*, 107 B.R. at 202. *Ejusdem generis* is a canon of statutory construction which dictates that, if there is both general and specific language that conflicts but seems applicable to a given situation, the specific language governs. BLACK'S LAW DICTIONARY 517 (6th ed. 1990).

92. *Kaczmarczyk*, 107 B.R. at 202.

93. *Id.*

IV. ANALYSIS OF THE COURT IN NOBELMAN

In *Nobelman v. American Savings Bank* (In re Nobelman),⁹⁴ the United States Supreme Court resolved the issue of whether undersecured claims secured only by an interest in the real property comprising the debtor's principal residence may be bifurcated into secured and unsecured claims pursuant to section 506(a) and modified with respect to the unsecured portion under section 1322.⁹⁵ The Court decided that such bifurcation is prohibited by section 1322(b)(2) based primarily on a literal grammatical analysis of the distinction between "rights" and "claims."⁹⁶

American argued that the plan proposed by the Nobelmans impermissibly modified its rights as a homestead mortgagee.⁹⁷ The Nobelmans claimed that their plan did not modify American's rights because those rights are defined by the status of the claim as determined by section 506(a).⁹⁸ The Court held that the proper application of section 506(a) is to determine whether the creditor holds a secured claim.⁹⁹ The fact that a portion of the creditor's claim is thus rendered unsecured does not mean that the protected rights of the creditor are limited by the value of its secured claim.¹⁰⁰ Instead, the Court held that if a creditor holds a claim that is secured only by an interest in the debtor's principal residence, even if it is undersecured, all of the creditor's contractual rights are protected.¹⁰¹

The Court turned to state law to determine what rights American possessed that were protected by section 1322(b)(2).¹⁰² The rights that the Court held to be protected included the rights: To have the principal paid back over a fixed term in monthly installments bearing specified rates of interest; to keep its lien on the property until the debtor pays in full; to accelerate the maturity of the loan upon default; to foreclose and sell; and to recover any deficiency remaining after the foreclosure.¹⁰³ The Court held that these rights could not be modified by the Chapter 13 plan.¹⁰⁴

94. *Nobelman v. American Sav. Bank* (In re Nobelman), 113 S. Ct. 2106 (1993).

95. *Id.* at 2106.

96. *Id.* at 2110.

97. *Id.* at 2109.

98. *Id.*

99. *Id.* at 2110.

100. *Id.*

101. *Id.*

102. *Id.*

103. *Id.*

104. *Id.*

In reaching this decision, the Court rejected the grammatical analysis used by the court in *Houglund*.¹⁰⁵ The Court acknowledged that the interpretation given by the *Houglund* court "is quite sensible as a matter of grammar."¹⁰⁶ It found, however, that the more persuasive reading is one that applies the broad definition of claim set forth in section 101(5),¹⁰⁷ which includes secured and unsecured rights to payment.¹⁰⁸ The Court also acknowledged the practical impossibility of modifying the rights with respect to the unsecured component without modifying the rights associated with the secured component as well.¹⁰⁹ Thus, the Supreme Court concluded that a debtor cannot bifurcate claims secured by home mortgages in a Chapter 13 bankruptcy plan.¹¹⁰

In his concurring opinion, Justice Stevens indicated that the legislative history of section 1322(b)(2) explained the seemingly bizarre policy of affording a debtor less protection for his homestead than for his other assets.¹¹¹ In Justice Stevens's opinion, the legislative history suggested that Congress afforded the extra protection to home mortgage lenders to encourage growth in that market.¹¹²

V. SIGNIFICANCE

The most immediate impact of *Nobelman v. American Savings Bank* (In re *Nobelman*) is that it changed the law of bankruptcy in at least twenty-one states by prohibiting the bifurcation of claims secured by home mortgages in Chapter 13 bankruptcies.¹¹³ As a result, the debtors in these jurisdictions considering Chapter 13 may now find it more difficult to save their homes. Indeed, debtors faced with a similar situation to that which the Nobelmans encountered may well opt for a solution like the one the Nobelmans' attorney, Philip I. Palmer, Jr., foresaw the Nobelmans taking if the Supreme

105. *Id.* at 2111.

106. *Id.*

107. 11 U.S.C. § 101(5) (1988 & Supp. III 1993).

108. *Nobelman*, 113 S. Ct. at 2111.

109. *Id.*

110. *Id.*

111. *Nobelman v. American Sav. Bank (In re Nobelman)*, 113 S. Ct. 2106, 2111-12 (1993) (Stevens, J., concurring).

112. *Id.* at 2112.

113. At least twenty-one states were bound by the circuit court decisions cited in note 21 including: Alaska, Arizona, California, Colorado, Connecticut, Delaware, Hawaii, Idaho, Kansas, Montana, Nevada, New Jersey, New Mexico, New York, Oklahoma, Oregon, Pennsylvania, Utah, Vermont, Washington, and Wyoming. See *supra* note 21 and accompanying text.

Court ruled against them. According to the Washington Post, Mr. Palmer said that in lieu of paying \$71,000 for a condominium worth \$23,500, "[w]e will wheel Mr. Nobelman out in the hall, buy the vacant [condo] next door for \$23,500 and move him back in."¹¹⁴

Such an extreme solution is, however, not the debtor's only alternative. While *Nobelman* prohibits bifurcation in Chapter 13 cases, and although another recent Supreme Court opinion prohibits bifurcation in Chapter 7 cases,¹¹⁵ there has not been a definitive Supreme Court ruling on whether it is allowed in Chapter 11 cases.¹¹⁶ Michael S. Polk, a bankruptcy attorney who represents mortgage companies, said that he "anticipates a rise in the more cumbersome and expensive Chapter 11 filings as a last resort for cramdowns."¹¹⁷ If this view is correct, bifurcation seems to still be a viable alternative in Chapter 11 cases.

Nobelman also does not completely foreclose the possibility of a debtor's use of bifurcation in some Chapter 13 cases. Neither section 1322(b)(2) nor the *Nobelman* decision prohibits the modification of the rights of a creditor when the creditor has a security interest in collateral other than the debtor's principal residence.¹¹⁸ Although the Nobelmans' lien was secured by more than just their residence,¹¹⁹ the Supreme Court did not specifically address this issue. At least one court has refused to apply *Nobelman* in a case where the note was also secured by appliances and fixtures.¹²⁰ Before *Nobelman* was decided, some courts held that rents and profits were enough to remove a claim from the ambit of section 1322(b)(2).¹²¹ Whether these distinctions will hold up in light of *Nobelman* remains to be seen.

114. H. Jane Lehman, *Mortgage Reduction Issue Still Alive Despite Ruling, Cramdowns Possible for Some Bankrupt Homeowners*, THE WASHINGTON POST, June 5, 1993, at F1.

115. *Dewsnup v. Timm*, 112 S. Ct. 773 (1992).

116. Although the Supreme Court has not decided whether bifurcation of claims secured only by the debtor's primary residence is allowed in Chapter 11, some lower courts have held that such bifurcation is allowed in Chapter 11 cases. See, e.g., *Deever v. Internal Revenue Serv. (In re Deever)*, Adv. No. LA-92-03426-LF, 1994 WL 43906, (Bankr. C.D. Cal. Feb. 4, 1994); *In re Kennedy*, 158 B.R. 589 (Bankr. D.N.J. 1993).

117. H. Jane Lehman, *Court Deals Setback to Bankrupt Homeowners 'Cramdowns' Reduce Mortgage to Property Value*, LA TIMES, June 13, 1993, at K1.

118. 5 COLLIER ON BANKRUPTCY ¶ 1322.06, at 1322-16 (L. King 15th ed. 1989).

119. See *supra* note 25.

120. *Hammond v. Commonwealth Mortgage Co. of Am.*, 156 B.R. 943 (Bankr. E.D. Pa. 1993).

121. See, e.g., *Sapos v. Provident Inst. of Sav.*, 967 F.2d 918, 925 (3d Cir. 1992).

Another question that *Nobelman* leaves unanswered is whether a completely undersecured lien can be modified by a Chapter 13 plan. The Court in *Nobelman* held that it was proper to apply section 506(a) to determine the status of a claim as secured or unsecured.¹²² This language strongly suggests that a completely undersecured claim is thus an unsecured claim and, as such, can be modified in a Chapter 13 plan.¹²³ Therefore, bifurcation seems to still be available in many Chapter 13 plans as a means of discharging junior liens that are completely undersecured.

Critics of the holding in *Nobelman* warn that it may result in more undersecured loans being made to unsophisticated debtors since the creditors will depend on the leverage that foreclosure gives them to obtain repayment in the event of bankruptcy. According to Henry J. Sommer, a Philadelphia lawyer who represents low-income clients, about ten to twenty percent of all second mortgages are currently undersecured, but that number is expected to rise in light of the *Nobelman* decision.¹²⁴

Supporters of the decision envision that the true significance of *Nobelman* lies in what its holding prevented: more expensive mortgages. The executive vice president of the Mortgage Bankers Association of America, Warren Lasko, said that a contrary decision would have meant that lenders would have had to price everybody's mortgages higher to make up for the potential losses that bifurcation would have caused.¹²⁵

Both positions recognize that *Nobelman* has the potential to substantially affect bankruptcy practice and the residential lending industry. Although the Supreme Court left many loopholes for debtors that would permit bifurcation, the decision in *Nobelman* has made it substantially more difficult to do so. The net effect of *Nobelman* is that, for the most part, home mortgages are not dischargeable in Chapter 13 bankruptcy proceedings.

Steven O. Vondran

122. *Nobelman v. American Sav. Bank (In re Nobleman)*, 113 S. Ct. 2106, 2108 (1993).

123. COLLIER, *supra* note 118, ¶ 1322.06.

124. Lehman, *supra* note 114, at F1.

125. Lehman, *supra* note 114, at F1.