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Underwater Homeowner to Uncooperative Mortgage Lender: Take My Home, Please! Does Dirt for Debt Work in Chapter 13?

Eugene R. Wedoff

Consider this situation: A couple with only moderate income has had to relocate, and the mortgage on their vacated home is underwater, with a balance greater than the home's value. The homeowners can't sell the home unless their mortgage lender agrees, and the mortgage lender won't agree to a sale and chooses not to foreclose the mortgage. So the homeowners still have the obligation to make mortgage payments on the vacated home—and insure it, and maintain it, and pay its property taxes, and (if it's a condo) pay their homeowners' assessments—but now they also have whatever costs are incurred in their new living space. They don't have enough income to cover all of these expenses. A bankruptcy could help them by discharging their personal liability for the mortgage payments, but could it also remove the other obligations of ownership? Specifically, can a bankruptcy filing require their lender to assume the ownership obligations by taking the home in payment of its secured claim?

This method of treating a secured claim, known colloquially as making the creditor take "dirt for debt," is recognized in Chapter 11 cases, but the cost of proceeding in that chapter makes it impractical for most homeowners. For most homeowners, the dirt for debt option would only be viable in Chapter 13. Its availability under that chapter, though, is debatable, with a set of conflicting decisions on the question,[1] and at least two cases now pending at the circuit level.[2]

This *Law Letter* takes a closer look at dirt for debt in Chapter 13, first outlining the settled law in Chapter 7 and 11 and then examining the arguments made in the Chapter 13 decisions.[3] The conclusion is that Chapter 13 does offer the same dirt-for-debt option that Chapter 11 does.

Paying Claims with Estate Property Outside of Chapter 13

Chapter 7

In Chapter 7 there is no provision for payment of claims other

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than in cash. The trustee's duty under Code § 704(a)(1) is to "reduce to money" the property of the debtor's estate and then, under § 726, to pay creditors in the specified priority from the liquidated estate.[4] To reduce the estate property to money, of course, the trustee often has to sell the property, including property subject to liens, but underwater property will probably be sold only with the mortgage holder's consent.[5] Most important for underwater homeowners, the trustee is given no authority to transfer property to a lienholder rather than selling it. The almost universal treatment of underwater property in Chapter 7, then, is abandonment by the trustee under Code § 554(c), leaving the debtor as the owner of the property,[6] with personal liability for whatever ownership expenses are not discharged.[7] So Chapter 7 offers only limited relief to a debtor holding underwater property—and certainly does not offer a live possibility of requiring the mortgage holder to take dirt for debt.

Chapter 11

The situation in Chapter 11 is different. Code § 1123, titled "Contents of plan," sets out, in subsection (a), a number of provisions that a plan must include for dealing with creditor claims and, in subsection (b), a number of optional provisions. Among the mandatory provisions, § 1123(a)(5) requires that each Chapter 11 plan "provide adequate means for the plan's implementation," and in a list of possible means for implementation, it includes subparagraph (D): "sale of all or any part of the property of the estate, either subject to or free of any lien, or the distribution of all or any part of the property of the estate among those having an interest in such property of the estate."[8] *In re Sandy Ridge Dev. Corp.*, the leading case on dirt-for-debt plans in Chapter 11, the Fifth Circuit reads subparagraph (D) as plainly allowing such plans.[9] It points out that the subparagraph makes a sale of estate assets, as would take place in Chapter 7, only the first of two alternatives—emphasizing the word "or"—with the second alternative being a direct "distribution" of estate property to secured creditors. *Sandy Ridge* concludes, then, that "a plan may include a 'give-back' " to creditors.[10]

Sandy Ridge also recognizes the major limitation on dirt-for-debt plans in Chapter 11. In addition to § 1123, governing the content of a plan, § 1129 sets out requirements for plan confirmation. If the holders of secured claims do not accept the plan, § 1129(b)(1) requires that the plan treat their claims fairly and equitably. Requirements for fair and equitable treatment are in turn set out in § 1129(b)(2). For secured claims, under § 1129(b)(2)(A), that treatment must include satisfaction of the claims in one of three ways: (i) cash payments with the debtor retaining the collateral subject to the creditors' liens, (ii) sale of the collateral with liens to attach to the proceeds, or (iii) "the realization by such holders of the indubitable equivalent of such claims."[11] Since dirt-for-debt

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plans do not involve either of the first two options, they can only be confirmed if the objecting creditor's receipt of its collateral is the "indubitable equivalent" of its claim, and the "indubitable equivalent" language, the Fifth Circuit observes, is "at the heart" of its decision.[12]

Sandy Ridge states that the application of this language is "relatively straightforward."[13] To find the indubitable equivalent of a secured claim, *Sandy Ridge* first points out that Code § 506(a) bifurcates the total claim of a secured creditor into an allowed secured claim for the value of the collateral that supports it, and an unsecured claim for the balance.[14] Then, because the claim in question was underwater, with collateral worth less than the amount of the claim, "common sense tells us that property is the indubitable equivalent of itself," so that giving the creditor its collateral necessarily satisfies § 1129(b)(2)(A)(iii).[15] The decision also relies on *In re Murel Holding Corp*., the pre-Code decision that first used "indubitable equivalent" to describe fair treatment of secured claims.[16] In determining an appropriate "substitute" for a secured claim, *Murel Holding* had pointed out that the creditor's goal was "to get his money or at least the property." And because the plan in *Sandy Ridge* gave the secured creditor precisely the property that was its substitute for cash payment, the Fifth Circuit held the indubitable equivalence that *Murel Holding* required was satisfied.[17]

This holding has been well accepted.[18] The only circuit opinion applying *Sandy Ridge* to a proposed dirt-for-debt plan, the Ninth Circuit's *Arnold & Baker Farms* decision, adopts *Sandy Ridge's* holding and states it this way:

> [T]he value of the secured portion of an undersecured creditor's total claim is *by definition* equal to the value of the collateral securing it. Therefore, a creditor necessarily receives the indubitable equivalent of its secured claim when it receives the collateral securing that claim, regardless of how the court values the collateral.[19]

Arnold & Baker Farms, however, affirmed a district court's reversal of a bankruptcy court order confirming a dirt-for-debt plan. This was because, in contrast to *Sandy Ridge,* the plan did not propose to transfer to the secured creditor all of its collateral, but only a portion that the debtor asserted was sufficient to satisfy the creditor's entire claim. The Ninth Circuit held that the portion of the collateral proposed to be transferred was not sufficiently valuable to make it equivalent to the claim.[20]

Lower court decisions have reflected the guidance of *Sandy Ridge* and *Arnold & Baker Farms*: if the entire collateral is offered in a dirt-for-debt plan, the plan is confirmable, but if only a portion of the collateral is offered, confirmability depends on the value of that portion found by the court.[21]

Chapter 11, then, would provide a solution for a homeowner burdened by an underwater mortgage in vacated property—the mortgage could be satisfied by transferring ownership to the lender, and the unsecured deficiency discharged. Since the entire collateral would be conveyed, there would be no problem complying with indubitable equivalence. The difficulty is not the availability of dirt-for-debt. Rather, for most homeowners, the difficulty is with the cost of an individual Chapter 11 case. The filing fee alone for a Chapter 11 case is now over $1700,[22] and an ongoing study of individual Chapter 11 cases found that the median fee that debtors in 2013 had agreed to pay their Chapter 11 attorneys was over $10,000.[23] Unsurprisingly, the same study found that the median monthly income of individuals filing Chapter 11 in 2013 was over $8,600 (more than $100,000 annually), compared to a median annual income for Chapter 13 filers in 2010 of less than $38,000.[24] Chapter 11 is not likely to be economically available to most homeowners with underwater mortgages.

Paying Claims with Estate Property in Chapter 13

The provisions of Chapter 13 that bear on dirt-for-debt plans appear, at least at first glance, to make Chapter 13 not only more economical than Chapter 11, but also equally available. As in Chapter 11, there is one section (§ 1322) governing plan content and another (§ 1325) governing plan confirmation. Each of these sections includes two provisions that have been cited in support of dirt-for-debt plans.

For plan content, § 1322(b)(8) allows "the payment of all or part of a claim against the debtor from property of the estate or property of the debtor" and § 1322(b)(9) allows "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."

For plan confirmation, § 1325(a)(5) sets out three alternatives for treatment of a secured claim. The first, § 1325(a)(5)(A) allows confirmation of any claim treatment that the creditor accepts. For nonconsenting creditors, two alternatives remain: payment of the claim under § 1325(a)(5)(B) or "surrender" of the collateral under § 1325(a)(5)(C). The payment and surrender options—subparagraphs (B) and (C) of § 1325(a)(5)—have generated separate lines of case law on the availability of dirt-for-debt treatment in Chapter 13.

Surrender of estate property—the definition of "surrender"

The most common dirt-for-debt Chapter 13 plans treated in the published decisions (1) exercise the § 1322(b)(9) option of vesting the mortgaged property in the mortgage lender at confirmation and (2) propose to comply with § 1325(a)(5) by surrendering the property under subparagraph (C). All of the published decisions accept that "vesting" has the effect of transferring title.[25] The dispute in the case law is over the meaning of "surrender."

The decisions that approve a dirt-for-debt plan based on surrender and vesting in Chapter 13 view "surrender" as affecting the debtor only. Under this view, surrendering property requires the debtor to give up all rights in the property, but it has no effect in itself on ownership of the property, instead making ownership subject to other applicable provisions.[26] With surrender focusing only on the debtor's ceding of property rights, there is no conflict with an additional provision vesting those rights in the mortgage lender. To the contrary, as *In re Sagendorph* observes, "[A] transfer of property presupposes its surrender by the transferor. Surrendering . . . is a preliminary step in the process of transferring title."[27]

The decisions rejecting dirt-for-debt plans have a more expansive view of surrendering property. These decisions read "surrender" as affecting both debtors and creditors, not only requiring debtors to cede ownership rights, but also preserving nonbankruptcy rights in the creditors—either to accept or reject any tender of title to the surrendered property, as they choose. *In re Rosa* states the position: "'[S]urrender' means only that the debtor will make the collateral available so the secured creditor can, if it chooses to do so, exercise its state law rights in the collateral."[28] Surrender, in this view, contradicts vesting, since vesting would remove the creditor's right to decline a conveyance of the surrendered property.

The dispute then, is a tightly focused one. There is agreement that surrender under § 1325(a)(5)(C) does not in itself convey the surrendered property. The question, rather, is whether surrender prevents any other provision—like vesting under § 1322(b)(9)—from providing for such a conveyance.

In other legal contexts, "surrender" does not appear to confer a right to reject a conveyance. So, for example, when a life insurance policy is "surrendered," the insurer is given no option of refusing the tendered policy, but is required—as the contract specifies—to cancel the policy and pay its surrender value.[29] And in a more pertinent context, Code § 521(a)(3) requires a debtor to "surrender to the trustee all property of the estate." Far from giving the trustee a right to decline to accept estate property surrendered by the debtor, the Code sets out procedures in § 554 for the property to be abandoned—which would only be relevant if property surrendered came within the trustee's control. Like an insurer who is bound by a contract to accept a surrendered insurance policy, the trustee is bound to "collect" surrendered estate property by Code § 704(a)(1). In neither situation does "surrender" negate otherwise applicable provisions requiring acceptance of the surrendered property.

Surrender of estate property—the impact of the Pratt *decision*

So what is the source of the idea that "surrender" confers a right on secured creditors to refuse to accept surrendered property in Chapter 13? One source is a set of bankruptcy decisions discussing the effect of § 1325(a)(5)(C) without considering whether vesting would produce a different result.[30]

But another source is the First Circuit's *Pratt* decision, which interprets "surrender" as used in Code § 521(a)(2).[31] This provision requires all individual Chapter 7 debtors whose schedules include debts secured by estate property (A) to file at the beginning of the bankruptcy case "a statement of . . . intention with respect to the retention or surrender of such property" and (B) to perform this intention shortly thereafter. Section 523(a)(2), then, often results in collateral being surrendered to creditors in Chapter 7 cases. The First Circuit's analysis of the effect of surrender in this context has been cited as persuasive in decisions both supporting and rejecting dirt-for-debt plans in Chapter 13.[32] And *Pratt* is indeed instructive.

The factual predicate of *Pratt* is unusual. The Pratts were a married couple who owned a car that they had financed through GMAC with a lien in GMAC's favor. Five years after they bought the car, when the Pratts were in a Chapter 7 case, they gave notice that they intended to surrender the car, and GMAC obtained relief from the automatic stay so that it could enforce its lien. But GMAC determined that the car was worth less than the cost of repossession, so it left the car in the Pratts' possession. The car, meanwhile, had become inoperable and worthless, and the Pratts wanted to dispose of it. The applicable state law, however, required that a salvage dealer could only accept a car that was free of liens. This requirement led the debtors to ask GMAC for a release of its lien. GMAC refused, and the debtors sought sanctions against GMAC for violation of the bankruptcy discharge, arguing that GMAC's refusal to issue a lien waiver had the effect of coercing them into paying the remaining debt on the car.[33]

The First Circuit ruled on this argument by first considering whether the Pratts, by surrendering the car, had imposed a requirement on GMAC to take it back. The court explained its understanding of surrender under § 521(a)(2) and held that it imposed no requirement on GMAC's part:

> [T]he most sensible connotation of "surrender" in the present context is that the debtor agreed to make the collateral available to the secured creditor - viz., to cede his possessory rights in the collateral . . . . [N]othing in subsection 521(a)(2) remotely suggests that the secured creditor is required to accept possession of the vehicle . . . as such a reading would be at odds with well-established law that a creditor's decision whether to foreclose on and/or repossess collateral is purely voluntary and discretionary. Thus, we agree with the GMAC contention that the Pratts' surrender did not require that it repossess the vehicle if GMAC deemed such repossession cost ineffective.[34]

This discussion of "surrender," however, while useful for indicating that surrender itself involves only the ceding of the debtor's rights, does not imply that surrender itself confers a right on a secured creditor to take no action with respect to the surrendered property. To the contrary, the analysis is limited to "the present context"—a Chapter 7 case—and its reference to the creditor's choice about repossession is based on nonbankruptcy law (with no citation to any bankruptcy provision). As discussed above, there is no provision in Chapter 7 that provides for transferring estate property to a secured creditor, and so, in the Chapter 7 context, a secured creditor can properly rely on its nonbankruptcy right to decline to accept surrendered property. But *Pratt's* discussion of surrender is completely compatible with the understanding that other bankruptcy provisions may require action that surrender itself does not.

Indeed, *Pratt* goes on to hold that, in the circumstances of that case, another provision of bankruptcy law—discharge under § 524(a)(2)—did require GMAC to issue a lien waiver that surrender itself would not have required. As the decision explains, § 524(a)(2) prohibits action by a creditor to coerce a debtor into paying a discharged debt, and it found GMAC's failure to issue the lien waiver had the practical effect of coercing the Pratts to pay their car loan in order to dispose of the car, thus "eliminating the Pratts' 'surrender' option under § 521(a)(2)."[35]

Pratt, then, supports an interpretation of "surrender" in § 1325(a)(5)(C) consistent with dirt-for-debt plans: surrendering collateral under subparagraph (C) does not negate the debtor's option to vest the collateral in the secured creditor under § 1322(b)(9).

Surrender of estate property—other considerations

Pratt also addresses two policy arguments made in favor of prohibiting vesting in connection surrender of collateral: (1) that this would improperly impair the secured creditor's state law rights, and (2) that it would impose unfair costs on the creditor. The court addressed GMAC's right under state law to refuse to issue a lien waiver by holding that "the federal bankruptcy-law interest in according debtors a fresh start, free from objectively coercive . . . demands, must be accorded supremacy."[36] The need of a homeowner to be free from the ownership obligations of property that the debtor cannot inhabit is parallel.

As to the danger that GMAC might be improperly burdened by having to dispose of worthless property, the court quoted *In re Groth*:

> [A] debtor in a chapter 7 case, as part of his fresh economic start, should be permitted to surrender [worthless] collateral he does not intend to keep. If the secured creditor determines that its collateral is worth less than the cost of taking it into its possession, the creditor must waive the effect of its lien so that the debtor is able to dispose of the collateral.[37]

In the context of surrender of underwater real estate, the answer to the creditor's concern about costs would again be parallel—the creditor should release its mortgage on any property that would have a negative financial value.

The alternative approach: paying secured claims with estate property

There is an alternative approach for Chapter 13 plans to convey an underwater home to a mortgage lender. Instead of vesting the home in the lender under § 1322(b)(9) and surrendering it under § 1325(a)(5)(C), a plan could provide (1) that the lender's secured claim will be paid from property of the estate—the home—as authorized by § 1322(b)(8), and (2) that the payment will comply with the confirmation requirements of § 1325(a)(5)(B) for paying secured claims. This approach is fully considered in only two reported decisions. The approach was approved in a Chapter 12 case, with relevant statutory language identical to Chapter 13, in the Second Circuit's *Kerwin* decision.[38] It was rejected in a Chapter 13 bankruptcy case, *In re Lemming*.[39] The holdings of each are worth considering.

Approving payment of secured claims with estate property—Kerwin

Kerwin involved a farming operation. The debtor had tried to operate a 135-acre farm with her husband; the farm failed, the couple divorced, and the debtor was left with a mortgage that the farm's cash flow could not support. She proposed a Chapter 12 plan that would pay the mortgage by transferring to the lender the bulk of the farmland, with a value equal to the mortgage balance, and retain a small portion of the land for herself, free of the mortgage lien. The lender objected, arguing that it should either receive all of the farmland that served as its collateral, or if not, retain a lien on whatever portion of the land the debtor kept for herself until it received the full principal and interest owed on its loan.[40]

The Second Circuit rejected the lender's arguments. It dealt first with § 1225(a)(5), which sets out Chapter 12's requirements for confirming a plan's treatment of secured claims and, at the time of the decision, contained the same language as § 1325(a)(5). The Court held that a surrender of collateral—the subparagraph (C) option—would have required a transfer of all of the collateral, and so could not support the debtor's plan.[41] But it held that the subparagraph (B) option could be satisfied by a direct transfer of estate property, not limited to cash payments and not limited to a creditor's collateral, with the only requirement being that the property transferred be at least equal to the amount of the secured claim.[42] The court's final holding on the terms of the plan was that adequate protection was only required to assure that the amount of the secured claim was paid, so that liens would be required if periodic payments of the claim were being made, but not if the transferred property satisfied the claim in full.[43] The only mention in the opinion of the optional plan payments set out in § 1222(b) is the observation that the interpretation given to § 1225(a)(5)(B) "fits with" them. As an example of the congruity, the opinion points to § 1222(b)(7), which, in language identical to § 1322(b)(8), allows a plan to "provide for the payment of all or part of a claim against the debtor from property of the estate or property of the debtor."[44]

Kerwin is entirely supportive of a Chapter 13 plan providing for payment of an underwater mortgage by conveying the mortgaged home to the lender. The only relevant difference is that *Kerwin* involved an oversecured mortgage claim, so that transfer of a portion of the collateral satisfied the creditor's full claim. With an underwater mortgage, conveyance of the entire collateral satisfies only the allowed secured claim resulting from bifurcation under § 506(a), and leaves an unsecured deficiency. As amended by BAPCPA, § 1325(a)(5)(B)(i) now provides that the secured creditor must retain its lien until the debtor receives a discharge under § 1328 (usually at the completion of plan payments) or until "the payment of the underlying debt determined under nonbankruptcy law." The apparent intent of the new language was to deal with a situation in which a Chapter 13 debtor retains collateral worth less than the full claim. If the debtor pays the amount of the bifurcated secured claim, but later fails to obtain a discharge, the retained lien continues to protect the creditor's right to payment of the deficiency under nonbankruptcy law.[45]

It could be questioned whether a continuing lien gives the creditor any additional protection when its secured claim is paid through transfer of all of its collateral. In this situation, the creditor would have title to all of the property to which the lien attaches. There is, however, a benefit to the creditor in situations where the collateral is subject to junior liens. Mortgage lenders have objected to receiving title to their collateral on the ground that their mortgage lien would merge into the transferred title, preventing a subsequent foreclosure.[46] But the BAPCPA requirement that plans provide for the lien to be maintained until the full claim is paid prevents this merger, allowing the secured creditor to file a foreclosure case if necessary.

Rejecting payment of secured claims with estate property—Lemming

The bankruptcy court decision that rejects the *Kerwin* reasoning, *In re Lemming*, makes a holding that Chapter 13 plans may virtually never pay a secured claim by conveying collateral to the secured creditor.[47] *Lemming* gives three reasons for this holding: first, that allowing property to pay the claim would "short-circuit" the decisions disallowing surrender and vesting as a means of dealing with secured claims; second, that the payment of a secured claim with property conflicts with state law; and finally, that the legislative history of § 1322(b)(8) indicates that it permits estate property to be used in payment of claims only if the property is first sold.[48]

Each of these reasons is questionable. The decisions disapproving surrender and vesting—even if they were correctly decided—deal with separate statutory provisions, and so their reasoning cannot apply directly here. And, of course, if the Bankruptcy Code permits payment of claims with estate property, contrary state law would be preempted.[49] The most significant reason given by *Lemming* for prohibiting payments with property, the legislative history of § 1322(b)(8), also has difficulties.

Lemming examines legislative history because it finds that the option given in § 1322(b)(8) to pay claims "from property of the estate" is ambiguous. It points out that the 1973 *Report of the Commission on the Bankruptcy Laws of the United States,* one of the foundational documents for the 1978 Bankruptcy Code, suggested that Congress amend the former Bankruptcy Act's Chapter XIII to authorize "payment of debts out of proceeds of the sale" of the debtor's property as well as from future income.[50] *Lemming* then quotes a Committee Report on the Bankruptcy Code stating that § 1322(b)(8) would permit a plan to provide not only for payments out of the debtors future income but also through "liquidation of some of the debtors [sic] property."[51] *Lemming* suggests that by giving liquidation of property as an option under § 1322(b)(8), the paragraph was intended to require liquidation before the property is used in payment.

A closer look at the legislative history suggests the contrary. The 1973 Commission Report set out statutory language to implement its recommendations, and its proposed Section 6-201 stated that a wage-earner's plan "may include provisions for the payment of part of the debts from other money or from *proceeds of* the debtor's property."[52] But in formulating § 1322(b)(8), the drafters of the Code eliminated the words "proceeds of" from the Commission's statutory draft, indicating the property itself, not only its proceeds, could be transferred in payment of a debt. Moreover, in its section-by-section analysis of the Code, the Committee report cited in *Lemming* does not limit § 1322(b)(8) to payment through proceeds of estate property, but—reflecting the text of the provision—puts no limit on direct payment from the property itself. ("Paragraph (8) [of § 1322(b)] is new. It permits the plan to provide for payment of claims from property of the estate or from property of the debtor . . . .")[53]

Finally, *Lemming* recognizes that § 1325(a)(5)(B) allows confirmation of a plan paying secured claims directly with estate property.[54] The subparagraph requires that "the value . . . of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim," and since there is only a need to value the property being used to pay claims if the property is in a form other than cash, direct payments of estate property are necessarily allowed. Here the legislative history—statements reporting on the final draft of the bill—is directly on point: "The secured creditor in a case under chapter 13 may receive any property of a value . . . equal to the allowed amount of the creditor's secured claim rather than being restricted to receiving deferred cash payments."[55] *Lemming's* holding—that § 1325(a)(5)(B)'s allowance of direct property payments is negated by § 1322(b)(8)—would make that part of § 1325(a)(5)(B) a nullity, and so violate what the Supreme Court declared in *RadLAX* to be a "cardinal rule" of statutory construction: "if possible, effect shall be given to every clause and part of a statute."[56]

Kerwin's interpretation of the secured debt provisions of Chapter 12/13, then, is sound, and both of the approaches for confirming dirt-for-debt plans—surrender/vesting and direct property payment—should be available to the homeowner with an underwater mortgage.

ENDNOTES:

[1]Decisions holding that a Chapter 13 plan may require a mortgage holder to accept transfer of the debtor's home in payment of the mortgage include In re Brown, No. 14-12357-JNF (Bankr. D. Mass. March 4, 2016) (available at http://www.ncbrc.org/wp-content/uploads/Brown-Bankr-Mass-opinion-030416.pdf); In re Stewart, 536 B.R. 273 (Bankr. D. Minn. 2015); In re Zair, 535 B.R. 15 (Bankr. E.D. N.Y. 2015), vacated sub nom., HSBC Bank USA, N.A. v. Zair, 550 B.R. 188 (E.D. N.Y. 2016); In re Sagendorph, 2015 WL 3867955 (Bankr. D. Mass. 2015); and In re Watt, 520 B.R. 834, 72 Collier Bankr. Cas. 2d (MB) 908 (Bankr. D. Or. 2014), vacated sub nom., Bank of New York Mellon v. Watt, 2015 WL 1879680 (D. Or. 2015). Employing identical statutory language in Chapter 12, a plan requiring a mortgage lender to accept farmland in payment of its claim was approved in In re Kerwin, 996 F.2d 552, 24 Bankr. Ct. Dec. (CRR) 615, 29 Collier Bankr. Cas. 2d (MB) 82, Bankr. L. Rep. (CCH) P 75310 (2d Cir. 1993).

Decisions finding that mortgagees cannot be required to accept such transfers of their collateral include Bank of New York Mellon v. Watt, 2015 WL 1879680 (D. Or. 2015); In re Tosi, 546 B.R. 487 (Bankr. D. Mass. 2016); In re Sherwood, 2016 WL 355520 (Bankr. S.D. N.Y. 2016); In re Weller, 548 B.R. 392 (Bankr. D. Mass. 2016); In re Williams, 542 B.R. 514, 521 (Bankr. D. Kan. 2015); In re Lemming, 532 B.R. 398 (Bankr. N.D. Ga. 2015); In re Rose, 512 B.R. 790, 793 (Bankr. W.D. N.C. 2014); and In re Rosa, 495 B.R. 522, 523 (Bankr. D. Haw. 2013).

[2]There are circuit level appeals presently pending from the district court decisions in Bank of New York Mellon v. Watt, 2015 WL 1879680 (D. Or. 2015), and HSBC Bank USA, N.A. v. Zair, 550 B.R. 188 (E.D. N.Y. 2016). I am one of the attorneys for the debtor in the *Zair* appeal. The bankruptcy court's decision in In re Brown, No. 14-12357-JNF (Bankr. D. Mass. March 4, 2016), is subject to a request for direct appeal to the First Circuit.

[3]Chapter 12 involves identical statutory provisions to those in Chapter 13 and so the one significant dirt-for-debt decision arising in a Chapter 12 case is considered in the discussion of Chapter 13.

[4]This is a longstanding limitation on the method of paying claims in bankruptcy. Section 2 of the 1898 Bankruptcy Act gave jurisdiction given to courts to "[c]ause the estates of bankrupts to be collected, reduced to money and distributed." See Williams v. Austrian, 331 U.S. 642, 644, 67 S. Ct. 1443, 91 L. Ed. 1718 (1947) (discussing bankruptcy jurisdiction). And trustees, like Chapter 7 trustees under the Code, were authorized by § 47(2) of the Act, to "[c]ollect and reduce to money" the property of the debtor's estate.

[5]The possibility of a nonconsensual sale of underwater property free and clear of liens is thoroughly discussed in Brad B. Erens and David A. Hall, *Secured Lender Rights in 363 Sales and Related Issues of Lender Consent*, 18 Am. Bankr. Inst. L. Rev. 535, 543-56 (2010) (reporting conflicting decisions with no consensus allowing sales without lienholder consent). But even if it were clear that a nonconsensual sale was possible, it is unlikely that a Chapter 7 trustee would pursue one, since the sale would produce no apparent benefit to the estate.

[6]See In re Service, 155 B.R. 512, 515 (Bankr. E.D. Mo. 1993) ("Abandonment typically contemplates a determination by a trustee . . . that a certain property is not beneficial to the bankruptcy estate. Thereafter, the trustee . . . releases the property to the debtor.").

[7]The Chapter 7 discharge removes the debtor's personal liability under the mortgage, not the claims that can be asserted against the property in rem. Johnson v. Home State Bank, 501 U.S. 78, 84, 111 S. Ct. 2150, 2154, 115 L. Ed. 2d 66, 21 Bankr. Ct. Dec. (CRR) 1293, 24 Collier Bankr. Cas. 2d (MB) 1171, Bankr. L. Rep. (CCH) P 73993 (1991). That is of little concern to a debtor who wants to give up the property that would remain subject to claims. But because the discharge under Code § 707(b) only covers prepetition debts, it does nothing to reduce the debtor's ownership costs that arise after the bankruptcy filing. See In re Rosenfeld, 23 F.3d 833, 837, 25 Bankr. Ct. Dec. (CRR) 981, 30 Collier Bankr. Cas. 2d (MB) 2054, Bankr. L. Rep. (CCH) P 75871 (4th Cir. 1994) (debts arising from "continued post-petition ownership of the property" are not discharged). Any duty of the debtor to maintain the property under local ordinances, pay property taxes as a personal obligation, and insure against personal liability are postpetition obligations that are not discharged. And while homeowners' assessments were treated in some decisions as a dischargeable prepetition contractual obligation—see, e.g. Matter of Rosteck, 899 F.2d 694, 697, 20 Bankr. Ct. Dec. (CRR) 625 (7th Cir. 1990)—Code § 523(a)(16), added by BAPCPA in 2005, continues the debtor's liability by excepting assessments for a condominium unit from discharge in Chapter 7 "for as long as the debtor . . . has a legal, equitable, or possessory ownership interest in such unit."

[8]Like Chapter 7 provisions for paying claims only in money, this is also a continuation of prior law. The House Report on the Bankruptcy Code states that the language of § 1123(a)(5) (originally subparagraph (a)(4)) was drawn from § 216 of the Bankruptcy Act. H.R. Rep. 95-595 (1977), at 407, reprinted in 1978 U.S.C.C.A.N. 6363. Section 216(10) of the Act listed as one of the means for execution of a plan of reorganization, "the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein."

[9]Matter of Sandy Ridge Development Corp., 881 F.2d 1346, 1352, 18 Bankr. Ct. Dec. (CRR) 13, 19 Bankr. Ct. Dec. (CRR) 1237, Bankr. L. Rep. (CCH) P 73070 (5th Cir. 1989).

[10]Sandy Ridge, 881 F.2d at 1352.

[11]This set of requirements for the cramdown of secured claims is outlined in RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065, 2069-70, 182 L. Ed. 2d 967, 56 Bankr. Ct. Dec. (CRR) 144, 67 Collier Bankr. Cas. 2d (MB) 483, Bankr. L. Rep. (CCH) P 82218 (2012).

[12]Sandy Ridge, 881 F.2d at 1350.

[13]Sandy Ridge, 881 F.2d at 1350.

[14]Sandy Ridge, 881 F.2d at 1349, citing United Sav. Ass'n of Texas v. Timbers of Inwood Forest Associates, Ltd., 484 U.S. 365, 108 S. Ct. 626, 630, 98 L. Ed. 2d 740, 16 Bankr. Ct. Dec. (CRR) 1369, 17 Collier Bankr. Cas. 2d (MB) 1368, Bankr. L. Rep. (CCH) P 72113 (1988).

[15]Sandy Ridge, 881 F.2d at 1349-50.

[16]Sandy Ridge, 881 F.2d at 1350, citing In re Murel Holding Corp., 75 F.2d 941, 942 (2d Cir. 1935) as the source of the indubitable equivalent provision.

[17]Sandy Ridge, 881 F.2d at 1350.

[18]See, e.g., Matter of James Wilson Associates, 965 F.2d 160, 172, 26 Collier Bankr. Cas. 2d (MB) 1673, Bankr. L. Rep. (CCH) P 74636 (7th Cir. 1992), which, while not dealing with a dirt-for-debt plan, cited *Sandy Ridge* as illustrating the operation of the cramdown of secured claims in Chapter 11:

> [I]t is the law that, provided the plan of reorganization gives the secured creditor the "indubitable equivalent" of his secured interest, the bankruptcy judge can force the creditor to accept the exchange. 11 U.S.C.A. § 1129 (b)(2)(A)(iii); In re Murel Holding Corp., 75 F.2d 941, 942 (C.C.A. 2d Cir. 1935) (L. Hand, J.); Matter of Sandy Ridge Development Corp., 881 F.2d 1346, 1349-50, 18 Bankr. Ct. Dec. (CRR) 13, 19 Bankr. Ct. Dec. (CRR) 1237, Bankr. L. Rep. (CCH) P 73070 (5th Cir. 1989).

[19]Arnold & Baker Farms v. United States ex rel. United States Farmers Home Admin. (In re Arnold & Baker Farms), 85 F.3d 1415, 1423 (9th Cir. 1996).

[20]Arnold & Baker Farms, 85 F.3d at 1422.

[21]See Irving E. Walker and Jonathan A. Grasso, *Can a Debtor Force a Secured Creditor to Accept "Dirt for Debt"?* 31 No. 4 Prac. Real Est. Law. 41, 47 (July 2015) (collecting authorities and distinguishing between dirt-for-debt plans proposing full collateral transfers—approved by an "overwhelming majority" of decisions—and those proposing partial collateral transfers, in which "the critical issue . . . is the court's valuation of the property to be surrendered").

[22]Bankruptcy Court Miscellaneous Fee Schedule, issued under 28 U.S.C.A. § 1930, effective June 1, 2016. The total fee consists of an administrative fee of $550 (¶ 8) and the current statutory filing fee of $1,167 (reflected in ¶ 15).

[23]Preliminary Report of ABI Task Force on Individual Chapter 11 (April 6, 2016 draft) at 72 (available at https://abi-org-corp.s3.amazonaws.com/materials/IndividualCh11StudyFindings__0.pdf).

[24]Preliminary Report of ABI Task Force on Individual Chapter 11 at 56.

[25]For example, In re Rosa, 495 B.R. 522, 524 (Bankr. D. Haw. 2013), one of the first decisions

holding that a dirt-for-debt plan cannot be confirmed over the mortgage holder's objection, states that "[t]he plain meaning of 'vesting' includes a present transfer of ownership." A more recent decision, In re Tosi, 546 B.R. 487, 493 (Bankr. D. Mass. 2016), while also rejecting a dirt-for-debt plan, makes the same point: "[T]o vest property in another, as contemplated in 11 U.S.C. § 1322(b)(9) . . . is to effect of transfer of ownership of that property from the estate to another person or entity."

[26]See, e.g., In re Sagendorph, 2015 WL 3867955 at *2 (Bankr. D. Mass. 2015), citing In re Pratt, 462 F.3d 14, 19, 56 Collier Bankr. Cas. 2d (MB) 1016, Bankr. L. Rep. (CCH) P 80698 (1st Cir. 2006) for this definition of "surrender."

[27]Sagendorph, 2015 WL 3867955 at *4.

[28]In re Rosa, 495 B.R. 522, 523 (Bankr. D. Haw. 2013), citing In re Pratt, 462 F.3d 14, 19, 56 Collier Bankr. Cas. 2d (MB) 1016, Bankr. L. Rep. (CCH) P 80698 (1st Cir. 2006) for this definition of "surrender."

[29]See, e.g., U.S. v. Aetna Life Ins. Co. of Hartford, Conn., 46 F. Supp. 30, 34, 42-1 U.S. Tax Cas. (CCH) P 9266, 29 A.F.T.R. (P-H) P 1123 (D. Conn. 1942) (noting "the power of the insured to demand the cash surrender value of his policy and his right thereafter, upon a physical surrender of the policy, to receive the cash value thereof").

[30]E.g., In re Arsenault, 456 B.R. 627, 629-30 (Bankr. S.D. Ga. 2011); In re Service, 155 B.R. 512, 515 (Bankr. E.D. Mo. 1993).

[31]In re Pratt, 462 F.3d 14, 18-19, 56 Collier Bankr. Cas. 2d (MB) 1016, Bankr. L. Rep. (CCH) P 80698 (1st Cir. 2006).

[32]See notes 26 and 28, above.

[33]Pratt, 462 F.3d at 15-16.

[34]Pratt, 462 F.3d at 18.

[35]Pratt, 462 F.3d at 20.

[36]Pratt, 462 F.3d at 20.

[37]Pratt, 462 F.3d at 20, quoting In re Groth, 269 B.R. 766, 767-68 (Bankr. S.D. Ohio 2001).

[38]In re Kerwin, 996 F.2d 552, 24 Bankr. Ct. Dec. (CRR) 615, 29 Collier Bankr. Cas. 2d (MB) 82, Bankr. L. Rep. (CCH) P 75310 (2d Cir. 1993).

[39]In re Lemming, 532 B.R. 398 (Bankr. N.D. Ga. 2015).

[40]Kerwin, 996 F.2d at 555-56.

[41]Kerwin, 996 F.2d at 557.

[42]Kerwin, 996 F.2d at 558.

[43]Kerwin, 996 F.2d at 558-59.

[44]Kerwin, 996 F.2d at 559.

[45]See, e.g., In re Bullard, 494 B.R. 92, 100-01, Bankr. L. Rep. (CCH) P 82489 (B.A.P. 1st Cir. 2013), appeal dismissed, 752 F.3d 483, 71 Collier Bankr. Cas. 2d (MB) 1058 (1st Cir. 2014), cert. granted, 135 S. Ct. 781, 190 L. Ed. 2d 649 (2014) and aff'd, 135 S. Ct. 1686, 191 L. Ed. 2d 621, 60 Bankr. Ct. Dec. (CRR) 258, 73 C.B.C. 1492, Bankr. L. Rep. (CCH) P 82793 (2015), aff'd sub nom. Bullard v. Blue Hills Bank, 135 S. Ct. 1686, 191 L. Ed. 2d 621, 60 Bankr. Ct. Dec. (CRR) 258, 73 C.B.C. 1492, Bankr. L. Rep. (CCH) P 82793 (2015) (holding that a mortgage bifurcated under § 506(a), but not discharged would have to be subject to the mortgage lien for the full amount of the debt).

[46]In re Zair, 535 B.R. 15, 24 (Bankr. E.D. N.Y. 2015), vacated sub nom., HSBC Bank USA, N.A. v. Zair, 550 B.R. 188 (E.D. N.Y. 2016).

[47]The decision notes one narrow theoretical exception: "If trade custom or course of dealings entails routine settlement of debt with something other than money, it is possible that a plan in a Chapter 12 case or a Chapter 13 business case could provide for such a payment in kind." Lemming, 532 B.R. at 410.

[48]Lemming, 532 B.R. at 408-10.

[49]See Elliott v. Bumb, 356 F.2d 749, 755 (9th Cir. 1966) ("If state law is contrary to federal bankruptcy law, the state law must yield."); Butner v. U.S., 440 U.S. 48, 55, 99 S. Ct. 914, 59 L. Ed. 2d 136, 19 C.B.C. 481, Bankr. L. Rep. (CCH) P 67046 (1979) (state property law should be applied "[u]nless some federal interest requires a different result").

[50]*Report of the Commission on the Bankruptcy Laws of the United States,* H.R. Doc. No. 93-137, at 163-64, 93d Cong., 1st Sess. (1973).

[51]Lemming, 532 B.R. at 409-10, quoting H.R. REP. 95-595, 123 & n.597. 1978 U.S.C.C.A.N. 5963, 6084.

[52]*Report of the Commission on the Bankruptcy Laws of the United States,* at 439 (emphasis added).

[53]H.R. REP. 95-595, 429, 1978 U.S.C.C.A.N. 5963, 6385.

[54]Lemming, 532 B.R. at 410.

[55]124 Cong.Rec. H11, 107 (daily ed. Sept 28, 1978) (statement of Rep. Edwards), reprinted in 1978 U.S.Code Cong. & Admin.News 6481-82; 124 Cong.Rec. S17,423 (daily ed. Oct. 6, 1978) (statement of Sen. DeConcini), reprinted in 1978 U.S.Code Cong. & Admin.News 6550-51.

[56]RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065, 2071, 182 L. Ed. 2d 967, 56 Bankr. Ct. Dec. (CRR) 144, 67 Collier Bankr. Cas. 2d (MB) 483, Bankr. L. Rep. (CCH) P 82218 (2012) (quoting D. Ginsberg & Sons v. Popkin, 285 U.S. 204, 208, 52 S. Ct. 322, 76 L. Ed. 704 (1932)).

