

2009 SURVEY OF RESIDENTIAL MORTGAGE ISSUES IN CONSUMER BANKRUPTCY CASES

By David P. Leibowitz

Introduction

This article examines case law in bankruptcy courts involving residential mortgage issues since the beginning of 2008. Readers may also refer to *Residential Mortgage Issues in Consumer Bankruptcy Cases*, by the author, that appeared in Part III of Norton Annual Survey of Bankruptcy Law (2008 ed), which was meant as a foundation for subsequent study. This article addresses more particularized issues presently in litigation before bankruptcy courts throughout the U.S. The current economic conditions have driven an increase in this mortgage-related litigation. In particular:

- Consumer bankruptcy filings increased dramatically in 2008 along with all other consumer bankruptcy filings;
- Foreclosures are at record rates in virtually every state;
- In many cases people are filing Chapter 13 to save their homes;
- The mortgage industry is highly complex owing to securitization; and
- The nature of the mortgage industry gives rise to complex legal issues that often clash with the summary nature of high-volume bankruptcy court calls.

As a result of these factors, serious issues often arise in the context of mortgage foreclosures. As Chapter 7 debtors and Chapter 7 trustees often lack sufficient economic interest to assert their rights against mortgage lenders and servicers, these issues typically arise in the context of Chapter 13 cases. Moreover, where servicers and lenders offer their attorneys strong incentives to get cases out of bankruptcy court quickly, shortcuts are inevitable. Finally, some bankruptcy courts have difficulty grappling with the complexities of mortgage securitization and its implications on a wide array of legal issues. It appears that these judges would rather not address these issues and instead defer to the state courts that are handling the substance of mortgage foreclosure cases.

David Leibowitz is the founder and managing member of Lakelaw (www.lakelaw.com), practicing in Illinois and Wisconsin. He serves as a Chapter 7 trustee in Cook County, Illinois (Chicago). He also represents people and businesses in bankruptcy and defends them against mortgage foreclosures.

In light of rapidly declining real estate values, “cure and maintain” plans under Bankruptcy Code § 1322(b)(5) are less prevalent than in the past. Indeed, many issues that might have come up in the Chapter 13 context before are less likely to arise today. The bankruptcy courts will, however, have to address these in the event that residential mortgage modifications are authorized for Chapter 13, as discussed below, or if property values recover.

Today, the residential real estate in consumer bankruptcy cases often has negative equity. This is because real estate was often financed during the early 21st century with the borrower putting no money down. Real estate values have also declined drastically since 2007. Congress was, at the time of this writing, considering legislation that would modify section 1322(b) of the Bankruptcy Code to allow mortgage modifications (or, in the parlance of lenders who oppose such treatment, “cram-downs”) of mortgages solely secured by residential real estate in Chapter 13. Such legislation would also provide for “claw-backs” or “shared appreciation” depending upon one’s viewpoint. Under these provisions, if the principal balance of a mortgage was reduced by reason of a Chapter 13 modification, and the property was sold within five years thereafter for a price greater than the valuation at the time of loan modification, the lender would be entitled to a portion of the appreciation on a sliding scale, depending on how soon after confirmation the sale takes place.

Modifications under this proposed legislation would require court determination as to value as well as appropriate interest rates, thus implicating *Associates Capital Corp. v. Rash*¹ and *Till v. SCS Credit Corp.*² The nature and breadth of this legislation is beyond the scope of this article. Furthermore, executive plans for mortgage modifications and refinancing under the Home Affordability and Stability Plan³ are also beyond the scope of our inquiry. This article does survey representative cases in the residential mortgage arena but does not address every case in these particular areas during the past year.

It should be noted that Congress failed to enact legislation that would have allowed for modification of mortgages in Chapter 13 cases during the winter and spring of 2009.

Standing and Real Party in Interest

In bankruptcy cases, the issue of standing can arise either upon the filing of a proof of claim or on a motion for relief from stay. The Bankruptcy Code provides that filing a petition gives rise to an automatic stay against any attempt to collect or enforce any lien, judgment, or claim against the estate.⁴ In a Chapter 7 case, however, a court may lift the automatic stay if an interested party can show a lack of adequate protection of a creditor’s interests or if the debtor has no equity in the collateral.⁵ Relief from stay hearings may be summary in nature, strictly limited to an examination of the adequacy of protection for the creditor’s interests and other equitable considerations.⁶

As a result of the *Vitreous Steel* decision, lenders and servicers posit that they need only show a colorable interest in the property in order to pursue their rights.⁷ They also assert that the definition of “creditor” under the Bankruptcy Code is extremely broad. Bankruptcy Code section 101(10) provides:

(10) The term “creditor” means—

- (A) entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor;⁸

Further, a “claim” is defined by Bankruptcy Code section 101(5) as:

- (A) right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured;⁹

Mortgage servicers assert that they are “creditors” entitled to a “claim” because they have the right to payment under the note and mortgage. Typically, it is the servicer who is listed as the creditor on a debtor’s schedules. When this is taken by a court as an admission, a stay motion is typically summarily granted, and the matter moves on to state court. Sometimes the Chapter 13 case is even dismissed.

Suppose a debtor files a Chapter 13 case and lists the mortgagee under Schedule D as “Unknown Trustee Under Undetermined Trust Pursuant to Undisclosed Pooling and Servicing Agreement with XYZ Servicer.” The servicer files a proof of claim but does not disclose the actual noteholder. Assume for this hypothetical that the debtor does not object to the claim and that the plan is confirmed. The debtor continues to make payments to the servicer on the mortgage regularly during the course of the plan, and the debtor thinks that there is nothing wrong. The lender, on the other hand, thinks that the payments are late and imposes late charges. When the late charges are not paid, the lender then sends inspectors out to examine the collateral, orders a new appraisal and a title search in anticipation of foreclosure, and moves for relief from the automatic stay in the name of “ABC Bank as Trustee c/o XYZ Servicer.”

The debtor’s attorney now objects on grounds that: (1) the loan is not in default postpetition; (2) “ABC Bank as Trustee c/o XYZ Servicer” is not a legitimate or legal entity; (3) “XYZ Servicer” is not a creditor; (4) “XYZ Servicer” does not have standing even if it is a creditor; and (5) “ABC Bank as Trustee” is the real party in interest.

In similar circumstances, *In re Woodberry*¹⁰ holds that a mortgage servicer is a creditor and has standing to seek relief from the automatic stay. In *Woodberry*, the loan servicer moved for relief from stay to allow it to foreclose on real property held as collateral by the securitized trust on whose behalf the servicer was acting. The debtor challenged the servicer’s standing to pursue relief from the automatic stay, arguing that the servicer must be both: (1) the current holder of the note and (2) the current holder of the mortgage securing the note (either as the original named mortgage holder or by a recorded written assignment).

In rejecting the debtor’s arguments, the bankruptcy court followed the state law of South Carolina on recordation of instruments as well as the Uniform Commercial Code. Neither the servicer, the trustee of the trust, nor the trust itself was the original named holder of the note and mortgage. The servicer held an unrecorded assignment of the loan to the trust and had the right to collect payments on the note and mortgage pursuant to a pooling and servicing agreement.

Under South Carolina law, an assignment of a mortgage need not be recorded. The note in question was a bearer instrument, and the servicer had physical custody of the original note and mortgage. While the servicer was prima facie the owner of the note because it was in possession of bearer paper, that was not the determinative factor. Instead, the servicer was held to have standing to pursue relief from stay because of the servicer's contractual obligations under its securitization subservicing agreement. Under this contract, the servicer had authority to collect payments due under the note and to foreclose on collateral in the event of a default.

Accordingly, the *Woodberry* court held that the servicer provided sufficient evidence that it was a "party in interest" and a creditor under § 101(10)(A) of the Bankruptcy Code. The court further held the servicer to be a "real party in interest" under Bankruptcy Rule 7017, which, as interpreted by case law, requires that actions be prosecuted in the name of the person or entity holding the legal right "which is sought to be enforced or is the party entitled to bring suit."¹¹ The court found much precedent upon which to rely in support of its conclusion.¹²

The bankruptcy court also held the mortgage servicer had standing to file a proof of claim in *In re Conde-Dedonato*.¹³ The court reasoned that for a claimant to be entitled to file a proof of claim, the claimant must be a "creditor or the creditor's authorized agent."¹⁴ The court further noted that the Bankruptcy Code defines a creditor as "an entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor;"¹⁵ and a claim is a "right to payment" or a "right to an equitable remedy for breach of performance if such breach gives rise to a right to payment."¹⁶ Finally, the court noted that Bankruptcy Code § 502(a) provides that "a claim or interest, claim of which is filed under section 501 of this title, is deemed allowed, unless a party in interest... objects." Accordingly, the *Conde-Dedonato* court held that a servicer of a mortgage is clearly a creditor and has standing to file a proof of claim against a debtor pursuant to its duties as a servicer.¹⁷

In *In re Viencek*, the debtor attempted to expunge a mortgage servicer's proof of claim because the servicer failed to identify the actual owner of the claim. In opposition, the servicer argued that it had a tangible interest in the estate, pursuant to which it could file the claim. The bankruptcy court agreed, stating that the servicer was a party in interest "because of its pecuniary interest in the mortgage it services."¹⁸

Standing to assert the rights of a mortgagee has not been universally recognized. In *In re Hayes*, the bankruptcy court denied a mortgage purchaser's motion for relief from the automatic stay in a Chapter 13 case on the grounds that the purchaser lacked standing.¹⁹ The purchaser in that case could not provide documentary evidence showing each transfer of the mortgage.

In *Hayes*, the debtor's original mortgage to Argent Mortgage Company LLC subsequently was sold. It ultimately ended up with Deutsche Bank as trustee for an asset securitization trust. In June 2007, the debtor filed a voluntary Chapter 13 petition. Deutsche Bank filed a motion for relief from automatic stay, to which the debtor objected, asserting that Deutsche Bank lacked standing. At the hearing on Deutsche Bank's motion for relief, Citi Residential Lending, Inc., the servicer of the mortgage for Deutsche Bank, introduced multiple documents purporting to establish Deutsche

Bank's ownership of the mortgage. The documents showed Deutsche Bank was a party to a Pooling and Servicing Agreement with Argent Securities Inc.. However, no document showed the transfer of the mortgage from Argent Mortgage to Argent Securities or any relationship between those two entities. The bankruptcy court noted that, in Massachusetts, a mortgagee or an entity with a valid assignment of a mortgage may foreclose on real estate and seek relief from the automatic stay to do so. However, in order to do so, Deutsche Bank was required to establish that it owned the mortgage and that it was asserting its own rights. The court found that, according to Local Bankruptcy Rule 4001-1(b)(f), a movant must establish both the original holder of the obligation secured by the mortgage "and every subsequent transferee."²⁰

The bankruptcy court held in *Hayes* that Deutsche Bank failed to prove standing because it did not show that the mortgage in favor of Argent Mortgage had been assigned to Argent Securities, the entity from whom Deutsche Bank ultimately received its interest. In other words, "Deutsche Bank failed to adequately trace the loan from the original holder, [Argent Mortgage], to it."²¹ The court cited *Nosek v. Ameriquest (In re Nosek)*,²² which discussed the misbehavior in bankruptcy mortgage claims, and noted that parties "who do not hold the note or mortgage and do not service the mortgage do not have standing to pursue motions for relief."²³

In the end, the bankruptcy court not only held that Deutsche Bank failed to establish its standing because of the gap between Argent Mortgage and Argent Securities but it also issued an order for Deutsche Bank to show cause why it should not be sanctioned for pursuing its motion for relief from without competent evidence of its standing to do so. In its decision denying relief from stay, the bankruptcy court noted that sanctions may be appropriate given the "tangle of inconsistent and incomplete documents introduced into evidence" by Citi, which forced the bankruptcy court to apply intensive scrutiny to hundreds of pages of documents during the two day hearing.²⁴

In *Nosek v. Ameriquest Mortgage Company*,²⁵ the bankruptcy court did impose monetary sanctions on Ameriquest as the servicer, Wells Fargo as the purported noteholder, and the attorneys involved in filing the claim, all for misrepresenting the holder of the note. In *Nosek*, the original lender was Ameriquest Mortgage. Soon after closing, Ameriquest Mortgage assigned its note and mortgage to Wells Fargo. The assignment was not recorded for three years. During the debtor's Chapter 13 case, and subsequent to Ameriquest's assignment, Ameriquest, which had maintained servicing of the mortgage, filed a proof of claim asserting that it was the owner of the mortgage. Even though Ameriquest owned servicing rights, the bankruptcy court held that it had no right to represent itself to the court as the owner of the note and mortgage in its proof of claim. It did not make any difference to the court that the assignment was of record or that Ameriquest had servicing rights for Wells Fargo under a Pooling and Servicing Agreement. The bankruptcy court took umbrage at the misrepresentations in the parties' pleadings and imposed severe sanctions on the parties and their attorneys.

The question of standing is not just limited to the dichotomy of the servicer and the purported assignee of the mortgage under a securitized trust. Complex questions may also arise under the U.C.C. as well as the Federal Rules of Civil Procedure involving the question of real party in interest. This is illustrated by Judge Bufford's decision in

In re Hwang.²⁶ In this case, IndyMac Federal Bank was the original mortgage lender for the debtor's Las Vegas home. Shortly after originating the loan, IndyMac sold it to Federal Home Loan Mortgage Company (Freddie Mac), which in turn, according to the court, almost certainly sold the note to "unknown third parties for securitization."

The court held an evidentiary hearing on the motion for relief from stay. Based on that hearing, the court held that IndyMac was the holder of the note and had the right to enforce it but that it was not entitled to relief from stay. This was because joinder of the owner of the note was required by Civil Rule 19,²⁷ where IndyMac was not the real party in interest pursuant to Federal Civil Rule 17.²⁸ The court made this determination even though IndyMac asserted, without rebuttal, that it was the servicer for the new owner of the note. IndyMac did not know who owned the note at the time of the hearing, nor did it offer into evidence any servicing agreement with the present owner of the note.

The court then turned to the question of who is the real party in interest after securitization. The court provided a detailed analysis of this inquiry:

If a loan has been securitized, the real party in interest is the trustee of the securitization trust, not the servicing agent. *See LaSalle Bank N.A. v. Nomura Asset Capital Corp.*, 180 F. Supp. 2d 465, 469-71 (S.D.N.Y. 2001) ("*LaSalle-Nomura*"); *accord, LaSalle Bank N.A. v. Lehman Bros. Holdings, Inc.*, 237 F. Supp. 2d 618, 631-34 (D. Md. 2002) ("*LaSalle-Lehman*"). This rule does not turn on who is in possession of the note.

In the *LaSalle-Nomura* case, the bank brought an action against Nomura Asset Capital Corp., the asset securitization trustee, "as Trustee for Certificate Holders of Asset Securitization Corporation Commercial Mortgage Pass-Through Certificates, Series 1997-D5." Defendants moved to dismiss, in part on the grounds that the real party in interest, pursuant to Rule 17, was the mortgage servicer. In denying the motion, the court found that the real party in interest was the trustee of the trust (the plaintiff in the case), and not its loan servicer (which had not been joined in the litigation). *LaSalle-Nomura*, 180 F. Supp. 2d at 469-71.

The only reported opinion discovered that disagrees with this conclusion is *In re Tainan*, 48 B.R. 250 (E.D. Pa. 1985), an early case that gives no analysis for its conclusion that a servicing agent is a real party in interest in seeking relief from the automatic stay. *See id.* at 252. The court finds the *Tainan* case unpersuasive.

* * *

If the note is part of a securitization, the burden of joining the owner of the note is not substantial. A securitization typically involves the creation of a trust, the appointment of a trustee, a transfer to the trust of some ten thousand secured real estate notes (such as the one involved in this case) and the sale of interests in the trust to a substantial number of investors. *See generally*, Katherine Porter, *Mistake and Misbehavior in Bankruptcy Mortgage Claims*, 87 Tex. L. Rev. ____, ____ (2008). The trustee of the trust is authorized, pursuant to trust law, to act on behalf of the trust. Thus only the trustee, and not the investors, should be joined

as the owner of the note at issue. Indeed, this is exactly what happened in both *LaSalle-Nomura* and *LaSalle-Lehman*.

The right to enforce a note on behalf of a noteholder does not convert the noteholder's agent into a real party in interest." As a general rule, a person who is an attorney-in-fact or an agent solely for the purpose of bringing suit is viewed as a nominal rather than a real party in interest and will be required to litigate in the name of his principal rather than in his own name." 6A Wright § 1553. Consequently, even if the court had found that a proper agency relationship exists between the holder of the note and the party seeking to enforce its security, this does not excuse the agent from the requirement that an action be prosecuted in the name of the noteholder, who is the real party in interest. Fed. R. Civ. P. 17(a) (1). Thus, even if IndyMac is the loan servicer for the unidentified owner of the note here at issue (a fact that IndyMac has failed to prove), it is not the real party in interest that is required to bring the motion before the court.²⁹

Thus even though IndyMac was deemed to both have had "standing" and to be a "party in interest," it was nevertheless held not to be the "real party in interest." Standing is merely a threshold question in every federal case and cannot be waived.³⁰ To obtain relief from stay in a federal court, the movant must establish that it is a party in interest not only to meet constitutional muster but also to meet the "prudential requirement" of being a "real party in interest."³¹ Finally, the court noted that there was a failure to join all necessary parties pursuant to Civil Rule 19, which, while not incorporated by reference in Bankruptcy Rule 9014, may be incorporated upon order of the court.

The court therefore held that if a servicer seeks relief from the automatic stay, it must join or obtain the authority of the real party in interest, the true owner of the mortgage note. Moreover, the servicer must at least plead and prove that it had some capacity to proceed, and if so, under what authority. For these reasons, the court denied relief from the automatic stay to IndyMac as servicer for the undisclosed note owner.

Proofs of Claim

Mortgage lenders and their servicers routinely file proofs of claim in Chapter 13 cases. These proofs of claim have not always been subjected to close scrutiny by debtors or courts. This is rapidly changing. Illustrative of this trend is *In re Stewart*.³² There, Wells Fargo submitted a proof of claim signed by its attorney. The debtor objected and demanded a payment history and a detailed analysis to support the claims. In addition, the debtor contended that her payments were not applied in accordance with the terms of her note. Moreover, she claimed that numerous charges were not reasonable, inaccurate, or not legally due. Wells Fargo responded but did not provide backup or supporting documentation. The court ordered a Wells Fargo representative to testify in support of its claim.

The court found considerable fault with Wells Fargo's practices. First, it found that Wells Fargo systematically failed to notify borrowers of assessment of fees, costs, and charges at the time that they were incurred during all stages of loan administration

and that this practice was not limited to loans in bankruptcy cases. Wells Fargo also misapplied payments, resulting in assessment of late charges and placement of funds in a “suspense account” rather than application of such funds to balances of interest and principal due on the note.

In addition, the court was troubled by the automatic imposition of charges for drive-by inspections of the property any time the loan was more than 20 days past due—even if the past-due status was triggered by the lender’s computer logic rather than any act or omission of the debtor. Wells Fargo charged for multiple “broker price opinions” obtained during the pendency of the Chapter 13 case. Even worse, the actual out-of-pocket expenses of Wells Fargo for these broker price opinions were inflated by internal charges not actually expended by Wells Fargo in obtaining them. Wells Fargo also made excessive charges for forced place property insurance.

In accordance with the terms of its note with the borrower, similar to all uniform notes, Wells Fargo was to apply funds first to outstanding escrow charges, then accrued interest, and then principal. Once these sums were satisfied, late fees should no longer have been imposed. While Wells Fargo legitimately imposed a late charge for one late payment, it also continued to impose late charges on each subsequent payment because the late fee for the first payment had not been satisfied. The court found this practice likewise objectionable.

The court was disturbed that it took over four months and three hearings just to explain and reconcile Wells Fargo’s claim. The debtor had been charged for 44 inspections, only one of which the court allowed. The debtor had been charged 49 late charges, only 10 of which the court allowed. The court also held that Wells Fargo’s legal fees were excessive. As a result of the foregoing, the *Stewart* court imposed \$10,000 in damages as well as \$12,350 in legal fees against Wells Fargo.³³ Further, Wells Fargo was ordered to audit all subsequent proofs of claims in the bankruptcy court.

On appeal, Wells Fargo argued, among other things, that its contractual rights had been modified impermissibly by the bankruptcy court. The district court disagreed.³⁴ Wells Fargo also argued that the bankruptcy court abused its discretion by imposing improper procedures for determination of claims and by acting as an accounting expert to aid the debtor. The district court found this argument “unconvincing.” The district court remanded for additional findings on the question of whether the bankruptcy court had the right to enjoin subsequent conduct by Wells Fargo in its mortgage servicing and proof of claim practices.

On remand, the bankruptcy court noted that Wells Fargo’s servicing practices were well established and documented in a series of cases before the bankruptcy court.³⁵ It had the obligation to remedy “obvious and blatant administrative errors on loans under jurisdiction of [the] court.” Since Wells Fargo had admitted to “systematic error” in administration of its loans, it became incumbent on Wells Fargo to remedy its errors. No other remedy was deemed by the bankruptcy court to be sufficient.³⁶

The court rejected Wells Fargo’s claim that either the Real Estate Settlement Procedures Act or bank regulations required a contrary result. It also rejected Wells Fargo’s contention that the court could not bind Wells Fargo to make the required audit

throughout the Eastern District of Louisiana. Accordingly, it ordered that Wells Fargo audit all proofs of claim in all bankruptcy cases in that district.

The loan procedures and the “Fidelity” software utilized by Wells Fargo is at issue for mortgage loans and by mortgage servicers throughout the U.S. It can be inferred that the mortgage servicing practices denounced by the bankruptcy court in *Stewart* are being utilized on a regular basis throughout the nation. It remains to be seen whether other bankruptcy courts will take the same direct and affirmative action taken by the court in *Stewart*, particularly in light of economic conditions now extant in the U.S.

Similar abuses were noted by the court in *In re Parsley*.³⁷ While the court declined to enter sanctions, it was unequivocal and unambiguous in its disapproval of the conduct of the attorneys and mortgage servicers that had systematically filed false pleadings on motions for relief from the automatic stay in the bankruptcy court. In fact, the court cited a series of decisions demonstrating that mistakes and careless practices were endemic within the residential mortgage creditors’ bar throughout the U.S.³⁸

To the same effect, in *In re Schuessler*,³⁹ the court not only denied relief from the automatic stay to mortgage lenders but it also imposed attorneys’ fees upon the movants and barred them from seeking attorney’s fees for their own misguided efforts. A more relaxed approach was taken by a New Jersey bankruptcy court in *In re Rodriguez*.⁴⁰ Although that court found that Countrywide acted arbitrarily in organizing its claim, the court simply ordered Countrywide to correct its errors, finding that Countrywide had not violated RESPA or any other statute in filing its claim.

In contrast to his approach in *Parsley*, Bankruptcy Judge Bohm called Citi Residential Lending to task for its inadequate proof of claim in *In re Prevo*.⁴¹ Judge Bohm stated:

Lenders apparently have been operating under the assumption that the fees and costs in their proofs of claim are invulnerable to challenge because debtors lack the sophistication, the debtors’ bar lacks the financial motivation, and bankruptcy courts lack the time. The tide is changing... in courts across the country (citing authorities).⁴²

The original proof of claim was deficient in many respects: (1) there was no payment history; (2) there was no evidence that Citi was the current owner or servicer of the note; (3) neither the note nor the deed of trust was attached; and (4) no bills, invoices, or other documentation were attached to support the reasonableness of the fees requested.

After a month-long delay, Citi amended its proof of claim, reducing escrow advances by more than \$2,000. However, it did not alter late charges, BPO fees (Broker Price Opinion), or foreclosure fees, and it provided no documentation supporting the reasonableness of fees and costs. The court denied allowance of the fees, stating that Citi failed to introduce documents in support of its claim.⁴³ The court refused to allow any of these fees absent an explanation of their nature and proof that they were actually incurred as well as invoices detailing who performed the services and for how long—essentially the same information that would be included in a fee application.

The court recognized that the assembly-line nature of consumer credit practice has led to flat fees being paid to the creditors' bar for services such as filing proofs of claim. However, this did not excuse the creditors' bar from filing a claim with insufficient information for the court to make a determination as to whether the claim was reasonable. Indeed, the court asserted that certain members of the mortgage industry are "intentionally attempting to game the system by requesting undocumented and potentially excessive fees and then reducing those fees in amended proofs of claim only after being exposed by debtor's counsel" (likening this to a "carnival shell game"). Citi's claim was substantially disallowed, and in addition, Citi was ordered to show cause why it should not be ordered to pay the attorney's fees of the debtor for objecting to the claim.

Real Estate Settlement Procedures Act

Qualified Written Request

The Real Estate Settlement Procedures Act (RESPA) entitles a borrower to receive periodic accounting upon receipt of a Qualified Written Request (QWR) to the lender or its servicer.⁴⁴ A servicer is required to acknowledge a QWR within 20 business days and to provide the required information within 60 business days. In *Miller v. Ameriquest (In re Laskowski)*,⁴⁵ the Chapter 13 trustee made a qualified written request to Ameriquest for a loan accounting. No response was forthcoming. She made this request because all Chapter 13 payments had been made, and she wanted to verify that with Ameriquest's records. When Ameriquest did not respond, the Chapter 13 trustee sued Ameriquest under RESPA for statutory damages and attorney's fees.

In response, Ameriquest sought to dismiss the complaint on the following grounds: (1) the RESPA claim is preempted by the federal bankruptcy laws; (2) the Chapter 13 trustee lacks the statutory authority to submit a QWR; (3) the QWR was not sent to the proper servicer, which was AMC Mortgage Services, Inc; (4) RESPA does not require an annual accounting for bankrupt borrowers; and (5) there is no private cause of action under RESPA.

The bankruptcy court denied the motion to dismiss, holding that RESPA claims were totally consistent with the Bankruptcy Code. It further held that the Chapter 13 trustee had the right to bring the RESPA claim. AMC Mortgage Services was a spin-off of Ameriquest. No notice had been given to the debtor of this fact. Accordingly, Ameriquest properly received the QWR. Debtor-borrowers are not entitled to an annual accounting, but they are entitled to a proper response to a QWR. Holding there was no private right of action for certain aspects of RESPA, the court nevertheless found that a statutory remedy was available for failure to provide a proper response to the QWR.

In *In re Payne (Payne v. Mortgage Electronic Registration Systems, Inc.)*,⁴⁶ the court sustained the Chapter 13 debtor's RESPA claim and also imposed damages for emotional distress and punitive damages (albeit in rather small amounts) together with attorney's fees. In another case, *In re Holland (Holland v. EMC)*,⁴⁷ the court denied a

RESPA claim on summary judgment where the QWR was sent to an attorney rather than the servicer and where the debtor did not establish any damages.

Recoupment

In the Chapter 13 case *In re Wentz*,⁴⁸ the debtor initiated an adversary proceeding against her lender, alleging violations of the Truth in Lending Act (TILA) and the Home Owners Equity Protection Act (HOEPA) as well as RESPA. Specifically, she alleged that a yield spread premium in connection with her loan was an illegal kickback. The statute of limitation for such claims is one year pursuant to 12 U.S.C.A. § 2614. However, since the lender had filed a proof of claim in the bankruptcy case, the court held that the RESPA claim was in the nature of recoupment, and thus the one-year statute of limitation did not apply.⁴⁹

Notification for Postpetition Charges and Forced-Placed Escrows

*In re Johnson*⁵⁰ addressed the lender's proof of claim for postpetition advances in a Chapter 13 case. The debtor objected on the ground that he never received notice from the lender regarding postpetition taxes during the course of the case. He contended that this was a violation of RESPA⁵¹ as well as the local bankruptcy rules. Accordingly, he asserted that the lender had waived any right to receive such postpetition advances.

Washington Mutual, the lender, asserted that it was not required to give notification where the funds were not pursuant to an escrow and also where notice requirements were not applicable in bankruptcy by regulation.⁵² Further, Washington Mutual asserted that RESPA did not create a private right of action for its failure to provide notice during the course of the case of its forced-placed escrow.

The bankruptcy court overruled Washington Mutual's objections, holding that it waived its rights by failing to notify the debtor, both in accordance with RESPA as well as the local bankruptcy rules. Accordingly, it reduced Washington Mutual's claim by approximately \$14,000.

Courts have not universally imposed liability upon lenders in Chapter 13 cases under RESPA. For example, in *In re Rodriguez*,⁵³ the bankruptcy court found no fault and overruled the debtor's objections to Countrywide's postpetition escrow analysis and determination that the debtor's payments were insufficient under the terms of the mortgage.

Truth in Lending Act

Statute of Limitations—Claim for Failing to Rescind Separate from Failure to Give Notice of Right to Rescind

TILA requires that the consumer give the lender notice of a rescission within three business days after the loan closes as a condition to rescission of the transaction. The lender then has 20 days within which to return all amounts paid by the consumer. Once that is done, the consumer must tender the property that was the subject of the transaction back to the lender.⁵⁴ If the necessary notices of right to rescind are not pro-

vided, or if the disclosures provided are defective, then the right to rescind is extended for three years.

In addition to the remedy of rescission, a claim for statutory damages may be maintained for not giving the proper rescission notices. The statute of limitation for that claim is only one year. In *In re Ebron*, (*Ebron v. First Franklin Financial Corp.*),⁵⁵ the court held that even though the one-year statute of limitation had passed, failure to respond is a separate violation and resurrects a claim for statutory damages pursuant to 15 U.S.C.A. § 1635(a).

Under 15 U.S.C.A. § 1640(e)'s one-year limitation period, an action for statutory damages and concomitant attorney's fees would have been time-barred in *Ebron* where more than a year had passed since the transaction at issue had closed. Therefore, the court granted defendant's motion to dismiss plaintiff's claim for statutory damages and attorney's fees under 15 U.S.C.A. § 1640 by reason of alleged inadequacy of the TILA disclosures provided at closing.

However, the court in *Ebron* did allow a separate claim for statutory damages and attorney's fees under 15 U.S.C.A. § 1635(g) because the lender failed timely to honor a request for rescission. The plaintiff alleged that the lender did not respond to her within the 20 days following the receipt of the rescission note. Therefore, the plaintiff had sufficiently pleaded that she would be entitled to seek statutory damages based upon the failure of the lender to honor a timely rescission notice.

Courts have held in other jurisdictions that if a note and mortgage is transferred and if the defect in the TILA disclosures is not apparent on the face of the documents, it would not be liable for statutory damages, even if it denied the TILA rescission after the one-year statute of limitations had expired. This would not, however, foreclose the plaintiff from pursuing rights to rescind pursuant to 15 U.S.C.A. § 1641(a).⁵⁶ Further, assignees would be liable for any claims that arise under HOEPA, even if they were not apparent from the face of the documents, pursuant to 15 U.S.C.A. § 1641(d).

Statutes of Limitation—No Barrier to Recoupment Claims in Defense

In re Wentz (*Wentz v. Saxon Mortgage*)⁵⁷ presented the question of whether the plaintiff, a Chapter 13 debtor, could raise otherwise-time-barred TILA claims, including claims for rescission, statutory damages, and attorney's fees, when faced with a pending mortgage foreclosure in state court and a corresponding proof of claim filed by the lender in the Chapter 13 case.

Debtor's Chapter 13 plan proposed, in part, to file an adversary proceeding seeking to rescind her mortgage by reason of TILA violations as well as to recover statutory damages and attorney's fees. In addition, she raised claims under HOEPA and RESPA. At the same time, the mortgage lender filed its secured proof of claim.

The debtor alleged that Saxon, along with other defendants, failed to disclose required information and also provided misinformation concerning the nature of the two loans, which constituted violations of both TILA and HOEPA. In response, the lender filed a motion to dismiss asserting that the claims for statutory damages and attorney's fees were time barred by the one-year statute of limitation in 15 U.S.C.A. § 1640. The debtor asserted that her claims were in the nature of recoupment so that the statute

of limitation did not apply. The lender responded that her claims were offensive, not defensive, so that the theory of recoupment did not apply.

The mortgagee argued on a motion to dismiss that these causes of action for damages were time barred because they were not commenced within a year of the occurrence of the loan closing. The debtor conceded that damage claims under TILA, HOEPA, and RESPA are generally subject to one-year statutes of limitation beginning from the consummation of the loan transaction and that the complaint was filed subsequent to the statutes of limitation having run.⁵⁸ The debtor argued in response that (1) 15 U.S.C.A. § 1635(g) provides an additional year from the date of the rescission of the mortgage to pursue TILA or HOEPA claims; and (2) all of the federal consumer lending protection causes of action seeking damages are in the nature of recoupment against Saxon's filed proof of claim and are excepted from the one-year statutes of limitation.

The court rejected the debtor's § 1635(g) theory. However, the court held that TILA and HOEPA causes of action for damages were in the nature of recoupment and are excepted from the one-year statute of limitation of 15 U.S.C.A. § 1640(e), stating that recoupment claims are not barred by the otherwise-applicable one-year statute of limitation for TILA or HOEPA damage causes of action and that recoupment claims are permitted under Ohio law.⁵⁹ The court similarly found that plaintiff's RESPA claim was in the nature of recoupment and not barred by the one-year statute of limitation of 12 U.S.C.A. § 2614.

Tender—Proof

Normally, in the event of a TILA rescission, the mortgagor must tender back to the lender what the mortgagor received at the closing, less the interest, fees, and other expenses impermissibly charged by the lender to the borrower and actually paid by the borrower to the lender, either at the closing or thereafter. Are these rules different for debtors in bankruptcy? Courts have varied on this issue.

In *In re Jaaskelainen (Jaaskelainen v. Wells Fargo Bank NA as trustee for Certificate holders of Carrington Mortgage Loan Trust Series 2006-OPT1 Asset Backed Pass-Through Certificates and Option One Mortgage Corporation)*,⁶⁰ Judge Hillman first addressed the evidentiary standard to be considered in rebutting the presumption raised by a statement on a notice of right to cancel that the mortgagors received multiple copies of a notice of right to cancel.

Quoting from an earlier First Circuit case, the court stated:

As Dean Wigmore has explained, "the peculiar effect of a presumption 'of law' (that is, the real presumption) is merely to invoke a rule of law compelling the (trier of fact) to reach a conclusion in the absence of evidence to the contrary from the opponent. If the opponent does offer evidence to the contrary (sufficient to satisfy the judge's requirement of some evidence), the presumption disappears as a rule of law, and the case is in the (factfinder's) hands free from any rule." As more poetically the explanation has been put, "(p)resumptions . . . may be looked on as the bats of the law, flitting in the twilight, but disappearing in the sunshine of actual facts."⁶¹

Under the facts of the case, the court found that the debtors had rebutted the presumption by establishing that the documents had been maintained in the same folder that they had been placed in at the closing. The court did not find the fact that the debtor's attorneys had copied the documents after removing them from the folder to be significant. The court did not require that the documents be maintained with the same level of "chain of custody" as though they had been removed from a crime scene. Rather, the court found that production of closing documents stored in a manner reasonably ensuring their integrity in conjunction with testimony supporting their reliability is sufficient to rebut the presumption. In addition, the borrower's testimony, by itself, may be sufficient to overcome the presumption of delivery.

The court stated:

A closing booklet is not a murder weapon or controlled substance which requires a perfect chain of custody to prove guilt. Such a standard is illogical and inappropriate to apply to a TILA case. The reason is obvious: a lender would never be satisfied with any chain of custody. If the Debtors themselves cannot maintain possession of their own Closing Booklet, the only reliable ones would be those containing exactly what the lender alleges it should. Moreover, none of the above cited cases contained exhaustive factual findings with respect to the chain of custody of the respective documents.⁶²

Under the facts of the case, the court found that the debtors had rebutted the presumption of having received multiple copies of the notice of right to cancel and that the lenders had not sustained their burden of proof of having provided the required two copies for each debtor. The court also rejected the lender's bona fide error defense.

From this point, the court turned to the question of tender. The issue presented became what exactly did the debtor have to tender for purposes of TILA in the context of a bankruptcy case. Relying on *Myers v. Fed. Home Loan Mortgage Co. (In re Myers)* and *Whitley v. Rhodes Financial Services, Inc. (In re Whitley)*,⁶³ the court decided that the debtor in a bankruptcy case had no tender obligation at all. Rather, the court held that, on rescission, the creditor was reduced to an unsecured claim. The court stated:

In a non-bankruptcy setting, the rights and duties of the parties upon TIL[A] rescission are clear and absolute. Each party must make the other as whole as he would have been had the contract never been entered into. In the absence of bankruptcy, there is no legal impediment to either party doing what is required to restore the status quo ante. Consequently, the creditor's statutory duty to perform first merely establishes the order of performance; it does not alter the ultimate effect on the remedy. Bankruptcy, however, relieves the debtor from his obligation to pay the creditor upon rescission. Conditioning rescission upon the debtor's payment therefore imposes an obligation from which the debtor has been legally freed. Unlike the situation absent bankruptcy, there is a legitimate, legal impediment to the debtor's reciprocal performance. It would be palpably unfair to deny the relief to which a consumer is entitled under TIL[A] because that consumer has also availed himself of bankruptcy relief. To do so would

require that the consumer choose between bankruptcy and TIL[A], something neither form of statutory relief contemplates.

* * *

Bankruptcy, however, relieves the debtor from his obligation to pay the creditor upon rescission. Conditioning rescission upon the debtor's payment therefore imposes an obligation from which the debtor has been legally freed. Unlike the situation absent bankruptcy, there is a legitimate, legal impediment to the debtor's reciprocal performance. It would be palpably unfair to deny the relief to which a consumer is entitled under TIL[A] because that consumer has also availed himself of bankruptcy relief. To do so would require that the consumer choose between bankruptcy and TIL[A], something neither form of statutory relief contemplates.

Essentially, when a borrower rescinds a transaction and the security interest is terminated as a matter of law, the creditor is left with an unsecured debt. Outside a bankruptcy proceeding, this characterization is of little consequence because unsecured debts must otherwise be paid in full, failing which, a creditor may take steps to reacquire a security interest. In a bankruptcy proceeding, however, unsecured debts are paid pro rata and may be discharged without payment. Requiring a Chapter 13 Debtor to tender the full amount of the loan on a creditor's now unsecured claim would unfairly discriminate among unsecured claims in violation of 11 U.S.C. § 1322(a)(3).⁶⁴

Jaaskelainen and cases upon which it relies should be considered a debtor's "best-case scenario" in bankruptcy-related TILA cases. More typical cases include *In re Merriman*,⁶⁵ where the bankruptcy court allowed rescission for a TILA violation but made that avoidance of the mortgage lien conditional upon obtaining refinancing. In so doing, the court relied upon cases such as *Yamamoto v. Bank of New York*.⁶⁶ However, the court also quoted from the administrative interpretation of the tender portion of TILA to support its conclusion, even though this agency interpretation, entitled to deference, could equally well have supported Judge Hillman's decision in *Jaaskelainen*: "The procedures outlined in § 226.23(d)(2) and (3) may be modified by a court. For example, when a consumer is in bankruptcy proceedings and prohibited from returning anything to the creditor, or when the equities dictate, a modification might be made."⁶⁷

Today, where so many debtors in Chapter 13 are "upside-down," conditioning a TILA remedy on refinancing in Chapter 13 is tantamount to saying that there is no remedy at all. Under the present circumstances, cases such as *Jaaskelainen* are the only hope that a Chapter 7 debtor or a Chapter 7 trustee might have in order to meaningfully pursue a TILA claim, either in bankruptcy or in state court proceedings.

Jaaskelainen was recently reversed in the district court⁶⁸ which essentially followed the analysis in *Yamamoto* to the effect that debtor could not rescind without a prior showing that he was able to tender. The court also held that there was no distinction between the context of bankruptcy and non-bankruptcy cases for purposes of tender.

The logic of *Jaaskelainen* as a matter of appellate jurisprudence is questionable. In *Jaaskelainen*, the trial court, as a matter of equity, decided on the application of the tender rule in the circumstances of the case. The district court basically held that as a matter of law, it could not do so.

Home Owners Equity Protection Act

Statute of Limitation—Recoupment

The *Wentz* decision, discussed at length in the TILA section of this article, held that HOEPA claims could be pleaded defensively under the doctrine of recoupment in the context of Chapter 13 cases, even if the applicable one-year statute of limitation had lapsed. Precisely the same reasoning as discussed in the context of TILA applies relative to HOEPA.

Assignee Liability for HOEPA Mortgages—Statute of Limitation

*In re Thomas (Thomas v. Wells Fargo Bank N.A.)*⁶⁹ addressed both statute of limitation defenses as well as mortgagee-assignee liability under HOEPA in the context of a motion to dismiss. Under these circumstances, all well-pleaded facts were treated by the court as true.

In considering whether the assignee might be liable on plaintiff's HOEPA claim, the court first noted:

Pursuant to 15 U.S.C. § 1641(d)(1), assignees of HOEPA mortgages are subject to a more expansive standard of liability than assignees have under TILA. Section 1641(d)(1) states, in pertinent part:

Any person who purchases or is otherwise assigned a mortgage within referred to in section 1602(aa) of this title [referring to mortgages covered by HOEPA] shall be subject to all claims and defenses with respect to that mortgage that the consumer could assert against the creditor of the mortgage, unless the purchaser or assignee demonstrates, by a preponderance of the evidence, that a reasonable person exercising ordinary due diligence, could not determine, based on the documentation required by this subchapter, the itemization of the amount financed, and other disclosure of disbursements that the mortgage was a mortgage referred to in section 1602(aa) of this title.⁷⁰

Having said that, the court concluded that it simply was too early for the case to be dismissed as it was not given an opportunity to demonstrate what it could or could not reasonably have been able to determine from the face of the documents. In addition, the court observed that, unlike a normal loan, assignees of HOEPA loans are subject to any claims or defenses that might have been raised against any of its predecessors in interest, including the loan originator such as the mortgage broker.⁷¹

In *Thomas*, plaintiff-debtor rescinded within three years of the closing but did not commence her case until more than four years after the closing in question. Under these circumstances, the court had to determine whether plaintiff's claim for rescission was time-barred by the applicable statute of limitation. The court observed that there were conflicting decisions on this point:

In *Madura v. Countrywide Home Loans, Inc.*, 2008 WL 2856813 (M.D. Fla. July 22, 2008), the district court observed that two schools of thought have emerged on the aforementioned issue. Under one approach, so long as a consumer has timely exercised her right to rescind, her suit for rescission is not time-barred even if it was filed after the period set forth in § 1635(f). *Id.* at *13. Under the other approach, the consumer must file her suit for rescission within the three year period set forth in § 1635(f); otherwise, the suit is time-barred regardless of whether she provided a timely notice to rescind. *Id.* Based on the Third Circuit's decision *Smith v. Fidelity Consumer Discount Company*, 898 F.2d 896 (3d Cir. 1990), the Third Circuit follows the latter approach.⁷²

Following *Smith*, the bankruptcy court held that the rescission claims were time-barred by the applicable statute of limitation. It held that rescission alone within the three-year period was insufficient. The actual lawsuit had to be commenced within the three-year period in order to preserve the claim within the statute of limitation. The court did not consider the doctrine of recoupment in its decision.

Extension of Statute of Limitation—11 U.S.C.A. § 108

While the statute of limitation for a claim under TILA is typically three years for a rescission claim and one year for a statutory damage claim, § 108 of the Bankruptcy Code offers a trustee an extension of up to two years.⁷³ In *In re Dawson*,⁷⁴ the court was asked to consider whether § 108 allowed an extension to the statute of limitation in a TILA case in favor of a Chapter 13 debtor. The bankruptcy court ultimately held that it did, but the decision was not easily reached.

Section 108, by its express terms, only applies to a debtor. However, the court noted that its provisions have been made available to debtors in possession under Chapters 11 and 12, and, by analogy, some courts have held that Chapter 13 debtors are analogous to Chapter 11 and 12 debtors in possession. The court also noted that the extension privileges in § 108 are not available either to debtors in Chapter 7 or to a debtor in any other chapter of the Code where the debtor is no longer a debtor in possession.

Even though the model plan, which was confirmed, specifically provided that the debtor's property did not revert until plan payments were completed, the debtor commenced an otherwise time-barred claim under TILA during the course of her Chapter 13 case.

The court noted that a debtor does not have the full panoply of rights under Chapter 13. For example, a Chapter 13 debtor does not have the same powers of a Chapter 11 trustee or debtor in possession. However, a debtor in a Chapter 13 case does have the rights of a trustee to "use" property of the estate pursuant to § 1303. The court also noted that, while Congress specifically reserved avoiding powers to the trustee in Chapter 13 cases, the same could not be said about other causes of action, including claims under TILA.

Having concluded that the Chapter 13 debtor had standing to bring such a claim, the court then concluded that the trustee's privilege to extend the statute of limitation pursuant to § 108 also applied to the Chapter 13 debtor. The court was mindful of the plain language reading of the Bankruptcy Code favored by the current Supreme Court. Indeed, the court carefully reviewed the Supreme Court decision in *Hartford Underwriters Insurance Co v. Union Planters Bank, NA*,⁷⁵ holding that only a trustee and not an administrative creditor could surcharge collateral pursuant to § 506(c).

In contrast, the court interpreted §108(a) as a modification of the limitations on a trustee's power under § 363. Since § 108(a) applies in Chapter 13, the court found that it would be incongruous to deprive that section of its utility by making it unavailable to debtors. This position is hard to square with the "plain language" of the Bankruptcy Code. One could argue that in order to take advantage of the provisions of § 108(a), the claim involved would have to be brought by the trustee, who also would have standing to pursue the claim in his name and for the benefit of the Chapter 13 estate. However, the court anticipated this argument and pointed out that the better-reasoned decisions held that such causes of action belong to the debtor and not to the trustee.

Further, if the case were converted to Chapter 7, 11, or 12, the powers of section 108(a) would spring to life even though not available to the debtor in Chapter 13. The court considered this to be an anomalous result and found it would be contrary to congressional intent.

Mortgage Rescue Fraud—Equitable Mortgage

*In re Brannan*⁷⁶ addressed several points in connection with a sale-leaseback transaction in the nature of a mortgage rescue fraud. The debtor in Chapter 13 sought to avoid this transaction on the grounds of fraud as well as TILA. The court carefully considered Virginia law to determine that the transaction, while facially a transfer by deed, was in fact an equitable mortgage. Since it was a mortgage, the court concluded that TILA applied and that there was inadequate disclosure in the transaction. The court also concluded that the debtor could invoke avoiding powers to preserve her exemption pursuant to § 522(h) of the Bankruptcy Code where the Chapter 13 trustee had not invoked avoiding powers on her behalf.

It can be argued that the right to invoke avoiding powers where the trustee does not might be an additional ground for allowing a debtor in Chapter 13 to avail herself of the extension to the statute of limitation pursuant to § 108. However, this was not implicated in any manner in *Brannan*. The court did not finalize its decision because the holder of a second mortgage, who should have been joined, had not been.

Lien Stripping

No Lien Stripping in Chapter 13 Where Discharge Is Not Available

In *In re Jarvis*,⁷⁷ the debtor filed a Chapter 13 case shortly after having obtained a Chapter 7 discharge in a prior case. In the parlance of some consumer bankruptcy attorneys, Jarvis was attempting to file a "Chapter 20." By reason of having received a discharge in the Chapter 7 case in the immediately prior year, the debtor was in-

eligible for a discharge in the subsequent Chapter 13 pursuant to § 1328(f)(1) of the Bankruptcy Code.

Nevertheless, the debtor asserted that a mortgagee held a fully unsecured junior lien on his home, and he filed a Chapter 13 plan seeking to strip off that lien and declare it to be void pursuant to § 506(d). While fully unsecured mortgage liens may not be stripped off in a Chapter 7 case, as held by *Dewsnup v. Timm*,⁷⁸ that court left undetermined the question of what happens to fully unsecured liens in other chapters of the Bankruptcy Code.

*Nobelman v. American Savings Bank*⁷⁹ instructs that a partially unsecured loan solely secured by residential real estate may not be bifurcated into both secured and unsecured portions. However, nothing in *Nobelman* addressed the right to completely strip off a fully unsecured loan secured by residential real estate. Accordingly, the court in *Jarvis* appropriately noted:

Many courts have held that, when a junior lien is totally unsecured because the senior liens exceed the value of the property, the anti-modification provisions of §1322(b)(2) relating to residential property do not apply. *See, e.g., In re McDonald*, 205 F.3d 606 (3d Cir. 2000); *In re Pond*, 252 F.3d 122 (2d Cir. 2001); *In re Lane*, 280 F.3d 663 (6th Cir. 2002); *In re Holloway*, 2001 WL 1249053 (N.D. Ill. 2001); *In re Waters*, 276 B.R. 879 (Bankr. N.D. Ill. 2002); *In re King*, 290 B.R. 641 (Bankr. C.D. Ill. 2003). *Contra In re Barnes*, 207 B.R. 588 (Bankr. N.D. Ill. 1997).

In *King*, the requirements for the strip off of a totally unsecured lien were outlined. The proposed strip off may be raised as a contested matter and presented as a provision in a Chapter 13 plan. A separate adversary proceeding is not necessary. *King*, 290 B.R. at 647-48. However, the plan provisions must be sufficiently detailed to give the creditor clear notice of the intended treatment of its claim. In addition to identifying the creditor and its claim specifically, the plan must provide “explanatory detail” to advise the creditor of the basis for the lien strip off. *Id.* at 649. Finally, although the “lien-avoiding effect of the confirmed plan” is established at confirmation, actual lien avoidance is contingent upon the debtor completing the plan and receiving a discharge.⁸⁰

Jarvis then addressed whether the debtor could obtain the result of lien stripping where the debtor was not eligible for a discharge in that case. Prior to BAPCPA, there was no waiting period from the time of a discharge under any chapter to a subsequent discharge under Chapter 13. BAPCPA did impose such a waiting period. Therefore, the court held that, absent the availability of a Chapter 13 discharge, a debtor could not obtain a lien strip in the subsequently-filed Chapter 13 case.

Lien Stripping in Chapter 13 Is Not Limited to Garden-Variety Mortgage Liens

*In re Korbe*⁸¹ addressed the contention that a wholly unsecured mortgage in favor of the U.S. Department of Housing and Urban Development (HUD) could not be stripped

off in a Chapter 13 case. The bankruptcy court found that a HUD loan was like any other loan, subject to lien stripping in Chapter 13. In so holding, the court stated:

This Court will not undo the statutory scheme set forth in the Bankruptcy Code. *Artuz v. Bennett*, 531 U.S. 4, 10 (2000) (“Whatever merits these and other policy arguments may have, it is not the province of this Court to rewrite the statute to accommodate them.”); *Harris v. Garner*, 216 F.3d 970, 976 (11th Cir. 2000) (en banc) (“We will not do to the statutory language what Congress did not do with it, because the role of the judicial branch is to apply statutory language not rewrite it.”). As a result, the Court will afford HUD the same treatment afforded to other creditors similarly situated under 11 U.S.C. § 506. That is, HUD is not immune from the lien stripping provisions of 11 U.S.C. § 506(a) and (d). *Cf.*, *Johnson v. The Internal Revenue Service et al.*, ___ B.R. ___, Adv. No. 07-2077, 2008 WL 1743950 (Bankr. W.D. Pa., April 16, 2008) (holding that the liens of the IRS and Pennsylvania Department of Labor and Industry may be stripped away pursuant to 11 U.S.C. §§ 506(a) and (d) in a reorganization under Chapter 11).⁸²

In *In re Johnson*,⁸³ the court allowed a Chapter 11 debtor to strip off fully unsecured liens in favor of the Internal Revenue Service and the Pennsylvania Department of Labor and Industry (whose lien was for state unemployment taxes). The IRS stipulated that the amount of its lien exceeded the value of the debtor’s assets. It also stipulated that its claim be allowed as follows: (1) a secured claim of \$ 41,374.83 (the value of debtor’s unencumbered personal property); (2) an unsecured priority claim of \$ 30,592.52; and (3) a general unsecured claim of \$109,079.

After analyzing § 506(a) and (d) in light of *Dewsnup*, the court concluded that the question of lien stripping in Chapter 11 and 13 remained open:

A great majority of the courts that have considered the issue in reorganization cases have concluded that the holding in *Dewsnup* should be limited to Chapter 7 cases and should not prevent lien stripping in reorganization cases. See 4-506 Collier on Bankruptcy, 15th ed. Rev. ¶ 506.06[1][c] (2007); *Sapos v. Provident Inst. of Savs. in the Town of Boston*, 967 F.2d 918, 925 (3d Cir.1992) (*Dewsnup* Court’s interpretation of Section 506 in a Chapter 7 liquidation does not apply in a Chapter 13 reorganization); *Wade v. Bradford*, 39 F.3d 1126 (10th Cir.1994) (Chapter 11 debtors could strip down lien on residence notwithstanding *Dewsnup*); *Harmon v. U.S. Through Farmers Home Admin.*, 101 F.3d 574 (8th Cir.1996) (allowing lien stripping in Chapter 12); *In re Jones*, 152 B.R. 155, 173 (Bankr.E.D.Mich. 1993) (categorically prohibiting lien stripping in Chapter 11 would disrupt established pre-Code law).

Many of the courts so limiting the *Dewsnup* holding have noted that a general prohibition against lien stripping in reorganization cases would be inconsistent with pre-Bankruptcy Code law, and would conflict with key provisions and principles applicable in the reorganization chapters of the Bankruptcy Code. This

Court agrees with the majority view and concludes that the holding in *Dewsnup* does not extend to cases filed under Chapter 11 of the Bankruptcy Code.⁸⁴

The court noted that this result was a continuation of a long-standing aspect of reorganization cases, that predates the adoption of the current Bankruptcy Code in 1978.⁸⁵ The court concluded that permitting lien stripping in a Chapter 11 reorganization was consistent with pre-Code practice. The implication from this holding is that the same result would be obtained in a Chapter 12 or 13 case.

Interestingly, the court adverted to the existence of the § 1111(b) election as a reason to permit lien stripping in Chapter 11. However, there is no comparable provision in Chapter 13. Practice in the majority of courts having considered the issue does not suggest that this is a distinction with a difference. The court also noted that current Chapter 11, like Chapter 13, prohibits modification of mortgages secured only by a security interest in real property that is the debtor's residence. Since Chapter 13 has allowed lien stripping, the court concluded that Chapter 11 now does as well.

Having concluded that Chapter 11 permits lien stripping, the court next concluded that there is nothing in particular in either the revenue lien's or statutory state tax lien's nature that would preclude it from being stripped in a Chapter 11 case (or by implication in a Chapter 13 case).

In *In re Dever*, supra, after a long and thoughtful discussion on various aspects of lien stripping, the court noted that Section 506 does not distinguish between voluntary and involuntary liens. It held that if a voluntary lien is avoidable by a strip down in Chapter 11, then so too should an involuntary one, like an IRS lien. 164 B.R. at 144. The *Dever* court further stated:

Nothing in Sections 506 or 1129 suggests that IRS liens or claims are totally immune from avoidance or modification. Under the Bankruptcy Code, the IRS is the beneficiary of several specific provisions that reflect Congressional desire to protect the federal fisc. For example, Congress required that all tax obligations must be paid under a Chapter 11 plan within six years of assessment date. Section 1129(a)(9)(C). Certain tax obligations are entitled to priority under Section 507(a)(7). Section 523(a)(1) makes some tax debts nondischargeable. Although none of the obligations here are alleged to be nondischargeable, most debtors facing IRS liens would not be able to walk out of bankruptcy court in complete defiance of their tax obligations. The granting of IRS priorities and the nondischargeable nature of many such obligations are strong evidence that Congress provided an alternative method of realizing on such claims. Reading an IRS exception into Section 506 to prevent avoidance of the liens here is unnecessary and inappropriate.

164 B.R. at 145.⁸⁶

The court also distinguished cases relied upon by the IRS to the contrary as having pertained to a situation where the revenue lien was undersecured as opposed to fully unsecured.

Conclusion

Residential mortgages in bankruptcy continue to be the subject of complex and intricate litigation. Much of the litigation occurs in the context of motion practice, although substantial litigation continues to arise in adversary proceedings under the Truth in Lending Act, the Real Estate Settlement Procedures Act, the Home Owners Equity Protection Act, and state consumer protection laws. Further litigation can be anticipated in 2009 and following years if Congress enacts mortgage modification legislation. Both the debtors' and creditors' bar should give sharper focus to these issues so that they can be handled in an efficient and effective matter, particularly in light of the current economic conditions facing our country in general and the residential real estate sector in particular.

NOTES

1. *Associates Commercial Corp. v. Rash*, 520 U.S. 953, 117 S. Ct. 1879, 138 L. Ed. 2d 148, 30 Bankr. Ct. Dec. (CRR) 1254, 37 *Collier Bankr. Cas.* 2d (MB) 744, *Bankr. L. Rep.* (CCH) P 77409 (1997).
2. *Till v. SCS Credit Corp.*, 541 U.S. 465, 124 S. Ct. 1951, 158 L. Ed. 2d 787, 43 *Bankr. Ct. Dec.* (CRR) 2, 51 *Collier Bankr. Cas.* 2d (MB) 642, *Bankr. L. Rep.* (CCH) P 80099 (2004).
3. Available online at <http://www.treasury.gov/press/releases/tg33.htm>.
4. 11 U.S.C.A. § 362(a); *Matter of Vitreous Steel Products Co.*, 911 F.2d 1223, 1231, *Bankr. L. Rep.* (CCH) P 73583, 12 *U.C.C. Rep. Serv.* 2d 549 (7th Cir. 1990).
5. See 11 U.S.C.A. § 362(d); *Vitreous Steel*, 911 F.2d at 1232; *Matter of Boomgarden*, 780 F.2d 657, 663, *Bankr. L. Rep.* (CCH) P 70891 (7th Cir. 1985).
6. *Vitreous Steel*, 911 F.2d at 1232; *In re Johnson*, 756 F.2d 738, 740, 13 *Bankr. Ct. Dec.* (CRR) 431, 12 *Collier Bankr. Cas.* 2d (MB) 573, *Bankr. L. Rep.* (CCH) P 70350 (9th Cir. 1985).
7. *Vitreous Steel*, 911 F.2d at 1232
8. 11 U.S.C.A. § 101(10).
9. 11 U.S.C.A. § 101(5).
10. *In re Woodberry*, 383 B.R. 373, 65 *U.C.C. Rep. Serv.* 2d 228 (*Bankr. D. S.C.* 2008).
11. *Woodberry*, 383 B.R. at 379. See *Fed. R. Bankr. P.* 7017.
12. See, e.g., *In re Tainan*, 48 B.R. 250, 252 (*Bankr. E.D. Pa.* 1985) (servicer, as representative of holder for collection purposes, was real party in interest with standing to seek relief from automatic stay); *Bankers Trust (Delaware) v. 236 Beltway Inv.*, 865 F. Supp. 1186, 1191, 26 *U.C.C. Rep. Serv.* 2d 776 (*E.D. Va.* 1994) (in light of terms of pooling agreement, both trustee and servicer had standing to foreclose and sue for deficiency); *In re O'Dell*, 268 B.R. 607, 618 (*N.D. Ala.* 2001), *aff'd*, 305 F.3d 1297, *Bankr. L. Rep.* (CCH) P 78723, 53 *Fed. R. Serv.* 3d 1285 (11th Cir. 2002) (servicer allowed to file and prosecute proof of claim on behalf of debt-holder); *In re Miller*, 320 B.R. 203, 206 n.2 (*Bankr. N.D. Ala.* 2005) (acknowledging servicing agent's authority to litigate motion for relief from stay on behalf of securitized trust).
13. *In re Conde-Dedonato*, 391 B.R. 247 (*Bankr. E.D. N.Y.* 2008).
14. See *Fed. R. Bankr. P.* 3001(b).
15. 11 U.S.C.A. § 101(10)(A).
16. 11 U.S.C.A. § 101(5)(A) and (B).
17. See *In re Viencsek*, 273 B.R. 354, 359 (*Bankr. N.D. N.Y.* 2002); see also *Greer v. O'Dell*, 305 F.3d 1297, 1302, *Bankr. L. Rep.* (CCH) P 78723, 53 *Fed. R. Serv.* 3d 1285 (11th Cir. 2002) (holding that loan servicer was a party in interest in proceedings involving loans that it services); *Bankers Trust*, 865 F. Supp. at 1191 (holding that both the lender and servicer

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had standing to sue on mortgagor's default even though the servicer was not the holder of the mortgage); Tainan, 48 B.R. at 252 (determining that mortgage servicer was a party in interest for purposes of a relief from stay proceeding).

18. Viencek, 273 B.R. at 358.
19. In re Hayes, 393 B.R. 259, 60 Collier Bankr. Cas. 2d (MB) 212 (Bankr. D. Mass. 2008).
20. Massachusetts Local Bankruptcy Rule 4001-1(b)(f).
21. Hayes, 393 B.R. at 268.
22. In re Nosek, 386 B.R. 374, 380 (Bankr. D. Mass. 2008), *aff'd* in part, vacated in part, 2009 WL 1473429 (D. Mass. 2009).
23. Hayes, 393 B.R. at 268-69.
24. Hayes, 393 B.R. at 269.
25. Nosek, 386 B.R. 374.
26. In re Kang Jin Hwang, 396 B.R. 757, 67 U.C.C. Rep. Serv. 2d 319 (Bankr. C.D. Cal. 2008).
27. See Fed. R. Civ. P. 19, incorporated by reference pursuant to Fed. R. Bankr. P. 7019.
28. See Fed. R. Civ. P. 17, incorporated by reference pursuant to Fed. R. Bankr. P. 7017.
29. Hwang, 396 B.R. at 766.
30. Hwang, 396 B.R. at 766 (citing *Warth v. Seldin*, 422 U.S. 490, 95 S. Ct. 2197, 45 L. Ed. 2d 343 (1975)).
31. Hwang, 396 B.R. at 768.
32. In re Stewart, 391 B.R. 327 (Bankr. E.D. La. 2008).
33. Stewart, 391 B.R. at 357.
34. Wells Fargo Bank, N.A. v. Jones, 391 B.R. 577 (E.D. La. 2008).
35. In re Stewart, 2008 WL 5096011, *3 (Bankr. E.D. La. 2008).
36. Stewart, 2008 WL 5096011 at *13.
37. In re Parsley, 384 B.R. 138 (Bankr. S.D. Tex. 2008)
38. Parsley, 384 B.R. at 175-77.
39. In re Schuessler, 386 B.R. 458 (Bankr. S.D. N.Y. 2008).
40. In re Rodriguez, 391 B.R. 723 (Bankr. D. N.J. 2008).
41. In re Prevo, 394 B.R. 847 (Bankr. S.D. Tex. 2008).
42. Prevo, 394 B.R. at 848.
43. Bankruptcy Rule 3001 states the terms on which a proof of claim is to be filed. If a proof of claim is filed with supporting documentation, it is *prima facie* valid. In contrast, a claim not filed in accordance with Bankruptcy Rule 3001 is not *prima facie* valid, and the creditor has the burden of proof and of going forward with evidence in order to establish its claim.
44. See 12 U.S.C.A. § 2605(e)(1)(A) and (B)(2); 12 U.S.C.A. Regulation X, 24 C.F.R. § 3500.21.
45. In re Laskowski, 384 B.R. 518 (Bankr. N.D. Ind. 2008).
46. In re Payne, 387 B.R. 614 (Bankr. D. Kan. 2008).
47. In re Holland, 2008 WL 4809493 (Bankr. D. Mass. 2008).
48. In re Wentz, 393 B.R. 545 (Bankr. S.D. Ohio 2008).
49. In re Thompson, 350 B.R. 842, 852 (Bankr. E.D. Wis. 2006); *Bull v. U.S.*, 1935-1 C.B. 310, 295 U.S. 247, 262, 55 S. Ct. 695, 79 L. Ed. 1421, 35-1 U.S. Tax Cas. (CCH) P 9346, 15 A.F.T.R. (P-H) P 1069 (1935). “[A]ctions by way of recoupment have been recognized by court decision in a broad variety of federal statutory settings including the bankruptcy code, the internal revenue code, and prior to Congressional clarification-in regard to TILA.” *Thompson*, 350 B.R. at 852, citing *Integra Bank/Pittsburgh v. Freeman*, 839 F. Supp. 326, 330, n. 6 (E.D.

Pa. 1993). See also *In re Harvey*, 2003 WL 21460063, *7-8 (Bankr. E.D. Pa. 2003) (allowing otherwise time-barred RESPA claims in recoupment).

50. *In re Johnson*, 384 B.R. 763 (Bankr. E.D. Mich. 2008).
51. 12 U.S.C.A. § 2609(b); 24 C.F.R. § 3500.17(b).
52. 24 C.F.R. § 3500.17(i)(2).
53. *Rodriguez*, 391 B.R. 723.
54. 15 U.S.C.A. § 1635(b); 12 C.F.R. § 226.23(d)(3) (2007).
55. *In re Ebron*, 2008 WL 819888 (Bankr. E.D. Va. 2008).
56. *Taylor v. Quality Hyundai, Inc.*, 150 F.3d 689, 695 (7th Cir. 1998); *Walker v. Wallace Auto Sales, Inc.*, 155 F.3d 927, 936 (7th Cir. 1998); *Ellis v. General Motors Acceptance Corp.*, 160 F.3d 703, 709, *Prod. Liab. Rep. (CCH) P 17503* (11th Cir. 1998); *Green v. Levis Motors, Inc.*, 179 F.3d 286, 295 (5th Cir. 1999); *Balderos v. City Chevrolet*, 214 F.3d 849, 853, *R.I.C.O. Bus. Disp. Guide (CCH) P 9893* (7th Cir. 2000); *Ramadan v. Chase Manhattan Corp.*, 229 F.3d 194, 198 (3d Cir. 2000); *Irby-Greene v. M.O.R., Inc.*, 79 F. Supp. 2d 630, 633-34 (E.D. Va. 2000)); *Knapp v. Americredit Financial Services, Inc.*, 245 F. Supp. 2d 841, 848 (S.D. W. Va. 2003); *Coleman v. General Motors Acceptance Corp.*, 196 F.R.D. 315, 47 Fed. R. Serv. 3d 1182 (M.D. Tenn. 2000), order vacated, 296 F.3d 443, 53 Fed. R. Serv. 3d 75, 2002 FED App. 0244P (6th Cir. 2002).
57. *In re Wentz*, 393 B.R. 545 (Bankr. S.D. Ohio 2008).
58. See 15 U.S.C.A. § 1640(e) (one-year statute of limitation for damage claims pursuant to TILA and HOEPA); 12 U.S.C.A. § 2614 (one-year statute of limitation for damage claims pursuant to RESPA).
59. See *Continental Acceptance Corp. v. Rivera*, 50 Ohio App. 2d 338, 4 Ohio Op. 3d 287, 363 N.E.2d 772, 776-78 (8th Dist. Cuyahoga County 1976) (allowing a recoupment claim despite the otherwise applicable TILA statute of limitation of 15 U.S.C.A. § 1640). Other bankruptcy court decisions have similarly ruled that a proof of claim constitutes “an action to collect a debt.” See, e.g., *In re Soto*, 221 B.R. 343, 359 (Bankr. E.D. Pa. 1998). But cf. *Williams v. Countrywide Home Loans, Inc.*, 504 F. Supp. 2d 176, 188 (S.D. Tex. 2007), *aff’d*, 269 Fed. Appx. 523 (5th Cir. 2008).
60. *In re Jaaskelainen*, 391 B.R. 627 (Bankr. D. Mass. 2008).
61. *Jaaskelainen*, 391 B.R. at 641-42.
62. *Jaaskelainen*, 391 B.R. at 642-43.
63. *In re Myers*, 175 B.R. 122 (Bankr. D. Mass. 1994); and *In re Whitley*, 177 B.R. 142 (Bankr. D. Mass. 1995).
64. *Jaaskelainen*, 391 B.R. at 645-46.
65. *In re Merriman*, 329 B.R. 710 (D. Kan. 2005).
66. *Yamamoto v. Bank of New York*, 329 F.3d 1167 (9th Cir. 2003).
67. *Merriman*, 329 B.R. at 744.
68. *Wells Fargo Bank, N.A. v. Jaaskelainen*, 2009 WL 1586702 (D. Mass. 2009).
69. *In re Thomas*, 2008 WL 5412113 (Bankr. E.D. Pa. 2008).
70. *Thomas*, 2008 WL 5412113 at *5.
71. See *In re Barber*, 266 B.R. 309, 320 (Bankr. E.D. Pa. 2001) (holding that 15 U.S.C.A. § 1641(d)(1) subjected the original lender’s assignee to cause of action which mortgagee could assert under the UTPCPL against the original lender). Based on § 1640(d)(1), it will be Wells Fargo’s burden to establish that a reasonable person exercising due diligence could not have determined, by reviewing the items listed in § 1641(d)(1), that the mortgage was subject to HOEPA. See *Short v. Wells Fargo Bank Minnesota, N.A.*, 401 F. Supp. 2d 549, 555 (S.D. W. Va. 2005) (observing that an assignee may raise as a defense to assignee liability under § 1641(d)(1) that it was without notice that the loan in question was a HOEPA loan).

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72. Thomas, 2008 WL 5412113 at *7.
73. 11 U.S.C.A. § 108.
74. In re Dawson, 2008 WL 1700419 (Bankr. D. D.C. 2008).
75. Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A., 530 U.S. 1, 120 S. Ct. 1942, 147 L. Ed. 2d 1, 36 Bankr. Ct. Dec. (CRR) 38, 43 Collier Bankr. Cas. 2d (MB) 861, Bankr. L. Rep. (CCH) P 78183 (2000).
76. In re Brannan, 2008 WL 1752206 (Bankr. E.D. Va. 2008), amended in part, 2008 WL 4526217 (Bankr. E.D. Va. 2008).
77. In re Jarvis, 390 B.R. 600 (Bankr. C.D. Ill. 2008).
78. Dewsnup v. Timm, 502 U.S. 410, 112 S. Ct. 773, 116 L. Ed. 2d 903, 22 Bankr. Ct. Dec. (CRR) 750, 25 Collier Bankr. Cas. 2d (MB) 1297, Bankr. L. Rep. (CCH) P 74361A (1992).
79. Nobelman v. American Sav. Bank, 508 U.S. 324, 113 S. Ct. 2106, 124 L. Ed. 2d 228, 24 Bankr. Ct. Dec. (CRR) 479, 28 Collier Bankr. Cas. 2d (MB) 977, Bankr. L. Rep. (CCH) P 75253A (1993).
80. Jarvis, 390 B.R. at 604.
81. In re Korbe, 386 B.R. 585, 59 Collier Bankr. Cas. 2d (MB) 1185 (Bankr. W.D. Pa. 2008).
82. Korbe, 386 B.R. at 589-90.
83. In re Johnson, 386 B.R. 171, 49 Bankr. Ct. Dec. (CRR) 237, 2008-1 U.S. Tax Cas. (CCH) P 50300, 101 A.F.T.R.2d 2008-1798 (Bankr. W.D. Pa. 2008).
84. Johnson, 386 B.R. at 175.
85. See Dewsnup, 502 U.S. at 418-19.
86. Johnson, 386 B.R. at 178.