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Recent Developments: Nobelman v. American Savings Bank: Debtor Who Files for Bankruptcy under Chapter 13 of the Bankruptcy Code May Not Reduce an Undersecured Homestead Mortgage to the Fair Market Value of the Mortgaged Residence

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premature misjudgment and avoid an otherwise erroneous verdict." *Id.*, (quoting *Herring*, 422 U.S. at 863 (1975)). Additionally, the court of appeals relied on *Spence v. State*, in which it stated that:

[T]he opportunity for summation by defense counsel prior to verdict in a non-jury trial as well as in a jury trial is a basic constitutional right guaranteed by Article 21 of the Maryland Declaration of Rights and the Sixth Amendment to the United States Constitution as applied to the States by the Fourteenth Amendment. *Spence*, 296 Md. 416, 419, 463 A.2d 808, 809 (1983).

The court of appeals therefore held that Holmes had been denied his

constitutional right to present closing argument, noting that the remarks Holmes made at the trial "were certainly not simply allocution in mitigation of punishment" but were his best attempt to argue his case to the judge. *Holmes*, 333 Md. at 657-58, 637 A.2d at 116. Further, the court held that although the trial judge assured Holmes that he would have an opportunity to address the court, that opportunity was not afforded until after the rendering of the verdict. The court found the error was not harmless. *Holmes*, 333 Md. at 659, 637 A.2d at 117.

Because the case was reversed on this ground, it was unnecessary for the court to reach Holmes' second contention, that the trial court

erred in not granting a postponement to allow the defendant to obtain counsel. The court of appeals remanded the case to the trial court for a new trial.

The court's holding in *Holmes* reaffirms its position that *pro se* defendants have a constitutional right to present closing arguments and ensures that they will be granted this opportunity to express their views and make final arguments in their defense *prior* to verdict. Moreover, this case forces judges to honor all defendants their right of allocution that is guaranteed by the United States Constitution and the Maryland Declaration of Rights.

- Erika F. Daneman

Nobelman v. American Savings Bank:

DEBTOR WHO FILES FOR BANKRUPTCY UNDER CHAPTER 13 OF THE BANKRUPTCY CODE MAY NOT REDUCE AN UNDERSECURED HOMESTEAD MORTGAGE TO THE FAIR MARKET VALUE OF THE MORTGAGED RESIDENCE.

In *Nobelman v. American Savings Bank*, 113 S. Ct. 2106 (1993), the United States Supreme Court held that a debtor who files for bankruptcy under Chapter 13 of the Bankruptcy Code may not reduce an undersecured homestead mortgage to the fair market value of the mortgaged residence. Bifurcation of an undersecured homestead mortgagee's claim into secured and unsecured portions impermissibly modifies the rights of the mortgagee. In so holding, the Court resolved a conflict among the courts of appeals in interpreting sections 506(a) and 1322(b)(2).

In 1984, Petitioners Leonard and Harriet Nobelman obtained a loan of \$68,250 from Respondent American Savings Bank for the purchase of a condominium which was to be used as their principal residence. Petitioners executed an

adjustable rate note payable to the bank which was secured by a deed of trust on the residence. By 1990, Petitioners had fallen behind in their mortgage payments, and they sought relief under Chapter 13 of the Bankruptcy Code ("Code"). The bank filed a proof of claim with the Bankruptcy Court for \$71,335, which represented the principal, interest, and fees owed on the note. However, Petitioners' Chapter 13 plan valued the residence at only \$23,500, an amount not disputed by the parties, and proposed to make payments pursuant to the mortgage contract only up to that amount. Petitioners sought to treat the remainder of the claim as unsecured. Creditors with unsecured claims would receive nothing under the plan.

Respondents American Savings Bank and the Chapter 13

trustee objected to the plan. They argued that the proposed bifurcation of the bank's claim into a secured claim for \$23,500 and an effectively worthless unsecured claim for the balance owed violated section 1322(b)(2) of the Code because it modified the bank's rights as a homestead mortgagee. The Bankruptcy Court agreed with respondents and denied confirmation of the plan. The District Court for the Northern District of Texas and the Court of Appeals for the Fifth Circuit affirmed the decision of the Bankruptcy Court. The United States Supreme Court granted certiorari.

The question before the Court was whether section 1322(b)(2) prohibits a Chapter 13 debtor from relying on section 506(a) to reduce an undersecured homestead mortgage to the fair market value of the mortgaged residence. The Court held that it does.

A Chapter 13 debtor may adjust his indebtedness through a flexible repayment plan which must be approved by a bankruptcy court. *Nobelman*, 113 S. Ct. at 2109. Section 1322 lists the elements of a confirmable Chapter 13 plan and provides that a debtor must turn over a portion of his future earnings and income to the trustee for supervised payments to creditors over a period not exceeding five years. Section 1322(b)(2) allows modification of the rights of secured and unsecured creditors. There is, however, an exception for homestead mortgagees. Rights of creditors whose claims are secured only by a lien on the debtor's principal residence may not be modified. Section 1322(b)(2) states, in pertinent part, that the plan may "modify the rights of holders of secured claims, other than a claim secured only by a

security interest in real property that is the debtor's principal residence, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims." *Id.* at 2109 (quoting 11 U.S.C. § 1322(b)(2)) (emphasis omitted).

Petitioners argued that their Chapter 13 plan did not propose a modification of the bank's rights. They maintained that section 1322(b)(2) applies only to the extent the mortgagee holds a "secured claim" in the debtor's residence. *Id.* Section 506(a) provides that an allowed claim secured by a lien on the debtor's property "is a secured claim to the extent of the value of [the] property." *Id.* (quoting 11 U.S.C. § 506(a)). It is an "unsecured claim" to the extent the claim exceeds the value of the property. *Nobelman*, 113 S. Ct. at 2109. Petitioners claimed that section 506(a) allows the downward adjustment of the amount of a lender's undersecured home mortgage before any disposition proposed in a debtor's Chapter 13 plan. Thus, if Petitioners were correct, the bank's loan would have been secured for the value of the collateral, only \$23,500. Petitioners argued that, because the plan proposed to make \$23,500 worth of payments in accordance with the terms of the mortgage contract, the plan did not alter the bank's rights as the holder of a claim. *Id.*

The Court disapproved of this interpretation because it failed to observe the focus of section 1322(b)(2) which is on the rights of creditors. That provision does not state that a plan may modify "claims" but that it may modify "rights." *Id.* at 2109-10. Section 506(a) defined the bank's claim as a secured claim for \$23,500 and an unsecured claim for the bal-

ance. However, that did not mean that the "rights" of the bank as mortgagee, which were protected by section 1322(b)(2), were limited by the valuation of its secured claim. *Id.* at 2110.

Pointing out that the Bankruptcy Code does not define the term "rights," the Court assumed that Congress intended that property rights be determined by state law. Therefore, the mortgage instrument, which was enforceable under state law, reflected the bank's rights. *Id.* The rights addressed in the mortgage included the right to repayment of the principal in monthly installments over a fixed term at specified adjustable rates of interest, the right to retain the lien until the debt is paid off, the right to accelerate the loan upon default and to proceed against Petitioners' residence by foreclosure and public sale, and the right to bring an action to recover any deficiency remaining after foreclosure. These were the rights that section 1322(b)(2) protected. *Id.*

Petitioners next argued that the clause "other than a claim secured only by a security interest in . . . the debtor's principal residence" modifies its immediate antecedent, "secured claims." If this "rule of the last antecedent" applies, only "secured claims," as defined in section 506(a), that are secured by a lien on the debtor's home would be protected. *Id.* at 2111.

Four courts of appeals have applied the rule of the last antecedent and held that section 1322(b)(2) allows such bifurcation and downward adjustment of undersecured homestead mortgages. *Id.* at 2109 n.2 (citing *In re Bellamy*, 962 F.2d 176 (2d Cir. 1992); *In re Hart*, 923 F.2d 1410 (10th Cir. 1991); *Wilson v. Commonwealth Mortgage Corp.*, 895 F.2d 123 (3d Cir. 1990);

In re Hougland, 886 F.2d 1182 (9th Cir. 1989)).

The Court declined to apply the rule of the last antecedent, reasoning that, if Congress had intended that the phrase apply only to "secured claims," it would have used that term of art as it had done throughout the Bankruptcy Code. Instead, Congress used only "claims," intending that the phrase apply to both secured and unsecured claims. *Nobelman*, 113 S. Ct. at 2111. The unqualified word "claim" is broadly defined in section 101(5) as a right that is "secured or unsecured." *Id.* (citing 11 U.S.C. § 101(5)). In addition, section 506(a) uses the phrase "claim . . . secured by a lien" to encompass both the secured and unsecured portions of an undersecured claim. *Nobelman*, 113 S. Ct. at 2111.

The Court further stated that Petitioners' interpretation was implausible and would not have allowed for a discernable administration of section 1322(b)(2). *Id.* Petitioners proposed to reduce the outstanding mortgage principal to the fair market value of the home. They insisted that they could do so without modifying the bank's rights as to the contract terms, including the interest rates and payment amounts. *Id.* Believing this to be impossible, the Court noted that the terms of the contract were contained in a unitary note that applied to the bank's overall claim, which was comprised of a secured and an unsecured portion. It would not have been possible to modify the payment and interest terms for the unsecured portion without also modifying the terms of the secured portion. To preserve the interest rate and the amount of each monthly payment specified in the note after reducing the principal to \$23,500,

the plan would also have to have reduced the terms of the note dramatically, constituting a significant modification of a contractual right. *Id.*

In addition, the bank held an adjustable rate mortgage. This required that the principal and interest payments on the loan be recalculated with each adjustment in the interest rate. Neither the contract nor the Code suggested a basis for recalculating the amortization schedule. Therefore, the Court concluded the interpretation proposed by petitioners was inoperable. *Id.*

In *Nobelman v. American Savings Bank*, the United States Supreme Court held that a debtor who files for bankruptcy under Chapter 13 of the Bankruptcy Code may not reduce an undersecured home-
stead mortgage to the fair market

value of the mortgaged residence. Although section 506(a) allows bifurcation of undersecured claims through a Chapter 13 plan, section 1322(b)(2) prohibits the modification of the rights of a holder of a security interest where the claim is secured only by a lien on the debtor's principal residence. Bifurcation of an undersecured home-
stead mortgage, which would result in such a modification, is therefore prohibited. The rights of the mortgagee are not limited by the valuation of its secured claim but instead by the relevant mortgage instrument which is enforceable under state law. In so holding, the Court resolved a conflict among the courts of appeals and standardized the application of sections 506(a) and 1322(b)(2).

- Maria Ellena Carey

