97th Annual National Conference of Bankruptcy Judges
October 11–14, 2023 Austin, TX

Interesting Consumer Issues: When I Find Myself in Times of Trouble

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I. Chapter 13 Voluntary Dismissals and Lien Carve-Outs

A. The Debtor's Right to Dismiss a Chapter 13 Case

Query: Is the Debtor's right to dismiss a chapter 13 case truly absolute?

1. *Relevant Bankruptcy Code Provisions*

§ 1307(b) On request of the debtor at any time, if the case has not been converted under section 706, 1112, or 1208 of this title, the court shall dismiss a case under this chapter. Any waiver of the right to dismiss under this subsection is unenforceable.

§ 1307(c) Except as provided in subsection (f) of this section, on request of a party in interest or the United States trustee and after notice and a hearing, the court may convert a case under this chapter to a case under chapter 7 of this title, or may dismiss a case under this chapter, whichever is in the best interests of creditors and the estate, for cause, including—

(1) unreasonable delay by the debtor that is prejudicial to creditors;

(2) nonpayment of any fees and charges required under chapter 123 of title 28;

(3) failure to file a plan timely under section 1321 of this title;

(4) failure to commence making timely payments under section 1326 of this title;

(5) denial of confirmation of a plan under section 1325 of this title and denial of a request made for additional time for filing another plan or a modification of a plan;

(6) material default by the debtor with respect to a term of a confirmed plan;

(7) revocation of the order of confirmation under section 1330 of this title, and denial of confirmation of a modified plan under section 1329 of this title;

(8) termination of a confirmed plan by reason of the occurrence of a condition specified in the plan other than completion of payments under the plan;

(9) only on request of the United States trustee, failure of the debtor to file, within fifteen days, or such additional time as the court may allow, after

the filing of the petition commencing such case, the information required by paragraph (1) of section 521(a);

(10) only on request of the United States trustee, failure to timely file the information required by paragraph (2) of section 521(a); or

(11) failure of the debtor to pay any domestic support obligation that first becomes payable after the date of the filing of the petition.

2. *Caselaw*

a. ***Law v. Siegel***, 571 U.S. 415, 427–28 (2014) – In exercising the Bankruptcy Code's statutory and inherent powers, a bankruptcy court may not contravene specific statutory provisions; the bankruptcy court has authority to respond to debtor misconduct with meaningful sanctions that do not contravene the Code.

b. ***In re Mills***, 539 B.R. 879, 887 (Bankr. D. Kan. 2015) – "*Law v. Siegel* precludes bankruptcy courts from crafting a bad faith exception to a chapter 13 debtor's voluntary dismissal. Chapter 13 is a voluntary remedy only; in the absence of specific statutory direction, a debtor should be able to exit without risking being subjected to involuntary liquidation without the due process protections afforded involuntary debtors by § 303. If a debtor commits sanctionable wrongdoing in the course of the case, the court has many means of addressing that other than forced liquidation premised on a shaky legal foundation."

c. ***In re Pustejovsky***, 577 B.R. 671, 674 (Bankr. W.D. Tex. 2017) – There is a bad faith exception to a debtor's right to dismiss a chapter 13 case. "Interpreting the word *shall* as mandatory in § 1307(b), without a bad faith exception, would create absurd results because sections of the Code must be read together and harmonized." An absolute right to dismiss under § 1307(b) would render § 1307(c) meaningless.

d. ***In re Fulayter***, 615 B.R. 808, 815 (Bankr. E.D. Mich. 2020) – A chapter 13 debtor's right to dismiss under § 1307(b) is not subject to a "bad actor" exception, even where there is a pending motion by another party to convert the case to chapter 7. The Code "does not require a debtor seeking dismissal to give any reason, explain any motive, or show any facts." The Code sets no temporal limitations; it simply requires a debtor to make a request to dismiss, and, so long as the case was not previously converted from chapter 7, 11, or 12, the bankruptcy court has no discretion in the matter and "shall" dismiss the case.

e. ***In re Minogue***, 632 B.R. 287, 292 (Bankr. D.S.C. 2021) – Given the clear instruction of *Law v. Siegel* and *Marrama v. Citizens Bank of Mass.*, 549 U.S. 365 (2007), a chapter 13 debtor may voluntarily dismiss his or her case despite a pending motion to convert or allegations of bad faith conduct.

f. ***In re Hunter***, No. 19-30213 (Bankr. W.D.N.C. January 12, 2023) – Debtors have a right to voluntarily dismiss a chapter 13 case, but they do not have a right to disregard court orders. The court held that the debtor had to first comply with an order requiring turnover to the trustee of certain funds resulting from the sale of the debtor's home before the court would allow the debtor to dismiss his case.

B. <u>Lien Carve-Outs in Aid of the Trustee's Sale of the Debtor's Property</u>

Query: Can the trustee negotiate carve-outs with secured creditors to facilitate a sale of the debtor's property?

1. *Relevant Bankruptcy Code Provisions*

§ 724(b) – Property in which the estate has an interest and that is subject to a lien that is not avoidable under this title (other than to the extent that there is a properly perfected unavoidable tax lien arising in connection with an ad valorem tax on real or personal property of the estate) and that secures an allowed claim for a tax, or proceeds of such property, shall be distributed—

(1) first, to any holder of an allowed claim secured by a lien on such property that is not avoidable under this title and that is senior to such tax lien;

(2) second, to any holder of a claim of a kind specified in section 507(a)(1)(C) or 507(a)(2) (except that such expenses under each such section, other than claims for wages, salaries, or commissions that arise after the date of the filing of the petition, shall be limited to expenses incurred under this chapter and shall not include expenses incurred under chapter 11 of this title), 507(a)(1)(A), 507(a)(1)(B), 507(a)(3), 507(a)(4), 507(a)(5), 507(a)(6), or 507(a)(7) of this title, to the extent of the amount of such allowed tax claim that is secured by such tax lien;

(3) third, to the holder of such tax lien, to any extent that such holder's allowed tax claim that is secured by such tax lien exceeds any amount distributed under paragraph (2) of this subsection;

(4) fourth, to any holder of an allowed claim secured by a lien on such property that is not avoidable under this title and that is junior to such tax lien;

(5) fifth, to the holder of such tax lien, to the extent that such holder's allowed claim secured by such tax lien is not paid under paragraph (3) of this subsection; and

(6) sixth, to the estate.

2. *Caselaw*

a. ***In re Reeves***, No. 10-02562-8-SWH, 2011 WL 841238, at *3 (Bankr. E.D.N.C. Mar. 8, 2011), *aff'd sub nom*. *Reeves v. Callaway*, 546 Fed. Appx. 235 (4th Cir. 2013) – The fact that the debtor would, in the absence of unavoidable tax liens, be entitled to claim an exemption does not prevent the trustee from selling the property and distributing the proceeds in accordance with § 724(b), where the IRS agreed to a carve-out of 30% to pay administrative claims and unsecured creditors.

b. ***Law v. Siegel***, 571 U.S. 415, 425 (2014) – Federal law provides no authority for bankruptcy courts to deny an exemption on a ground not specified in the Bankruptcy Code.

c. ***In re Turnage***, 644 B.R. 656, 666 (Bankr. W.D.N.C. 2022), *aff'd sub nom. Summerlin v Turnage*, 648 B.R. 793, 799 (W.D.N.C. 2023) – The trustee could not rely on § 724(b) and a voluntary carve-out for unsecured creditors agreed to by the tax lien holder in order to justify the sale of property, where the only priority claims to pay were the administrative claims generated by the sale of the property and the trustee would not pay the debtor's exemption because the "proposal would not benefit the Debtor's estate and would violate the principle that trustees should not administer property solely for the benefit of secured creditors and/or themselves."

d. ***Jubber v. Bird (In re Bird)***, 577 B.R. 365, 384–88 (B.A.P. 10th Cir. 2017) – The trustee was not entitled to compensation for selling property in which the IRS had subordinated claims because the sale generated only a small amount for unsecured creditors at the expense of the debtor's ability to retain the home in contravention of the Code's fresh start policy.

II. When Procedural Rules and Forms Become Substantive: A Look at Key Rules and Chapter 13 Form Plan Provisions from Various Jurisdictions

A. <u>Introduction</u>

Although we all work within the same statutory framework for chapter 13, courts around the country take different approaches to the administration of chapter 13 cases. For instance, some are in conduit-jurisdictions, where all payments are channeled through the trustee's office, and others are in non-conduit jurisdictions, where the debtors make direct post-petition payments to their secured creditors. However, these are not the only differences that are remarkable. There are several procedural differences that are encapsulated in the local rules and form plans used across the country. The three categories that are the focus of this discussion are sale/lease of property, incurrence of post-petition debt or re-financing, and the timing/impact of vesting property of the estate in the debtor.

B. Motions to Sell/Incur Debt

Query: Does an individual debtor have the power to sell his or her residential property without court approval? Does it matter if the case has been confirmed? Does it matter if the property has vested in the debtor under § 1327(b)?

1. *Relevant Bankruptcy Code Provisions*

§ 1303 Subject to any limitations on a trustee under this chapter, the debtor shall have, exclusive of the trustee, the rights and powers of a trustee under sections 363(b), 363(d), 363(e), 363(f), and 363(l), of this title.

§ 363(b) [sales/lease of property not in the ordinary course]

§ 363(c) [sales/lease of property in the ordinary course where debtor is engaged in business]

§ 363(f) [sales free and clear of liens]

§ 363(l) Subject to the provisions of section 365, the trustee may use, sell, or lease property under subsection (b) or (c) of this section, or a plan under chapter 11, 12, or 13 of this title may provide for the use, sale, or lease of property . . . .

§ 1304(b) Unless the court orders otherwise, a debtor engaged in business may operate the business of the debtor and, subject to any limitations on a trustee under sections 363(c) and 364 of this title and to such limitations or conditions as the court prescribes, shall have, exclusive of the trustee, the rights and powers of the trustee under such sections.

§ 364(a) [obtaining unsecured debt as an administrative expense, secured debt on property of the estate not otherwise liened or as a junior lien, and priming liens/adequate protection]

2. *Caselaw*

a. ***In re Loden***, 572 B.R. 211, 215 (Bankr. W.D. Ark. 2017) – The debtor has the ability to obtain post-petition debt without court authorization unless payments are to be made through the plan.

b. ***In re Fields***, 551 B.R. 424, 427–28 (Bankr. D. Minn. 2016) – Nothing in the Bankruptcy Code requires court authorization for a debtor in chapter 13 who is not engaged in business to incur post-petition debt or to obtain credit.

c. ***GMAC v. Bullock* (*In re Bullock*)**, No. 89-11537, 1990 WL 10007465, at *1 (Bankr. S.D. Ga. 1990) – In the absence of a court order to the contrary, a debtor may engage in post-confirmation debt transactions without prior approval.

d. ***In re Ripley***, No. 14-01265-DMW, 2018 WL 735342, at *4 (Bankr. E.D.N.C. Feb. 6, 2018); ***In re Ward***, 546 B.R. 667, 679 (Bankr. N.D. Tex. 2016) – Court approval is necessary for a significant post-petition debt, if for no other reason, that because of its possible impact on the plan.

e. ***In re Nacci***, 586 B.R. 733, 737 (Bankr. N.D. Ohio 2018) – The terms of a confirmed plan required court approval of post-petition debt exceeding $500.

f. ***In re Alomia***, No. 17-00561-5-DMW, 2017 WL 3994811, at *1 (Bankr. E.D.N.C. Sept. 8, 2017) – Local rules prohibited chapter 13 debtors from incurring debt of $7,500 or more without prior court approval.

C. <u>Vesting: When Does It Occur and Is There a Choice for Debtors?</u>

Query: Is it the debtor's choice whether to vest on confirmation or discharge? Can the Court mandate vesting at discharge?

1. *Relevant Bankruptcy Code Provisions*

§ 1306(a)(1) [property acquired by the debtor after the commencement of the case is property of the estate until the case is closed, dismissed, or converted, whichever occurs first]

§ 1322(b)(9) Subject to subsections (a) and (c) of this section, the plan may . . . provide for the vesting of property of the estate, on confirmation of the plan or at a later time, in the debtor or in any other entity.

§ 1327(b) Except as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor.

2. *Caselaw*

Trantham v. Tate, 647 B.R. 139, 141–42, 145 (W.D.N.C. 2022), *appeal filed*, 4th Cir., Dec. 9, 2022, No. 22-2263 (briefs filed May 22, 2023). The debtor included a non-standard provision in a form plan, changing vesting at confirmation rather than at plan completion. The bankruptcy court sustained the trustee's objection to the non-standard provision because the order of confirmation set forth the date of vesting as allowed by § 1327(b). The court explained that the order and plan delaying vesting until plan completion serves to "protect the debtor" since the automatic stay would no longer protect property from collection if the debtor missed a post-petition payment.

III. Benefit and *Bartenwerfer v. Buckley*

See attached article.

IV. Curing Nonmonetary Defaults

See attached opinion, ***In re Lazaro***, 650 B.R. 651 (Bankr. E.D. Pa. 2023).

Benefit and *Bartenwerfer v. Buckley*

by Angela Littwin

I. Introduction

In *Bartenwerfer v. Buckley*, the Supreme Court held that Mrs. Kate Bartenwerfer could be denied the discharge of a debt on the basis of fraud that her partner and husband, Mr. David Bartenwerfer, committed in selling a house that he remodeled and both spouses owned.[1] Partnership was key to decision; the Court embraced a precedent holding that the fraud of one partner prevented an innocent partner from discharging the debt.[2] And the concurrence explicitly stated that the decision is limited to partners, defined using principals of agency law.[3] Because the Bartenwerfers were both martial and business partners, a key question is which type of partnership is relevant. Fortunately for debtors with liabilities created by domestic violence, the Supreme Court characterized the Bartenwerfers as "business partners."[4] Unfortunately, the Court was unclear about how or why a business partnership existed in the case. To answer that question, one must look to the bankruptcy court's first opinion in the case.[5] In a footnote, the bankruptcy judge found an "agency relationship" between Mr. and Mrs. Bartenwerfer "based on their partnership with respect to the remodel project" because Mrs. Bartenwerfer, among other factors, stood to "financially benefit" from the remodel and sale of the house.[6] Thus, it would appear that a debtor who does not benefit from the fraud of her partner would be safe from a non-dischargeability action. The problem is that whether someone benefitted from a transaction is often unclear and complex in the context in which *Bartenwerfer* could have its most important impact: debt created by domestic violence.

Most of the commentary immediately following the Supreme Court's *Bartenwerfer* decision failed to notice its potential impact on coerced debt,[7] which is debt that batterers in abusive relationships incur in their partners' names using fraud or coercion.[8] For example, coerced debt occurs when a husband refinances the jointly-owned marital home fraudulently without telling his wife or a husband threatens physical harm to his wife and her pets if she does

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[1] *Bartenwerfer v. Buckley*, 143 S. Ct. 665 (2023) (interpreting 11 U.S.C. §523(a)(2)(A)).
[2] *Id.* at 675 ("The unmistakable implication is that Congress embraced Strang's holding—so we do too," referring to *Strang v. Bradner*, 114 U.S. 555, 5 S.Ct. 1038, 29 L.Ed. 248 (1885)).
[3] *Id.* at 676.
[4] *Id.* at 670.
[5] *In re Bartenwerfer*, 549 B.R. 222, Bankr.N.D.Cal., Apr. 01, 2016.
[6] *Id.* at 225, n. 3.
[7] *See, e.g.,* Lawrence J. Kotler & Drew S. McGehrin, *U.S. Supreme Court Clarifies Scope of Nondischargeable Debt in Favor of Victims of Fraud*, 2023 The Banking Law Journal § 2023-6.01 (June, 2023); David R. Kuney, *First Glance:, Feature, Supreme Court's Vicarious Liability Approach to Discharge Needs Congressional Reform*, 42-4 ABIJ 22 (April, 2023); Ronald Mann, Justices Narrow Bankruptcy Relief from Debts Incurred by Fraud, ScotusBlog (Feb. 23, 2023), available at https://www.scotusblog.com/2023/02/justices-narrow-bankruptcy-relief-from-debts-incurred-by-fraud/. The only exception I found is John Rao, *New Supreme Court Ruling: When Is a BankruptcyDebtor on the Hook for Partner's Fraud?*, National Consumer Law Center Digital Library, (March 2, 2023), available at https://library.nclc.org/article/new-supreme-court-ruling-when-bankruptcy-debtor-hook-partners-fraud#John+Rao.
[8] Angela Littwin, *Coerced Debt: The Role of Domestic Violence in Consumer Credit*, 100 CALIF. L. REV. 951-1026 (2012).

not allow him to charge ammunition and video games on her credit card.[9] My research partner and I have been studying coerced debt for more than a decade.[10] During that time, we have found that coerced debt appears to be pervasive; in one study, slightly more than half of callers to the National Domestic Violence Hotline who took our survey reported coerced debt.[11] Using a more restrictive conception of coerced debt, more than one-third of the callers reported it.[12] In that same study, we found that coerced debt was statistically significantly correlated with damage to callers' credit reports[13] and financial dependence on an abusive partner.[14]

We are currently analyzing the data for a National Science Foundation-funded study in which our research team interviewed 188 survivors of domestic violence about coerced debt.[15] Our data will provide detailed information about a wealth of topics related to coerced debt, but the finding most relevant to *Bartenwerfer* is the question of benefit. For each coerced debt a participant identified, we asked: "Did you benefit in any way from this debt? In other words, was it used to buy you something or pay for something you used?"[16] We are still analyzing these data – although I expect to report our benefit results during the October NCBJ Annual Conference – but already concerning patterns are emerging. In many cases, participants technically benefited from the debt, but did not really benefit in a fuller understanding of the word. For example, one participant was coerced into purchasing a vehicle for her then-husband that was significantly more expensive than what she wanted to buy. She ended up driving the purchased vehicle regularly, but only because her husband took her car, after someone told him that the vehicle he

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[9] These examples come from our current National Science Foundation-funded study of coerced debt. *See, infra* n. 15. Interviews with participants 10005004 and 20006005.

[10] Adrienne Adams, Angela Littwin & McKenzie Javorka, *The Frequency, Nature, and Effects of Coerced Debt Among a National Sample of Women Seeking Help for Intimate Partner Violence*, 26 Violence Against Women 1324 (2020); Angela Littwin, *Escaping Battered Credit: A Proposal for Repairing Credit Reports Damaged by Domestic Violence*, 161 Univ. of Penn. L. Rev. 363-429 (2013); Angela Littwin, *Coerced Debt: The Role of Domestic Violence in Consumer Credit*, 100 Calif. L. Rev. 951-1026 (2012); Adrienne E. Adams et al., Development of the Scale of Economic Abuse, 14 Violence Against Women 563, 563 (2008) (discussing various forms of economic abuse and recommending a scale for measuring such abuse); Adrienne E. Adams & Megan R. Greeson, Economic Abuse in the Lives of Women with Abusive Partners (2006) (unpublished report based on the same study published in Adams et al.) (on file with the author).

[11] Adams, Littwin & Javorka, supra n. 10 at 1331, Table 2 (showing that 52 percent of surveyed callers reported coerced debt).

[12] In an as-yet-unpublished analysis, we coded caller responses to our question of what threats callers feared if they did not incur the debt their partners wanted in order to determine the percentage that met the threshold for the "no reasonable alternative" prong of duress law. Threats that met this prong of duress law included physical abuse as well as threats like harm to pets to reporting the caller to the authorities. When we combined callers who reported fraudulent debt with those who reported debt via coercion under this more restrictive definition, 35 percent of the sample reported coerced debt.

[13] Adams, Littwin & Javorka, supra n. 10 at 1333, Table 5 (showing that callers who reported coerced debt were more than six times more likely than other callers to report credit damage).

[14] Adams, Littwin & Javorka, supra n. 10 at 1334, Table 6 (showing that callers who reported coerced debt were two-and-a-half times more likely than other callers to report financial dependence).

[15] Adrienne Adams, Angela Littwin & Angie Kennedy, *Debt as a Control Tactic in Marriage*, grant award available at https://www.nsf.gov/awardsearch/showAward?AWD_ID=1920557&HistoricalAwards=false.

[16] Reading through the interview transcripts, it became clear that interviewers often tailored the way they asked this question to reflect the circumstances of the debt. For example, for a student loan, an interviewer might ask whether at least some of the debt was used to pay her tuition. See, e.g., interview with participant 71009001.

had coerced her into buying looked like a "mommy" car.[17] Another participant lived in the home that she and her then-fiancé purchased and hence benefitted from the mortgage, but at the time of the loan, she had broken off the engagement and was looking for apartments on her own. She only acquiesced to the home purchase when he threatened to hurt himself if she did not join him in buying the house he had picked out.[18]

There are few legal remedies that address coerced debt directly and none of them are broadly effective.[19] That leaves victims of coerced debt seeking relief dependent on generally-applicable debtor-creditor laws, such as bankruptcy. *Bartenwerfer* leaves bankruptcy relief in doubt. The Court's emphasis on Congress' use of passive voice in 11 U.S.C. §523(a)(2)(A) is particularly concerning because non-dischargeability for fraud now "turns on how the money was obtained, not who committed fraud to obtain it,"[20] which fails to exclude someone who is also a victim of the fraud. For example, if an abuser fraudulently uses the credit card of his spouse,[21] both the credit card issuer and the spouse are fraud victims. I was an amicus curiae on a brief that made this argument,[22] and the *Bartenwerfer* Court's response was that victims of fraud will likely have other remedies, but the examples the Court gave do not apply to coerced debt.[23]

The most important limit in *Bartenwerfer* is that underlying law, not §523(a)(2)(A), determines the degree to which one partner is liable for another's fraud.[24] But whether the would-be partner benefitted from the fraud is an important consideration in underlying law. For example, to avoid liability for a fraudulent credit card transaction because it was an unauthorized use under the Truth in Lending Act, a consumer must not have benefited from the debt.[25] Courts have also considered whether an innocent partner of the fraudster benefitted from the fraud in determining dischargability under §523(a)(2)(A) and its predecessor provisions. *Strang v. Bradner*,[26] the Nineteenth Century precedent that the *Bartenwarfer* Court "embraced,"[27] stated in dicta that the innocent business partners could not discharge liability for the fraudulent debt "especially" because they "received and appropriated the fruits of the fraudulent conduct of their associate in business."[28] Courts applying *Strang* pre-*Bartenwerfer* have a mixed track record of

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[17] Interview with participant 94008002.
[18] Interview with participant 92011003.
[19] See Section II, infra.
[20] *Bartenwerfer*, 143 S. Ct. at 670.
[21] This is the most common type of fraudulent debt that we are seeing in the current study.
[22] Brief for the National Consumer Bankruptcy Rights Center and Professor Angela K. Littwin as Amici Curiae in Support of Petitioner, Kate Marie Bartenwerfer, Petitioner, v. Kieran Buckley, Respondent.
2022 WL 3006308, *1+, U.S. (Appellate Brief).
[23] *Bartenwerfer*, 143 S. Ct. at 676 ("Ordinarily, a faultless individual is responsible for another's debt only when the two have a special relationship, and even then, defenses to liability are available," referencing the principal that partners are not liable for the actions other partners take without authority).
[24] *Bartenwerfer*, 143 S. Ct. at 675. (Section "523(a)(2)(A) does not define the scope of one person's liability for another's fraud. That is the function of the underlying law—here, the law of California.")
[25] 12 C.F.R. § 226.12(b)(1)(i) "(For purposes of this section, the term "unauthorized use" means the use of a credit card by a person, other than the cardholder, who does not have actual, implied, or apparent authority for such use, and from which the cardholder receives no benefit.").
[26] *Strang v. Bradner*, 114 U.S. 555, 5 S.Ct. 1038, 29 L.Ed. 248 (1885)).
[27] *Bartenwerfer*, 143 S. Ct. at 675.
[28] *Strang*, 114 U.S. at 561.

including benefit from the fraud in the factors used to determine whether an innocent party may discharge a fraudulent debt.[29] That may be why the bankruptcy court in *Bartenwerfer* made it one of three reasons it found an agency relationship between the Bartenwerfers.[30]

This manuscript will proceed in three parts. Part II provides the context necessary to understand coerced debt and demonstrates the lack of direct legal remedies for it. Part III will argue that whether someone benefited from the fraud is an important element in determining whether she will be liable for it. Part IV will use data from our NSF study to argue that the benefit question is difficult to apply to real-world facts and will often lead to bizarre results.

II. Coerced Debt & Its Lack of Legal Remedies

A. How Does Coerced Debt Happen?

To understand coerced debt, one must know a little about domestic violence (DV). Recent research suggests that there are two main types: (1) situational violence, in which both partners in the relationship use relatively minor violence against each other, and (2) coercive control, in which one partner in the relationship uses severe violence to control the other.[31] In coercive control, the abusive partner's goal is to undermine the victim's agency to the point of eliminating her free will.[32] The abuser accomplishes this through behaviors such as monitoring the victim's time, isolating her from friends and family, preventing her from working, barring access to medical care, and in extreme cases, trapping her in the family home.[33] In heterosexual relationships, coercive control tends to be gendered – perpetrated by men against women[34] – which is why I use male pronouns to describe abusive partners and female pronouns to describe victims when unavoidable.

Coerced debt derives from coercive control.[35] An abuser who has control over other aspects of his partner's life can incur coerced debt in her name relatively easily. For example, if the abusive partner is controlling access to the family's mail,[36] that prevents his partner from

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[29] See, e.g., *BancBoston Mort. Corp. v. Ledford (In re Ledford)*, 970 F.2d 1556, 1561 (6th Cir. 1992) (holding that an innocent business partner could not discharge a fraudulent debt because, *inter alia*, he "shared in the monetary benefits of the fraud"). *Shelton v. Wells (In re Shelton)*, 28 B.R. 218, 222 (Bankr.E.D.Mo.1983) (holding a wife was bound by the fraudulent representations of her husband, because *inter alia*, she benefitted from them). *But see In re Bursh*, 14 B.R. 702, 706 (Bankr. D. Ariz. 1981) ("Plaintiff's assertion that the marital community benefited from defendant's husband's acts and therefore that the defendant should be barred from discharging the resulting debt amounts to fraud implied by law and it is the opinion of the court that such a result is not within the purview or contemplation of section 523(a).")

[30] *In re Bartenwerfer*, 549 B.R. at 225, n. 3 (finding an agency relationship between the Bartenwerfers because Mrs. Kate Bartenwerfer "was on title to the Property, signed the disclosure statements relating to the Property, and would financially benefit from the successful completion of the project and sale of the Property.")

[31] Evan Stark, Coercive Control: The Entrapment of Women in Personal Life 198-203 (2007); Michael P. Johnson, Conflict and Control: Gender Symmetry and Asymmetry in Domestic Violence, 12 Violence Against Women 1003, 1003, 1006 (2006).

[32] See Johnson, Gender Symmetry, supra note 31, at 1010.

[33] See Stark, supra note 31, at 11, 13 & 274-75.

[34] Littwin, *Coerced Debt*, supra note 8, at 978-81.

[35] This is why I named the phenomenon "coerced debt." Littwin, *Coerced Debt*, supra note 8, at 977-78.

[36] In our study with the National Domestic Violence Hotline, 71 percent of callers reported that an intimate partner had hidden financial information from them. Adams, Littwin & Javorka, supra n. 10, at 1331.

learning of credit cards opened in her name.[37] Or if a victim is afraid of the abuser, she is likely to sign a document he tells her to sign without questioning it.[38] This is also why we include debt incurred via fraud under the umbrella of coerced debt. Coercive control and fraud can reinforce each other. For example, if a victim discovers fraudulent debt in her name, she may feel unsafe addressing it with the abusive partner.[39] The intimate relationship itself also makes fraud easier. Intimate partners have each other's personal information, which is what creditors require to verify the identity of someone incurring a loan.[40]

Coerced debt, in turn, can become an element of coercive control, making it more difficult for a victim to leave an abusive relationship. In our study with the National Domestic Violence Hotline, we found that callers who reported coerced debt were 2.5 times more likely than other callers who took our survey to report staying longer than they wanted in an abusive relationship due to financial concerns.[41] One mechanism of this financial dependence may be credit reporting. Coerced debt is associated with damage to credit scores,[42] and low credit scores can prevent access to employment, housing, and basic utility service, the very items someone needs to leave an abusive relationship and start an independent household.[43]

B. Lack of Direct Legal Remedies

There are few legal remedies that relieve a consumer of debt because it is coerced, and those that exist have limited application and effectiveness. The type of coerced debt with the most legal protections is debt incurred via fraud. Fraudulent coerced debt is a form of identity theft,[44] and fraudulent credit card debt has particularly strong protection under the unauthorized use provision of the Truth in Lending Act (TILA).[45] But there are three major problems. First, victims of fraudulent coerced debt report difficulties obtaining police reports due to the intimate nature of their relationship with the abusive partner.[46] Creditors and credit reporting agencies may require police to substantiate identity theft under the law,[47] and anecdotal evidence suggests

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[37] In our Hotline study, callers who reported hidden financial information were more than 3.5 times more likely to report coerced debt than other callers. Adams, Littwin & Javorka, supra n. 10, at 1332, Table 4.
[38] Littwin, *Coerced Debt*, supra note 8, at 989-90.
[39] Littwin, *Escaping Battered Credit*, supra n. 10, at 375.
[40] Littwin, *Coerced Debt*, supra note 8, at 986-87.
[41] Adams, Littwin & Javorka, supra n. 10, at 1334, Table 6.
[42] Adams, Littwin & Javorka, supra n. 10, at 1333, Table 5 (showing that callers who reported coerced debt were more than six times as likely to report damaged credit as other callers who took our survey).
[43] See generally Littwin, *Escaping Battered Credit*, supra n. 10.
[44] A few states have recently passed laws making debt via coercion a form of identity theft. *See, e.g.,* Texas Penal Code § 32.51; Texas Business & Commerce Code § 521.051. But federal identity-theft law still covers only debt created via fraud. For example, to remove a debt created by identity theft from one's credit report under the Fair Credit Reporting Act, a consumer must provide "a statement by the consumer that the information is not information relating to any transaction by the consumer." 15 U.S.C. §1681c-2(a)(4). A consumer who incurred debt via coercion was involved in the debt's creation and thus would not be able to make such a certification.
[45] See Truth in Lending Act, 15 U.S.C. §1643(a) (limiting consumer liability for unauthorized credit card charges to fifty dollars).
[46] In my work with attorneys and advocates who serve victims of coerced debt, difficulty obtaining police reports is a constant refrain.
[47] 16 C.F.R. §603.3(a)(3).

that they do.[48] Second, much debt that victims consider fraudulent may not be legally fraudulent. For example, a victim who allows an abusive partner to be an authorized user on a credit card because she wants him to be able to make purchases for the family would not have a fraud claim for purchases he made outside that scope,[49] even purchases that the victim clearly would not want, such as gambling debts or expenses for strip club.[50] Third coerced debt via coercion appears to be much more common than that incurred by fraud. For example, in our Hotline study, 43 percent of callers reported debt via coercion, whereas only 22 percent reported debt via fraud.[51]

Duress is the doctrine that protects people from coerced contracts, but it usually does not apply to coerced debt because the creditor is an innocent third party (no knowledge of the coercion) who gave value, albeit value that was appropriated by the wrong partner in an abusive relationship.[52] Duress law covers the scenario in which one party coerces a second party into a contract that creates a debt to the first party, because duress law originated long before the development of the mass consumer-lending market.[53] With the advent of widely-available consumer credit, creating debt via a third-party creditor is a more lucrative way to obtain funds.[54]

Even if the abuser and victim are married and divorce, family law is not helpful. Family courts do not have jurisdiction over creditors and thus cannot alter victims' creditor contracts.[55] In the current study, we saw a frequent work-around for secured debts. Divorce decrees frequently required the spouse receiving encumbered property to refinance it in order to remove the other spouse's name from the debt.[56] For unsecured debts, the easier option is to order the spouse who created the debt to pay the victim. In the current study, of the 127 women with

[48] See, e.g., Schatten v. Sallie Mae, Inc., No. 08-0322, 2009 U.S. Dist. LEXIS 42801, at *6 (N.D. Ga. Mar. 4, 2009) (noting that Sallie Mae's ID Theft Affidavit requires the consumer to submit a police report).

[49] 12 C.F.R. § 226.12(b)(1)(i) "(For purposes of this section, the term "unauthorized use" means the use of a credit card by a person, other than the cardholder, who does not have actual, implied, or apparent authority for such use….").

[50] See, e.g., interview with participant 94008002 (describing her ex-husband's fraudulent use of her credit card for gambling and strip clubs).

[51] Adams, Littwin & Javorka, supra n. 10 at 1331, Table 2. Preliminary data from our current study suggest that debt via coercion is much more common than debt via fraud, although we have not yet completed data analysis.

[52] Restat. 2d of Contracts § 175 (1981) ("If a party's manifestation of assent is induced by one who is not a party to the transaction, the contract is voidable by the victim unless the other party to the transaction in good faith and without reason to know of the duress either gives value or relies materially on the transaction.")

[53] See, e.g., *Hackley v. Headley*, 45 Mich. 569, 574, 8 N.W. 511, 512-13 (1881) (finding no duress where the defendant paid the plaintiff less than the plaintiff was owed and issued a receipt saying the debt was paid in full; plaintiff felt obliged to accept because he was in dire financial straits although not ones caused by the defendant).

[54] Identity theft is a multi-billion dollar business. See, e.g., Megan Leonhardt, *Consumers Lost $56 Billion to Identity Fraud Last Year*, CNBC (Mar. 23, 2021 12:56 PM), https://www.cnbc.com/2021/03/23/consumers-lost-56-billion-dollars-to-identity-fraud-last-year.html..

[55] Littwin, *Escaping Battered Credit*, supra n. 10 at 368.

[56] This is my impression from working with dozens of participant divorce decrees during the current study. We have not yet systematically analyzed this facet of divorce decrees. Adrienne Adams, Angela Littwin & Angie Kennedy, *Debt as a Control Tactic in Marriage*, grant award available at https://www.nsf.gov/awardsearch/showAward?AWD_ID=1920557&HistoricalAwards=false.

coerced debt, we found one instance of a divorce decree ordering her ex-husband to pay it.[57] Moreover, even when remedies are available in theory, they are not necessarily available in practice. Represented participants frequently told us that their lawyers advised them that there was no point in attempting to make their spouse responsible for debt in the participant's name.[58] Indeed, participant divorce decrees regularly provided that each spouse was to pay the debt in his or her name.[59]

That leaves victims of coerced debt seeking relief dependent on generally-applicable debtor-creditor law, such as statutes of limitations,[60] the Fair Debt Collections Practices Act,[61] state-law versions of FDCPA,[62] the Fair Credit Reporting Act,[63] and of course, bankruptcy. Of these bodies of law, bankruptcy is the only one that does not require a debt to meet certain criteria – i.e., that the statute of limitations has run or the debt collector violated FDCPA – at least with respect to general unsecured debt.

[NOTE to attendees of the National Conference of Bankruptcy Judges 2023 Annual Conference – I was unable to draft Parts III and IV by the time of the materials deadline for this conference. Part IV requires a detailed data analysis that is currently underway. I expect to be able to discuss both sections by the time of my presentation at the in October 2023.]

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[57] This result is from data analysis that we have yet to publish. Adrienne Adams, Angela Littwin & Angie Kennedy, *Debt as a Control Tactic in Marriage*, grant award available at https://www.nsf.gov/awardsearch/showAward?AWD_ID=1920557&HistoricalAwards=false.
[58] See generally Adrienne Adams, Angela Littwin & Angie Kennedy, *Debt as a Control Tactic in Marriage*, grant award available at https://www.nsf.gov/awardsearch/showAward?AWD_ID=1920557&HistoricalAwards=false..
[59] See generally Adrienne Adams, Angela Littwin & Angie Kennedy, *Debt as a Control Tactic in Marriage*, grant award available at https://www.nsf.gov/awardsearch/showAward?AWD_ID=1920557&HistoricalAwards=false.
[60] E.g., Tex. Civ. Prac. & Rem. Code Ann. § 16.004(a)(4).
[61] 15 U.S.C. § 1692 et seq.
[62] E.g., Texas Fair Debt Collection Practices Act § 392.001.
[63] 15 U.S.C. § 1681 et seq.

650 B.R. 651
United States Bankruptcy Court, E.D. Pennsylvania.

IN RE: Jorge Geraldo LAZARO, Debtor.

Case No. 22-11871 (PMM)
|
Signed May 12, 2023

Synopsis
Background: Mortgagee objected to confirmation of debtor's Chapter 13 plan, asserting that debtor could not cure monetary default without first curing nonmonetary default, namely, breach of "due-on-sale" clause in that prohibited transfer of real property from debtor's father, jointly to himself and to debtor, without lender's prior authorization.

[Holding:] The Bankruptcy Court, Patricia M. Mayer, J., held that as matter of first impression, Bankruptcy Code's antimodification provision did not prohibit proposed Chapter 13 plan from curing monetary default on mortgage in which there was a non-monetary default.

Objection overruled.

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

West Headnotes (6)

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

Bankruptcy Home mortgages or similar obligations

Bankruptcy Code's antimodification provision did not prohibit confirmation of debtor's proposed Chapter 13 plan that called for curing monetary default on mortgage that remained exclusively in the name of debtor's father, after father had transferred the property jointly to himself and to debtor, without first curing nonmonetary default, namely, breach of "due-on-sale" clause that prohibited transfer of property without lender's prior authorization; cure of the monetary default was distinguishable from modification of mortgage, with "cure" taking care of something that had already happened whereas "modification" amounted to a change of terms going forward, and curing monetary default did not alter terms of mortgage, as mortgagee would receive the benefits of its bargain, including payment of principle at the agreed rate of interest, as well as the right to accelerate the mortgage contract. 11 U.S.C.A. § 1322(b)(2).

[2] **Bankruptcy** Curing Defaults

Bankruptcy Code allows any default to be cured by Chapter 13 plan. 11 U.S.C.A. § 1322(b)(3, 5).

[3] **Bankruptcy** Mortgages in general

Chapter 13 debtor not in privity with mortgagee may cure monetary default. 11 U.S.C.A. § 1322.

[4] **Bankruptcy** Curing Defaults

Meaning of "cure" by Chapter 13 plan is to remedy or rectify default and restore matters to status quo ante. 11 U.S.C.A. § 1322.

[5] **Bankruptcy** Curing Defaults

Cure of a default by Chapter 13 plan should return circumstances to where they were prior to the default; this provides a remedy for the breach. 11 U.S.C.A. § 1322.

[6] **Bankruptcy** Proceedings, Acts, or Persons Affected

Bankruptcy Modification of claim, right, or debt in general

Bankruptcy Curing Defaults

Both the automatic stay and cure deal with past defaults, whereas the modifications permitted, or prohibited, by Bankruptcy Code concern future obligations. 11 U.S.C.A. §§ 362, 1322(b)(2).

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Attorneys and Law Firms

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Scott F. Waterman [Chapter 13], Chapter 13 Trustee, Reading, PA, Trustee, Pro Se.

OPINION

PATRICIA M. MAYER, UNITED STATES BANKRUPTCY JUDGE

I. INTRODUCTION

Jorge Geraldo Lazaro (the "Debtor"), like most in chapter 13 bankruptcy, seeks to confirm a plan that would cure the mortgage arrears and allow him to stay in his home located at 1932 W. Allen Street in Allentown, PA (the "Property"), where he has lived for over a decade. [1]

The Debtor did not buy his home. Rather, the debtor's father, Jorge J. Lazaro (the "Debtor's Father"), the original owner, transferred the Property jointly to himself and the Debtor in 2012 for $1.00. The mortgage on the Property, however, remains exclusively in the name of the Debtor's Father. These facts mean that the transfer violated a "due- on sale" clause in the Debtor's Father's mortgage, a provision which prohibits transfer of the Property without the lender's prior authorization.

Towd Point Mortgage Trust ("Towd"), the current owner of the mortgage, objects to confirmation of the Debtor's chapter 13 plan (the "Plan"), asserting that the Debtor cannot cure the mortgage arrears – the monetary default – without first curing the non-monetary default (the breach of the due-on-sale clause). Towd also argues that confirmation of the Plan would amount to an impermissible modification of the mortgage.

The Debtor maintains that he seeks only to cure the arrears rather than to modify his father's mortgage and that the relief proposed by the Plan is specifically allowed by the Bankruptcy Code.

There are compelling arguments on both sides of this debate. After consideration, and for the reasons discussed below, I hold that the Debtor may cure the monetary default by way of his chapter 13 Plan and that such a cure is distinguishable from a modification of the mortgage.

*653 II. PROCEDURAL AND FACTUAL BACKGROUND

History of the Property and Mortgage

In 2006, the Debtor's Father executed a note and mortgage (the "Mortgage") in favor of Countrywide Home Loans, Inc. in the amount of $131,880.00. The Mortgage was secured by the Property then owned exclusively by the Debtor's Father.

The Mortgage was transferred to BAC Home Loans Servicing, LP in 2011, to Nationstar Mortgage LLC ("Nationstar") in 2013, and to Towd in 2018.

On July 14, 2012, the Debtor's Father transferred for $1.00 the Property to himself and the Debtor. The Mortgage, however, was not transferred and the mortgagee was not notified of the transaction.

The Mortgage and Modification

Section 18 of the Mortgage states, in relevant part:

> If all or any part of the Property or any Interest in the Property is **sold or transferred ... without Lender's prior written consent, Lender may require immediate payment in full** of all sums secured by this Security Instrument. However, this option shall not be exercised by Lender if such exercise is prohibited by Applicable Law. If Lender exercises this option, Lender shall give Borrower notice of acceleration. The notice shall provide a period of not less than 30 days from the date the notice is given in accordance with Section 15 within which Borrower must pay all sums secured by this Security Instrument.

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Ex. B to First Motion for Relief (the "Due-on-Sale Clause") (emphasis added).

The Debtor's Father and Nationstar executed a modification of the Mortgage on October 1, 2015. [2]

The Debtor's Previous Bankruptcy Filings

The Debtor filed three (3) previous chapter 13 petitions in this court:

- Case no. 12-17057 (the "First Case"): filed on July 26, 2012 and dismissed on January 13, 2013. The Debtor listed the Property on schedule A as being jointly owned with his father. No plan was confirmed.
- Case no. 13-17322 (the "Second Case"): filed on August 22, 2013 and dismissed on November 6, 2014. The Debtor listed the Property on schedule A as being jointly owned with his father. A Plan was confirmed on April 24, 2014, but the case was dismissed for failure to make plan payments.
- Case no. 15-13575 (the "Third Case"): filed on May 20, 2015 and was discharged on November 13, 2017. The Debtor listed the Property on schedule A as being jointly owned with his father. A Plan was confirmed on February 11, 2016. Following a Notice of Final Cure of mortgage arrears filed by the chapter 13 Trustee, the Debtor received a discharge.

In the Second Case, Nationstar, who at that time held the Mortgage, filed both an objection to confirmation and a motion for relief from the automatic stay. Both pleadings acknowledge that the Property is owned jointly by the Debtor and his father and make no mention or argument regarding a non-monetary default of the Mortgage.

***654** In the Third Case, a Motion to Approve a Loan Modification filed by Nationstar was approved by the Court on November 10, 2016. Doc. #33 (the "Motion to Approve"). The Motion states that Debtor applied for and was approved for a modification; however, the attached modification agreement includes only the name of the Debtor's Father. The Motion to Approve neither mentions nor contemplates a violation of the Due-on-Sale Clause.

The current bankruptcy filing

The Debtor filed this chapter 13 case on July 18, 2022. The Property appears on the Debtor's schedules as being "jointly owned with Debtor's father" as a tenancy in common. See Schedules A/B and H. Towd's secured Proof of Claim, filed on September 16, 2022 in the amount of $245,987.95, states the arrears on the mortgage in the amount of $46,643.73.

Prior to the current bankruptcy filing, a foreclosure action was commenced by Towd in the Court of Common Pleas. [3] In September 2022, Towd filed a Motion for Relief from the Stay. Doc. #13, amended at doc. #19 (the "First Motion for Relief"). The First Motion for Relief alleged that *in rem* relief was warranted because the Property was fraudulently transferred (from Debtor's Father to Debtor and his father jointly). The Motion stated an alternative ground for relief, alleging that the Debtor's bad faith is demonstrated by the fact that the Debtor "is incapable of curing the mortgage default[ ] while retaining the Property." Motion at ¶17. Following a hearing on the merits, the First Motion for Relief was denied.

On April 11, 2023, Towd filed another motion for relief (doc. #50, the "Second Motion for Relief"), alleging that the Debtor was $2,607.66 in arrears post-petition. The Debtor did not oppose this Motion and an Order was entered on May 2, 2023 granting the relief.

The Debtor's proposed Plan seeks, *inter alia*, to cure a monetary default on the Mortgage in the amount of $46,643.73.

Towd objects to confirmation because it contends that the Plan is "infeasible as Debtor is incapable of curing all existing defaults under the terms of the mortgage." Objection at 1. The only way to cure the default would be to transfer the Property back to the Debtor's Father.

Following a contested and continued confirmation hearing, the parties submitted briefs regarding the question of whether the Debtor can cure the mortgage default in chapter 13 or whether such a plan is futile.

III. THE PARTIES' ARGUMENTS

The Debtor argues that the purpose of the Plan is to cure only the monetary mortgage default. The Debtor's Brief suggests, without benefit of citation to law, that the non-monetary default may be enforced outside of the bankruptcy process and that such protection is adequate.

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Towd makes several points in response:

- The Code requires a plan to cure all defaults by taking care of the "triggering" event;
- If the Debtor were to cure the non-monetary default by removing himself from the title to the Property, then he would be unable to cure the monetary default; and
- Confirmation of the Plan would compel the creditor impermissibly to modify the mortgage to accept payments ***655** from the Debtor, with whom Towd is not in privity.

IV. RELEVANT BACKGROUND LAW

A. Due-on-Sale Provisions

This dispute concerns the relevance in bankruptcy of the boilerplate mortgage language which prohibits the unauthorized transfer of secured property to a third party. A "due-on-sale clause" is a contract provision which allows a lender, at its option, "to declare due and payable sums secured by the lender's security instrument if all or any part of the property, or an interest therein, securing the real property loan is sold or transferred without the lender's prior written consent." 12 U.S.C. § 1701j–3(a)(1) (St. Germain Depository Institutions Act).

Due-on-sale clauses, which are standard in most mortgage agreements, serve two (2) purposes. First, such a provision ensures that a lender will only contract with individuals whom they assess to be a good credit risk. In re Mullin, 433 B.R. 1, 3 (Bankr. S.D. Tex. 2010). Second, due-on-sale clauses allow a lender to recall below market interest loans and to maintain a portfolio that reflects market rates. Arthur J. Margulies, The Cure and Reinstatement of Mortgages by Third Party Assignees, 24 Cardozo L. Rev. 449, 454–55 (2002).

B. The St. Germain Act

The policy of protecting lenders from an unfavorable transfer of a mortgage was codified by Congress in 1982 with the passage of the Garn-St Germain Depository Institutions Act (the "St. Germain Act"). The St. Germain Act protects the validity of due-on-sale provisions, [4] regardless of state law to the contrary and provides, in relevant part:

> Notwithstanding any provision of the constitution or laws (including the judicial decisions) of any State to the contrary, a lender may ... enter into or enforce a contract containing a due-on-sale clause with respect to a real property loan.

12 U.S.C.A. § 1701j-3(1) (West).

Pennsylvania law conforms to this standard, allowing the inclusion of due-on-sale clauses in mortgages. See generally 15 West's Pa. Prac. Mortgages § 8.5 (3d ed.) (citing cases in fn.3); Marra v. Stocker, 532 Pa. 187, 615 A.2d 326 (1992); New Home Federal Sav. And Loan Ass'n v. Trunk, 22 Pa. D &C 3d 399, 420 (1982).

Split in Authority Regarding the Issue Presented

The question presented - whether a debtor who is not in privity with the mortgagee may cure default in a chapter 13 plan - has divided courts. See generally In re Mullin, 433 B.R. 1, 12 (Bankr. S.D. Tex. 2010); In re Tewell, 355 B.R. 674, 680 (Bankr. N.D. Ill. 2006) (describing the split).

In broad terms, the division breaks down as follows: some courts determine that allowing a debtor to cure a default on a mortgage where there has been a violation of the due-on-sale clause would amount to an impermissible modification in ***656** violation of 11 U.S.C. § 1322(b)(2) (the "First Line of Cases"). [5] The competing authority (the "Second Line of Cases") holds that because the mortgage is a claim on the debtor's property, the default on the lien may be cured, regardless of whether the debtor is in privity with the mortgagee. [6]

There is no binding authority on this Court. [7]

V. ANALYSIS

[1] I agree with the Second Line of Cases and, therefore hold that the Debtor's proposed Plan may be confirmed and the monetary default cured despite the fact that the Mortgage is only in the name of the Debtor's Father.

Cure of the Monetary Default is Distinguishable from a Modification of the Mortgage

The division between the First and Second Line of Cases results, in large part, from a disagreement about whether curing a monetary default in a mortgage pursuant to which there is a non-monetary default results in an impermissible modification of the lending agreement.

I hold that such a cure of the monetary default is possible and does not violate 11 U.S.C. § 1322 (b)(2).

[2] **[3]** I start with the understanding that the Code allows "*any*" default to be cured. 11 U.S.C. § 1322(b)(3) (emphasis added); see also § 1322(b)(5); In re Garcia, 276 B.R. 627, 637 (Bankr. D. Ariz. 2002) ("the drafters did not intend to exclude any particular kinds of defaults from the right to cure"). [8]

[4] **[5]** The meaning of cure, in turn, is to "remedy or rectify the default and restore matters to the *status quo ante*." Sapos v. Provident Inst. of Sav. in Town of Boston, 967 F.2d 918, 926 (3d Cir.1992) (citation omitted). A cure of a default should return circumstances to where they were prior to the default. This provides a remedy for the breach.

Towd insists, however, that curing a default necessitates "taking care of the triggering event ...." and thus concludes that in order to effect a "cure" of the Due-on-Sale Clause, the Property would first need to be transferred back to the Debtor's Father. In re Taddeo, 685 F.2d 24, 26 (2d Cir. 1982).

But a look at the complete passage from Taddeo points in a different direction. The Second Circuit there stated:

> When Congress empowered Chapter 13 debtors to 'cure defaults,' we think Congress intended to allow mortgagors to ***657 'de-accelerate' their mortgage and reinstate its original payment schedule**. We so hold for two reasons. First, we think that the power to cure must comprehend the power to 'de-accelerate.' This follows from the concept of 'curing a default.' A default is an event in the debtor-creditor relationship which **triggers certain consequences**-here, acceleration. Curing a default commonly means taking care of the triggering event and **returning to pre-default conditions. The consequences are thus nullified**... This history and the policy discussed above compel the conclusion that § 1322(b)(5) was intended to permit the cure and de-acceleration of secured long-term residential debt accelerated prior to the filing of a Chapter 13 petition.

In re Taddeo, 685 F.2d 24, 26–27 (2d Cir. 1982) (emphasis added) (further holding that the ability to cure under § 1322(b)(3) and (b)(5) is not limited by the anti-modification provision of § 1322(b)(2)). Taddeo stands not for the proposition that a cure necessarily involves reversing the *cause* of a default, but rather that rectifying a default entails taking care of the monetary *consequences* of a default.

As explored in In re Garcia, 276 B.R. 627, 634 (Bankr. D. Ariz. 2002), and discussed below, the rights of a lender complaining of the violation of a due-on-sale clause will likely be adequately protected by the payment of the mortgage balance; money is what is at stake. A mortgagee who can demonstrate that monetary relief is for some reason inadequate may receive relief from the stay in order to pursue additional remedies in state court. But it is unlikely that the non-monetary default itself will be cured during the chapter

13. See *Lundin*, Chapter 13 *Bankruptcy* § 82.3 (4 th Ed. 2023) (noting that it is "conceptually difficult" to see how a debtor cures a non-monetary default and expressing doubt about the feasibility of curing a pre-petition due-on-sale clause through a chapter 13 plan). I agree with Towd that a cure of the *nonmonetary* default of the Due-on-Sale Clause would involve a re-transfer of the Property. However, Towd fails to show any prejudice to it resulting from the mere fact that the Property was transferred. At the March 23, 2023 hearing, Towd acknowledged that any purchaser takes the Property subject to the existing liens. Towd remains protected.

Critically, curing the monetary default is all that the Debtor seeks to do by way of his Plan; he does not purport to cure the non-monetary default of the Due-on-Sale Clause. Confirmation of the Debtor's Plan would effect relief specifically allowed by the Code. Matter of Birckelbaw, 33 B.R. 720, 722 (Bankr. E.D. Mich. 1983). Further, Towd's rights to enforce the Due-on-Sale Clause will ride through the bankruptcy, ready to enforce if and when Towd chooses.

Allowing the Cure of the Non-Monetary Default does not Amount to a Modification

But does not treating – or, more bluntly, ignoring – a violation of a due-on-sale clause during the pendency of a bankruptcy effectively, and impermissibly, modify the mortgage contract? I find that such treatment of a non-monetary default pursuant to § 1322(b)(5) does not violate the anti-modification provision of § 1322(b)(2).

"Cure" and "modification" are distinct concepts. As discussed, the scope of the debtor's ability to cure is broad; however, the scope of the antimodification clause is "narrow." In re Klein, 106 B.R. 396, 401 (Bankr. E.D. Pa. 1989); In re Garcia, 276 B.R. 627, 634 (Bankr. D. Ariz. 2002).

A plan may cure a monetary default without altering the terms of the mortgage. Towd will receive the benefits of its ***658** bargain, including payment of principle at the agreed rate of interest, as well as the right to accelerate the mortgage contract.

Towd responds that the unauthorized transfer of the Property to the Debtor succeeds in changing the agreed terms of the contract because the mortgagee has effectively lost the ability to vet its borrower. Towd did not agree to do business with the Debtor, who may be a greater credit risk than the Debtor's Father. This fact, however, does not *modify* the terms of the mortgage. It means, rather, that the Debtor's Father may have breached the mortgage contract (whose terms remain consistent). Such breach is, in fact, contemplated by the language of the Mortgage, which allows Towd to accelerate payments under these circumstances. Thus far, Towd has chosen not to exercise this right, despite the fact that it had, at minimum, constructive knowledge of the transfer for more than ten (10) years prior to the current bankruptcy. [9]

Further distinguishing a cure of a mortgage default from a modification is the fact that a cure takes care of something that has already happened, whereas a modification amounts to a change of terms going forward:

> **[6]** Both the automatic stay and cure deal with past defaults, whereas the modifications permitted (or prohibited) by § 1322(b)(2) concern future obligations. Thus the antimodification provision says nothing about what can or must be done about past defaults, but merely provides that the debtor's future obligations to a lender cannot be modified from what is provided in the loan documents.

In re Garcia, 276 B.R. 627, 635 (Bankr. D. Ariz. 2002) (noting the effect of the language of "rights" included in the two provisions). [10]

The Default may be Remedied by Payment

The upshot of Towd's complaint is that the default of the Due-on-Sale Clause must be reversed, and that confirmation of the Debtor's Plan would prevent, or at a minimum not satisfy, this requirement. Towd's argument has an initial appeal; the Debtor does not deny that the Mortgage has been breached. Further, the inclusion of Due-on-Sale Clause was a contractual provision which, at least in theory, was agreed on as part of the mortgage terms.

But we must look at how, if at all, Towd has been harmed by the transfer. The question of Towd's damages is both

theoretical – is relief warranted where a breach does not amount to a loss – and practical: can Towd be made whole without reversal of the transfer?

Neither its predecessors nor Towd sought acceleration of the loan, in spite of the fact that the mortgagee knew of the nonmonetary default years prior to the Debtor's current bankruptcy filing. [11] And ***659** if the Mortgage debt had been accelerated, the Debtor would have the ability to cure the default in his bankruptcy. In re Thomas, 626 B.R. 793, 801 (Bankr. E.D. Pa. 2021). The specified remedy for breach of the Due-on-Sale Clause is for the mortgagee to move for quicker payments; the document does not provide for the lender to receive damages simply because the Property was transferred. Further, if Towd found the Debtor's Father's conduct so egregious, see First Motion for Relief, we have to wonder why Towd failed to seek redress for the non-monetary default prior to the Debtor's bankruptcy.

Garcia, which denied stay relief to the lender and held that the debtors could cure a nonmonetary default of a mortgage transferred in violation of a due on sales clause, is instructive here:

> [T]he Bank never complained about a violation of its due on sale clause until after the monetary default and, indeed, until after the bankruptcy was filed. The Bank's conduct, therefore, suggests that **all it was really concerned about was the money**—there was no complaint so long as payments were regularly made.

In re Garcia, 276 B.R. 627, 641 (Bankr. D. Ariz. 2002) (emphasis added). We can hardly be shocked that a mortgage company is motivated by profit. But this fact casts doubt on whether Towd has been harmed and will continue to be harmed by mere presence of the non-monetary default.

Counter-Arguments

As discussed, Towd maintains both that it is not obligated to accept payments from the Debtor and that allowing this case to move forward would violate the Bankruptcy Code.

Towd relies, in part, on In re Lippolis, 228 B.R. 106 (E.D. Pa. 1998). In Lippolis, the District Court reversed the Bankruptcy Court's Order denying stay relief and dismissed a case in which the property was transferred from mother (herself a bankruptcy debtor) to son (one of the debtors named in the case) on the eve of the sheriff's sale and in violation of the due-on-sale mortgage provision. The Court there found that a cure would require a re-transfer of the property and was thus not feasible.

The particular facts of Lippolis warranted relief and dismissal. The Debtor's mother, who was the original purchaser of the property, filed for bankruptcy protection. After receiving stay relief in the mother's bankruptcy, the lender scheduled a sheriff's sale. Two (2) days prior to that sale, the debtor dismissed her bankruptcy and sold the property to her son and his spouse for $1.00. The new owners of the property then immediately filed for bankruptcy, again subverting sale of the transferred property. The Lippolis Court specifically found that the because the bankruptcy had been filed in bad faith in order to thwart the rights of the creditor, that relief from the stay was appropriate. In re Lippolis, 228 B.R. 106, 112 (E.D. Pa. 1998). [12]

We have no evidence of bad faith here. And although Towd insists that the Debtor is executing a "scheme," the facts do not support that conclusion. First Motion for ***660** Relief at 4. The Debtor's Father transferred the Property to the Debtor and himself jointly in 2012, about eleven (11) years ago. The transfer was made not on the eve of a sheriff's sale but because the Debtor's Father's health was failing. [13] The Debtor has been struggling to keep up with payments for nearly a dozen years. Towd presents no evidence that the motivation here is subversive.

A more compelling argument, but one which Towd doesn't directly make, is that the mortgagee has been harmed both by the delay in payments and the necessary litigation and attorney's fees that have resulted from the Debtor's bankruptcy filing. The Debtor's Father- the mortgagor with whom Towd bargained- could also have filed for bankruptcy. But he did not do so. This bolsters Towd's assertion that it should not have to do business with someone with whom it didn't contract.

While the monetary harm suffered by Towd as a result of this bankruptcy lends credibility to the argument that Towd

would have been better off being paid by the Debtor's Father (assuming he had the ability to pay) with whom it chose to do business, in the end I find this argument unconvincing for two (2) reasons. First, as discussed, the law allows bankruptcy debtors to cure defaults even when they lack privity with lenders. The second reason is related to the first; one of the primary purposes of chapter 13 is to allow a debtor to remain in his home. E.g. In re Ortiz, 2008 WL 5157682, at *4 (Bankr. D.N.M. Aug. 14, 2008). I therefore find that the balance of the harms weighs in favor of the Debtor.

VI. CONCLUSION

This Opinion arguably dilutes the force of the Due-on-Sale Clause in the Mortgage. However, confirmation of the Debtor's Plan, if reached, will not erase this provision or even limit the availability of remedies. Towd will either get paid through the chapter 13 or can seek redress in state court.

Confirmation would therefore not violate Towd's rights. In balancing the interests between the chapter 13 Debtor, who is trying to stay in his home and pay off arrears, and the mortgage lender seeking the benefit of its bargain, I find that confirming a Plan which calls for the monetary cure of a mortgage in which there has been a non-monetary default is neither prohibited by the Code nor an affront to public policy.

All Citations

650 B.R. 651

Footnotes

1 Counsel for the Debtor informed the Court on April 20, 2023 (during a hearing on another matter) that the Property was damaged by a fire. No further facts or details have been provided; no record of or pleading related to the events has been submitted. While damage caused by the fire may – possibly and eventually – render the current matter moot, as of this writing the property secures the mortgage and, therefore, the dispute remains an actual controversy.

2 This modification was approved in one of the *Debtor's* prior bankruptcies. Doc. # 33 in case 15-13575.

3 The mortgagee does not indicate in the foreclosure complaint that the Due-on-Sale Clause may have been violated; the foreclosure action resulted from a default in payments.

4 However, under the St. Germain Act, "a lender may not exercise its option pursuant to such a 'due-on-sale' clause when the transfer is to a relative resulting from the death of the borrower *or when the spouse or children of the borrower become an owner of the property*. 12 U.S.C. §§ 1701j–3(d)(5) and (6) (emphasis added); In re Alexander, 2007 WL 2296741, at *3 (Bankr. N.D. Fla. Apr. 25, 2007) (holding that a due-on-sale clause was not effective upon transfer to the Debtor's children following the death of the Debtor); In re Martin, 176 B.R. 675, 676 n.1 (Bankr. D. Conn. 1995).

Here, neither party raises the issue of whether the fact that the relevant transfer was made from father to son affects the analysis. Therefore, I too will assume that the Due-on-Sale Clause is valid.

5 See e.g. In re Espanol, 509 B.R. 422, 427 (Bankr. D. Conn. 2014); In re Mullin, 433 B.R. 1 (Bankr. S.D. Tex. 2010) (noting that a cure of the mortgage would require reinstatement of property in original holder's name); In re Tewell, 355 B.R. 674, 681 (Bankr. N.D. Ill. 2006) ("To allow debtors to effectively ignore due on sale clauses invoked by holders of home mortgages stretches the language of § 1322(b)(2) past the

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breaking point.”); In re Threats, 159 B.R. 241 (Bankr. N.D. Ill. 1993); In re Allen, 300 B.R. 105, 116 (Bankr. D.D.C. 2003).

6 See, e.g., In re Smith, 469 B.R. 198, 201 (Bankr. S.D.N.Y. 2012); In re Garcia, 276 B.R. 627, 633 (Bankr. D. Ariz. 2002); In re Rutledge, 208 B.R. 624, 628 (Bankr. E.D.N.Y. 1997).

7 In re Lippolis, 228 B.R. 106 (E.D. Pa. 1998) is distinguished *infra* and, in any event, is not binding precedent.

8 A debtor not in privity with a mortgagee may cure a monetary default. In re Garcia, 276 B.R. 627, 631-33 (Bankr. D. Ariz. 2002); In re Rutledge, 208 B.R. 624, 628 (Bankr. E.D.N.Y. 1997) (citing Johnson v. Home State Bank, 501 U.S. 78, 111 S.Ct. 2150, 115 L.Ed.2d 66 (1991)).

9 Although Towd arguably sat on its rights by not raising the issue of the non-monetary breach prior to the current bankruptcy, the lender has not waived its rights to do so now. In re Espanol, 509 B.R. 422, 429 (Bankr. D. Conn. 2014); In re Tewell, 355 B.R. 674, 685 (Bankr. N.D. Ill. 2006).

10 It is also possible that the anti-modification clause is not applicable here due to the fact that the Property may have been destroyed in a fire in early April, 2023. However, these facts have not been developed on the record.

11 Contrary to the contention of Towd (see First Motion for Relief at 3), the mortgagee had at least constructive knowledge of the transfer. The Property has been identified as jointly owned between the Debtor and the Debtor's Father since the First Case (filed in 2012). The mortgagee filed several pleadings in the 2013 Second Case; these pleadings include reference to the fact that Property is jointly owned. During the pendency of the Debtor's prior case – the Third Case, filed in 2015 – the lender entered into a modification of the Mortgage, which was approved by the Bankruptcy Court.

12 Similarly, In re Allen, 300 B.R. 105, 115 (Bankr. D.D.C. 2003) found that the debtor could not cure the non-monetary default where the debtor's conduct was inequitable; a half interest in the property was transferred to the debtor's mother on the eve of foreclosure.

13 The Debtor represented this to the Court at the February 2, 2023 confirmation hearing.

End of Document

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