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Effects of the New Bankruptcy Code On Creditors with Secured Claims In Residential Real Property

RICHARD MEDNICK*

The sweeping changes brought about by the Bankruptcy Reform Act of 1978 may have a profound effect on the secured interests of lenders. The rights of a creditor against a debtor, and the procedure that he must follow vary with the chapter of the new Bankruptcy Code under which the debtor files his claim. Richard Mednick, a Judge on the Bankruptcy Court for the Central District of California, explains the procedures required and the interest affected by the most commonly invoked chapters of the new code. Judge Mednick strongly urges that creditors become familiar with these changes, as some new requirements may become traps for the unwary lender.

News all too familiar to lenders with security interests in residential real property is that the borrower has filed a petition in bankruptcy. Bankruptcy is a fact of life with which lenders must cope.¹ Therefore, they are well advised to become generally familiar with the provisions of the Bankruptcy Reform Act of 1978,² commonly referred to as the Bankruptcy Code, since it may affect their secured positions. The rights and problems of a secured creditor may vary depending upon the chapter of the new Bankruptcy Code under which the debtor seeks relief.³ The use of a

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1. *Wright v. Union Cent. Life Ins. Co.*, 304 U.S. 502 (1938); *Mueller v. Nugent*, 184 U.S. 1 (1901).

2. Pub. L. No. 95-598, 92 Stat. 2549 (codified at 11 U.S.C. §§ 101(1)-151326 (1978)).

3. Chapter 7 provides for straight liquidation. Chapter 11 provides for the reorganization of the debtor through a plan to pay creditors, and even permits a liquidating plan of reorganization. 11 U.S.C. § 1123(b)(4) (1978). Chapter 13 provides for the adjustment of debts of an individual with regular income. An involuntary petition may be filed against a debtor only under Chapters 7 and 11. 11 U.S.C. § 303 (1978). (Chapter 9 governs proceedings for municipalities and is not consid-

hypothetical situation will serve to illustrate some provisions of the new Code with which lenders having secured interests in residential real property and their counsel should become familiar.

Alfa owns a home. Beta Corporation holds a first deed of trust on the property in the amount of \$80,000. Gamma holds a second trust deed of \$20,000, which is in default. Delta is a judgment creditor for \$5,000.⁴ The real property has a market value of \$140,000. Gamma has a foreclosure sale set for January 14, 1981 at noon. In December, 1980, suspecting that Alfa is on the verge of filing for bankruptcy relief, Gamma discusses with his attorney how the filing by Alfa of a Chapter 7, 11, or 13 bankruptcy petition will affect his secured rights.

Upon Alfa's filing of a petition in bankruptcy, an estate is created.⁵ With limited exceptions, as of the commencement of the case, the estate is comprised of all the legal or equitable interest of the debtor in any property wherever located.⁶ When the petition is filed, Alfa's interest in the home becomes property of the estate.⁷

In a Chapter 7 filing, after the estate is created, a trustee is appointed to act as the representative of the estate. It is the duty of the trustee to liquidate the estate for the benefit of the creditors.⁸ After all the property comes into the estate, the debtor is permitted to exempt certain properly qualified property.⁹

ered here). The provisions of Chapters 7, 11, and 13 apply only to those Chapters. It is important to recognize that except where provided otherwise in the Code, the provisions of Chapters 1, 3, and 5 *all* apply to Chapters 7, 11, and 13. 11 U.S.C. § 103 (1978).

4. State laws may treat judgment creditors and judgment lien creditors differently. Under California law, a judgment creditor becomes a judgment lien creditor by perfection. CAL. CIV. PROC. CODE § 674.7 (West 1980).

5. 11 U.S.C. § 541 (1978).

6. 11 U.S.C. § 541(a)(1) (1978).

7. This is a major change under the Code. Under § 70a of the former Bankruptcy Act, exempt property did not pass to the estate. See note 19 *infra* and accompanying text.

8. 11 U.S.C. §§ 323(a), 701, 704 (1978). To assist the trustee in marshalling assets for the benefit of the unsecured creditors, 11 U.S.C. §§ 545, 547, 548, and 549 give the trustee certain avoiding powers that may affect the rights of secured creditors. The provisions of 11 U.S.C. § 546 limit those powers.

9. 11 U.S.C. § 522(b) permits the debtor to elect a set of exemptions prescribed in 11 U.S.C. § 522(d) (bankruptcy exemptions), or those created by state or local law and federal law other than § 522(d). The debtor may choose one set or the other, but not both. A dependent of the debtor may file a schedule of exempt property on behalf of the debtor if the debtor fails to do so. 11 U.S.C. § 522(1) (1978). Debtors filing a joint petition may *each* choose a set of exemptions. 11 U.S.C. § 522(m) (1978). The Code gives the state the option to pass legislation making the federal bankruptcy exemptions under § 522(d) inapplicable. The states passing such legislation as of September, 1980, are: Arizona, Florida, Georgia, Indiana, Kansas, Kentucky, Louisiana, Nebraska, Ohio, South Dakota, Tennessee, Virginia and Wyoming.

To protect the debtor and provide the trustee with the time necessary to evaluate and collect the property of the estate, an automatic stay of foreclosures becomes effective upon the filing of a bankruptcy petition. This stay restrains most creditors from taking any action to collect their claims.¹⁰ The scope of the automatic stay is extremely broad, limiting lien enforcement¹¹ and other actions that would affect or interfere with the property of the estate. To stop the noon sale on January 14, 1981, Alfa would have to file his petition with the bankruptcy court no later than 11:59 A.M. on that date. Although it would be ideal if he timely informed Gamma of the filing, it is not necessary to do so. Even without notice, any sale after the filing would be in violation of the automatic stay.¹² However, a petition filed after that time would not void an otherwise proper and timely sale.¹³ In order for Gamma to proceed with the foreclosure sale after a petition is timely filed, he must request the bankruptcy court to grant relief from the automatic stay.¹⁴ The stay created by the filing of the

10. 11 U.S.C. § 3629(a) (1978). The filing of a petition does not operate as a stay in those instances specified in 11 U.S.C. § 362(b).

11. 11 U.S.C. § 506(d) permits liens to pass through the bankruptcy estate unaffected other than by the automatic stay unless a party in interest requests the court to determine and allow or disallow, pursuant to § 506(a), the claim secured by the lien, in which event the lien is void to the extent it is not allowed. H.R. REP. No. 595, 95th Cong., 1st Sess. 357 (1977).

12. Even in the absence of formal notice, a lender with actual notice of the borrower's bankruptcy petition who proceeds with a foreclosure sale may be subject to contempt of court proceedings. See *Fidelity Mortgage Investors v. Camelia Builders, Inc.*, 550 F.2d 47 (2d Cir. 1976). See also note 14 *infra*.

13. The trustee's sale must otherwise be proper so as to prevent its avoidance pursuant to 11 U.S.C. § 548(a)(2), which permits the trustee to avoid any transfer of an interest of the debtor in property that was made within one year before the date of the filing of the petition if the debtor received less than a reasonably equivalent value in exchange for such transfer. 11 U.S.C. § 101(40) defines "transfer". In *Durrett v. Washington Nat'l Ins. Co.*, 621 F.2d 201 (5th Cir. 1980), a debtor's property was sold at a foreclosure sale nine days prior to the filing of a bankruptcy petition. The sole bidder at the foreclosure sale bid the exact amount necessary to liquidate the indebtedness secured by the deed of trust, which was approximately 57.7% of the fair market value of the property on the day of the sale. The court set aside the sale as fraudulent pursuant to § 67d of the former Bankruptcy Act because the transfer was not for "fair consideration" within the meaning of the Act. Section 548 of the Code is largely derived from § 67d of the Act and it would appear that the same principles may apply.

The effects of a bankruptcy proceeding on mortgages and deeds of trust are essentially the same. In those states recognizing mortgages and/or providing for judicial foreclosure procedures, there may be a redemption right that passes to the bankruptcy estate. Once a deed of trust is foreclosed by a trustee's sale, no redemption right remains.

14. 11 U.S.C. § 362(d) (1978). The request for relief from the stay should be

petition will terminate with respect to Gamma thirty days after its request for relief. The court may order the stay continued, pending a final determination of those factors, discussed below, which support relief from the stay.¹⁵

The Code provides that absent such a request, the stay of an act against property of the estate continues until it is terminated or otherwise modified by the court,¹⁶ or until such property is no longer property of the estate.¹⁷ Legislative history indicates that it was the intention of Congress that the stay terminate when the property ceases to be property of the estate because of sale, abandonment, or exemption; but that it not terminate if the property leaves the estate and simply passes to the debtor.¹⁸ This would be the case if Alfa were to perfect his homestead interest in the property prior to the filing of a bankruptcy petition, and the trustee, having no objection to the claim of homestead exemption,¹⁹ were to find no remaining value to the estate. The auto-

made in the district in which the debtor's petition has been filed. Jurisdiction and venue under the Code are governed by 28 U.S.C. § 1471. In *In re Coleman American Companies, Inc.*, 7 B.C.D. 127 (D. Kan. 1981), although the debtor's petition had been filed in the Bankruptcy Court in Kansas, the secured creditor requested relief from the Bankruptcy Court in Colorado. The Kansas court held that such action was a violation of the automatic stay subject to punishment for contempt. *But see In re Coleman American Companies, Inc.*, 6 B.R. 251 (D. Colo. 1980) in which the Colorado court held that it had jurisdiction.

15. 11 U.S.C. § 362(e) (1978) provides:

Thirty days after a request under subsection (d) of this section for relief from the stay of any act against *property of the estate* under subsection (a) of this section, such stay is terminated with respect to the party in interest making such request, unless the court, after notice and a hearing, orders such stay continued in effect pending, or as a result of, a final hearing and determination under subsection (d) of this section. A hearing under this subsection may be a preliminary hearing, or may be consolidated with the final hearing under subsection (d) of this section. If the hearing under this subsection is a preliminary hearing—

(1) the court shall order such stay so continued if there is a reasonable likelihood that the party opposing relief from such stay will prevail at the final hearing under subsection (d) of this section; and

(2) such final hearing shall be commenced within thirty days after such preliminary hearing.

Id. (emphasis added).

16. 11 U.S.C. §§ 362(d), 362(e) (1978).

17. 11 U.S.C. § 362(c)(1) (1978).

18. H.R. REP. NO. 595, 95th Cong., 1st Sess. 357 (1977); S. REP. NO. 989, 95th Cong., 2nd Sess. 52 (1978).

19. The bankruptcy exemptions allow a debtor to claim exempt up to \$7,500 in real or personal property that is the residence of the debtor or a dependent of the debtor. 11 U.S.C. § 522(d)(1) (1978). The debtor may also claim exempt \$400 in any property (which could result in an additional exemption in the debtor's homestead). 11 U.S.C. § 522(d)(5) (1978). The amount of homestead exemption varies under state laws. California, considered one of the most liberal states in this regard, currently provides for a homestead exemption of \$45,000. CAL. CIV. CODE § 1260 (West 1980).

As of the commencement of a bankruptcy case, the Code gives the trustee the rights of a judicial lien creditor, a creditor holding an execution return unsatisfied,

matic stay of an act against the debtor or his property that is created by the filing of the petition continues until the case is closed or dismissed and the debtor's discharge has been granted or denied.²⁰ However, the discharge itself operates as a permanent injunction against the collection of the debt. If secured creditors wish to foreclose after the debtor's discharge, they still may have to seek relief in the bankruptcy court.²¹

and a bona fide purchaser of real property from the debtor. 11 U.S.C. § 544(a) (1978). The trustee's rights vis-a-vis his various positions are defined by the jurisdiction governing the property in question. *Commercial Credit Co., Inc. v. Davidson*, 112 F.2d 54 (5th Cir. 1940). For example, in California, where a debtor elects the state exemptions and has previously recorded a declaration of homestead, the trustee takes the position of a judgment lien creditor whose lien does not attach to the debtor's homestead. *Engelman v. Gordon*, 82 Cal. App. 3d 174, 146 Cal. Rptr. 835 (1978). This reduces his status to that of a general unsecured creditor whose obligation is dischargeable. Where a declaration of homestead has not been recorded, but the debtor claims the benefits of California's "automatic" homestead provision, CAL. CIV. PROC. CODE § 690.31 (West 1980), the result is different. Since no declaration of homestead has been recorded, the trustee is in the position of a judgment lien creditor whose lien (in the amount of the claims validly due the unsecured creditors), attaches to the residential property subject to prior recorded liens and the debtor's exemption. CAL. CIV. PROC. CODE § 690.31, 674(c) (West 1980). For a more comprehensive discussion of the trustee's rights as a judicial lien creditor, see *In re Carole Jean Martin*, 6 B.R. 827 (C.D. Cal. 1980). *But cf.* *In re Campbell*, 5 B.C.D. 6 (S.D. Cal. 1978) (where no homestead declaration had been recorded at the date of the petition, California Code of Civil Procedure § 690.31 protected debtor's possession only, and title to the property passed to the trustee under § 70a of the Act). In connection with *Campbell*, see note 7 *supra* and accompanying text.

20. 11 U.S.C. § 362(c)(2) (1978).

21. 11 U.S.C. § 524(a)(2) (1978). It has been suggested that secured creditors should attempt to have the debtor reaffirm the debt prior to discharge in accordance with 11 U.S.C. § 524(c) or request relief from the court prior to discharge to avoid the effects of the permanent injunction created upon discharge by 11 U.S.C. § 524(a)(2). Where the loan is not in default prior to discharge, there is a question as to whether cause exists for the bankruptcy court to lift the stay. Can a secured creditor proceed with foreclosure absent default? In light of 11 U.S.C. § 506(d), note 11 *supra*, and § 524(c)(4), it is not clear that reaffirmation of a debt secured by real property is necessary unless one seeks a deficiency. See *In re Coots*, 6 B.C.D. 429 (S.D. Ohio 1980). The *Coots* court suggests that the debtor's personal liability is dischargeable while the secured creditor retains its lien. See also Mapoether, *Bankruptcy Strategies for Representing Creditors in Chapter 7 and Chapter 13 Cases*, 86 COMM. L.J. 133 (1981), where the author suggests that interaction of sections 524(a)(2) and 506(d) prohibits an unsecured creditor from collecting a debt by proceeding against the unencumbered property of the debtor, but that the right of the secured creditor to enforce its lien against the specific property in which it has a security interest is unaffected. *But see* *In re Williams*, 7 B.C.D. 388 (D. Kan. 1981) where the bankruptcy court held that a creditor may not enforce any pre-filing liens against debtors of their property after discharge absent an enforceable reaffirmation agreement.

Section 362(d) of the New Bankruptcy Code sets forth the grounds for relief from the automatic stay:

On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by termination, annulling, modifying, or conditioning such stay—

- (1) *for cause, including* the lack of adequate protection of an interest in property of such party in interest; or
- (2) with respect to a stay of an act against property, if—
 - (A) The debtor does not have an equity in such property; and
 - (B) such property is not necessary to an effective reorganization (emphasis added).²²

The Code does not define “adequate protection.” However, it does propose three non-exclusive methods of providing adequate protection to a creditor with a security interest in the property of the debtor. Section 361(1) suggests that periodic cash payments to the creditor may provide adequate protection to the extent that the automatic stay results in a decrease in the value of the security.²³ Section 361(2)²⁴ proposes an additional or replacement lien as a form of adequate protection to the extent that the stay results in a decrease in the value of the secured creditor’s interests. Section 361(3)²⁵ gives the court the flexibility to formulate adequate protection on a case by case basis by providing such relief as will result in the realization by the creditor of the indubitable equivalent of his interest in the property.²⁶

If the debtor desires to continue the stay, it is his duty to propose to the secured creditor a method of providing adequate pro-

22. 11 U.S.C. § 362(d) (1978).

23. 11 U.S.C. § 361(1) (1978) reads as follows:

When adequate protection is required under Section 362, 363 or 364 of this title of an interest of an entity in property, such adequate protection may be provided by

- (1) requiring the trustee to make periodic cash payments to such entity, to the extent that the stay under section 362 of this title, use, sale, or lease under section 363 of this title, or any grant of a lien under section 364 of this title results in a decrease in the value of such entity’s interest in such property . . .

Id. This concept is derived from *In re Bermec Corp.*, 445 F.2d 367 (2d Cir. 1971) where the secured creditor was adequately protected by payments sufficient to preserve the status quo with respect to the value of the creditor’s interest in the property. *See also* *In re Yale Express System, Inc.*, 384 F.2d 990 (2d Cir. 1967); *In re El Patio, Ltd.*, 6 B.C.D. 1098 (C.D. Cal. 1980).

24. 11 U.S.C. § 361(2) (1978) reads as follows: “(2) providing to such entity an additional or replacement lien to the extent that such stay, use, sale, lease, or grant results in a decrease in the value of such entity’s interest in such property”

25. 11 U.S.C. § 361(3) reads as follows: “(3) granting such other relief, other than entitling such entity to compensation allowable under section 503(b)(1) of this title as an administrative expense, as will result in the realization by such entity of the indubitable equivalent of such entity’s interest in such property.”

26. H.R. REP. NO. 595, 95th Cong., 1st Sess. 338 (1977); *In re Paradise Boat Leasing Corp.*, 5 B.R. 822 (D.C. V.I. 1980).

tection.²⁷ Methods vary, limited only by the ingenuity of the debtor and his attorney. Some bankruptcy courts have held that an equity cushion can itself constitute adequate protection.²⁸ In such cases, it is necessary to determine the amount of the debt owed and the value of the property in order to establish whether an equity cushion exists. In the hypothetical case presented here, the house is valued at \$140,000, and the recorded encumbrances total \$100,000. It would appear that Gamma is protected by an equity cushion of \$40,000, Beta Corporation, the first trust deed holder, is protected by an equity cushion of \$60,000²⁹ and Delta, the judgment creditor, is protected by an equity cushion of \$35,000, if its interest is secured.³⁰ The burden of showing that Alfa lacks equity in the property is on the creditor requesting relief from the stay, and the burden of proof on all other issues is on the party opposing such relief,³¹ usually the trustee and/or the debtor. Absent other factors which cause the lack of adequate protection, such as delinquent taxes, poor property maintenance, and insufficient insurance, Gamma appears to be over-secured and would not be able to have the stay lifted until its equity is eroded.³²

With the filing of a Chapter 11 bankruptcy petition, Alfa becomes a debtor in possession.³³ The purpose of a Chapter 11 peti-

27. 11 U.S.C. § 362(g)(2) (1978). *See also* *In re Lake Tahoe Land Co., Inc.*, 5 B.R. 34 (D. Nev. 1980); *In re Moore*, 5 B.R. 449 (D. Md. 1980); *In re Princess Baking Corp.*, 5 B.R. 587 (S.D. Cal. 1980); *In re San Clemente Estates*, 5 B.R. 605 (S.D. Cal. 1980); *In re Bradley*, 3 B.R. 313 (E.D. Va. 1980).

28. *In re Castle Ranch of Ramona, Inc.*, 5 B.C.D. 1386 (S.D. Cal. 1980); *In re Rogers Development Corp.*, 5 B.C.D. 1392 (E.D. Va. 1980); *In re Pitts*, 2 B.R. 476 (C.D. Cal. 1979). *Cf. In re Lake Tahoe Land Co., Inc.* 5 B.R. 34 (D. Nev. 1980) (adequate protection for a commercial lender is an equity cushion of 40-50% of market value).

29. In the hypothetical situation presented here, Alfa has not defaulted on the first trust deed to Beta Corporation. However, in the event of default, the rights and burdens of the parties are essentially the same as discussed herein with respect to the holder of the second trust deed.

30. The rights and burdens of the judgment creditor under the Code are essentially the same as discussed herein with respect to the holder of the second trust deed. *But cf.* 11 U.S.C. § 522(f)(1). *See also* note 4 *supra*. The rights of judgment creditors to perfect and execute on their liens are governed by varying state laws.

31. 11 U.S.C. § 362(g)(2) (1978).

32. The Code allows a creditor whose claim is over-secured to recover interest and any reasonable fees, costs, and charges provided for in the security agreement. 11 U.S.C. § 506(b) (1978).

33. The rights and duties of a debtor in possession are specified in 11 U.S.C. § 1107 and are substantially similar to those of a trustee.

tion is to provide a distressed debtor with time to formulate a plan to reorganize his affairs and pay his creditors. Ordinarily, a debtor in such a reorganization is a business; however, there is nothing in the Code that precludes an individual from seeking Chapter 11 relief.³⁴

If, prior to the time the debtor formulates a plan of reorganization, Gamma seeks relief from the stay, he still has the burden of showing that Alfa has no equity in his home. But, if, no equity exists, an additional element will be present. In addition to the duty of proposing a method to adequately protect the secured creditor's interest, Alfa may have the burden of proving that his home is necessary to an effective reorganization.³⁵

In the hypothetical facts, the \$40,000 equity cushion protecting Gamma may not be sufficient to allow the stay to remain in effect for the period of a reorganization, particularly if it can be shown that accruing taxes, interest, and fees are rapidly diminishing the cushion.³⁶ In addition, the court must ascertain the reasonable value of the property and whether it will decrease during the pendency of the stay.³⁷ Whether the secured creditor can be adequately protected for the period of the stay and how the protection is to be provided is a matter to be determined on a case by case basis, applying equitable principles where appropriate.³⁸ Where adequate protection is requested and allowed, but subsequently turns out to be inadequate, a priority is granted to the creditor upon distribution of the estate.³⁹

The Code gives a reorganizing debtor the right to alter the rights of secured creditors in a plan of reorganization, even over the objection of that class of creditors.⁴⁰ For example, Alfa could

34. See 11 U.S.C. §§ 109(d), 101(30) (1978).

35. 11 U.S.C. §§ 362(d)(2)(B), 362(g)(2) (1978). In *In re Sulzer*, 2 B.R. 630 (S.D.N.Y. 1980), the bankruptcy court found that the debtor had no equity in his home and it was not necessary to his reorganization. The debtor was a psychiatrist who saw patients in his home as well as in his city office. The court found that in order for the property to be necessary to an effective reorganization, it must be used directly in connection with the debtor's business. The fact that the debtor also used his residence as a place of business was not sufficient, since in order for the debtor to continue to operate, he could make use of any office space, and the use of his home was not essential.

36. See *In re Castle Ranch of Ramona, Inc.*, 5 B.C.D. 1386 (S.D. Cal. 1980).

37. See *In re El Patio Ltd.*, 6 B.C.D. 1098 (C.D. Cal. 1980). In *In re American Kitchen Foods, Inc.*, 2 B.C.D. 715, 722 (D. Me. 1976), the court stated that "the most commercially reasonable disposition practicable in the circumstances should be the standard [of value] universally applicable in all cases and at every phase of each case."

38. See note 26 *supra* and accompany text. See also 11 U.S.C. § 105 (1978); 28 U.S.C. § 1481 (1978); *In re El Patio, Ltd.*, 6 B.C.D. 1098 (C.D. Cal. 1980).

39. 11 U.S.C. § 507(b) (1978).

40. 11 U.S.C. § 1129(b) (1978).

propose that the secured creditors receive the full amount of their secured claims including interest⁴¹ upon the sale of his home at a price of no less than \$165,000. His plan could further provide that he has one year from the date of confirmation within which to consummate the sale, during which time the regular monthly payments will be made. While confirmation of a plan requires the consent of all classes of creditors impaired⁴² under the plan,⁴³ the debtor may "cram down" his plan without their acceptance by a showing that the treatment of the secured creditors is fair and equitable and does not discriminate.⁴⁴

Chapter 13 relief⁴⁵ is available only on a voluntary basis and only to individuals with regular income who owe, on the date the petition is filed, less than \$100,000 in unsecured debts, and less than \$300,000 in secured debts.⁴⁶ Like Chapter 11, Chapter 13 is designed to allow the debtor an opportunity to formulate a plan for the payment of his creditors. The issues and burdens in a request to lift the stay are essentially the same as previously discussed.⁴⁷

Although a Chapter 13 plan may modify the rights of a secured creditor when certain criteria are met,⁴⁸ it may not alter the rights of a creditor who holds a security interest *only* on the debtor's principal residence.⁴⁹ However, Alfa's plan could deal with such a

41. 11 U.S.C. § 506(b) (1978).

42. 11 U.S.C. § 1124 (1978) defines impairment.

43. 11 U.S.C. § 1129(a)(8) (1978).

44. 11 U.S.C. § 1129(b) (1978). For a comprehensive discussion of the standards under § 1129(b) that will permit "cram down," see Klee, *All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code*, 53 AM. BANKR. L.J. 122 (1979).

45. The purpose of this article is to familiarize readers in a general way with the provisions of Chapter 13 that may apply to affect the rights of creditors with secured claims in residential property; it is not intended to be an in-depth study of that, or any other, Chapter.

46. 11 U.S.C. § 109(e) (1978).

47. Chapter 13 provides for the adjustment of debts of an individual with regular income. It would appear that the nature of a Chapter 13 proceeding places the burden on the debtor to show under 11 U.S.C. § 362(d)(2) that his home is necessary to an effective reorganization. See note 35 *supra* and accompanying text. *But see* In re Feimster, 6 B.C.D. 131 (N.D. Ga. 1979) in which the bankruptcy court held that the question of reorganization is only applicable to Chapter 11 cases since the term "reorganization" is absent from the provisions of Chapter 13. *Contra*, In re McAloon, 1 B.R. 766 (E.D. Pa. 1980). The proposed Technical Amendments Bill to the Bankruptcy Reform Act of 1978 provides for the applicability of § 362(d)(2) in Chapter 13 cases.

48. 11 U.S.C. § 1325(a)(5) (1978).

49. 11 U.S.C. § 1322(b)(2) (1978).

creditor by providing that installment payments to cure the default,⁵⁰ as well as the current contract payments, be made through the Chapter 13 trustee.⁵¹

Creditors holding secured claims should be aware that a bankruptcy procedure rule⁵² requires that secured creditors file a proof of claim before the first meeting of creditors in a Chapter 13 case. Untimely claims are not treated as secured claims for purposes of distribution. The new Bankruptcy Code makes the Bankruptcy Rules in existence at the time of its passage applicable to cases filed under the Code to the extent they are not inconsistent with the Code.⁵³ Since it is usually unnecessary for secured creditors to file proofs of claim in Chapter 7 or Chapter 11 proceedings,⁵⁴ this Chapter 13 requirement could be a trap for the unwary. At least one bankruptcy court has held that the Bankruptcy Rule is not inconsistent with the new Chapter 13, and a secured creditor who fails to file a timely claim can retain its lien, but must participate pro rata with unsecured creditors and may not be paid in a preferential manner.⁵⁵

"The best defense is a good offense." That old cliché is sound advice to lenders with secured claims in residential property whose rights may be adjudicated in a bankruptcy court. A general familiarity with those provisions of the Bankruptcy Code affecting their interests will permit swift resort to their rights and remedies.

50. 11 U.S.C. § 1322(b)(5) (1978). The provision for curing a default must be reasonable. *In re Coleman*, 2 B.R. 348, *aff'd*, 5 B.R. 812 (W.D. Ky. 1980).

51. 5 COLLIER ON BANKRUPTCY § 1322.01 (14th ed. 1940).

52. BANKRUPTCY RULE 13-302(e).

53. Pub. L. 95-598, 92 Stat. 2549, (codified at 11 U.S.C. §§ 101(1)-151326 (1978)).

54. Caveat: You may wish to file your fully secured claim if listed as disputed, contested, or contingent, regardless of the Chapter under which the debtor has filed. The prior problems of withholding the filing of a claim for fear of inadvertently conferring jurisdiction on the Bankruptcy Court no longer exist. A major change in the Bankruptcy Code is the granting of expanded and all-encompassing jurisdiction. 28 U.S.C. § 1471 (1978).

55. *In re Price*, 5 B.C.D. 1115 (N.D. Cal. 1979).