NEW YORK LAW SCHOOL

NYLS Law Review

Volume 37 | Issue 1 Article 51

January 1992

Post-Foreclosure Statutory Right of Redemption Under Chapter 13 of the Bankruptcy Code: A Balance of State and Federal Interests

Gary A. Saunders

POST-FORECLOSURE STATUTORY RIGHT OF REDEMPTION UNDER CHAPTER 13 OF THE BANKRUPTCY CODE: A BALANCE OF STATE AND FEDERAL INTERESTS

I. INTRODUCTION

This note addresses the narrow issue of whether a state statutory right of redemption in favor of a mortgagor or junior lien holder survives the filing of a petition under Chapter 13 of Title 11, United States Code (the Bankruptcy Code).[1] The circuits that have addressed the role of the statutory right of redemption under the Bankruptcy Code have had difficulty giving the proper weight to the state property interest vis-a-vis the right to cure mortgage defaults under the Bankruptcy Code.

This note demonstrates that the statutory right of redemption[2] establishes the debtor's initial property interest, which, following a petition under Chapter 13 of the Bankruptcy Code, becomes property of the bankrupt estate.[3] Under Chapter 13, the debtor has a right to cure any default in real property that is the debtor's principal residence.[4] As long as the debtor retains an interest in the principal residence properly created under state law at the time of the petition for protection under Chapter 13, the debtor may cure the default and reinstate the mortgage. Although the initial interest in the property must be determined by state law,[5] state mortgage law cannot limit the scope of the federal right to cure unless that cure power is expressly limited under federal law. Therefore, the cure

---

1. 11 U.S.C. §§ 1301-1330 (1988).

2. *See infra* text accompanying notes 18-21.

3. *See* 11 U.S.C. § 541 (1988). Section 541 broadly sweeps all debtor property interests into the estate, encompassing "all legal or equitable interests of the debtor in property as of the commencement of the case." *Id.* § 541(a)(1); *see also id.* § 1306 (incorporating § 541 directly, and further expanding its reach); *In re* Thompson, 894 F.2d 1227, 1229 (10th Cir. 1990) ("[A] mortgage debtor must have some legal or equitable interest in property which enters the bankruptcy estate if he hopes to retain it through the bankruptcy cure provisions."); *In re* Ivory, 32 B.R. 788, 791 (Bankr. D. Or. 1983) ("[I]t is clear that a debtor retains an interest in the property until the statutory redemption period has run and legal title has passed.").

4. 11 U.S.C. § 1322(b)(2), (b)(5).

5. "State law" refers to the property laws of the individual states as opposed to federal law encompassed in the Bankruptcy Code, including the right to cure arrearages in the debtor's principal residence available under the Code. *See generally* Butner v. United States, 440 U.S. 48 (1975) (holding that the Bankruptcy Code leaves the determination of property rights in assets to state law).

right under § 1322(b)(5) of the Bankruptcy Code should be applied to the post-foreclosure statutory right of redemption as well as any other state-created property right. This interpretation is supported by the broad language of § 1322(b)(5),[6] the policy underlying Chapter 13,[7] and the lack of support in the legislative history evidencing Congress's intent to limit the right to cure at any point along the default and foreclosure process.[8]

The state statutory right of redemption creates a property interest in favor of the defaulting homeowner, that is, the right to redeem the homestead following foreclosure and sale.[9] A federal right providing "for the curing of any default" under § 1322(b)(5) of the Bankruptcy Code comes into existence following a voluntary, involuntary, or joint filing.[10] A collision of the state-based property rights with the constitutionally mandated federal bankruptcy powers[11] provides a classic example of how the bankruptcy and circuit courts address a fundamental interaction between traditional state and federal rights. Once the interest in the debtor's principal residence is established under state law and has been filed under the Bankruptcy Code, that interest comes into the estate and is capable of "cure" as provided in the Bankruptcy Code.[12] State mortgage and foreclosure laws that attempt to limit that right must fail.

Part II of this note is an amalgam of fact patterns in Chapter 13 cases on this issue, exemplifying the typical dilemma faced by the unwary homeowner. Part III.A reviews the state property law relative to mortgages and foreclosures. Part III.B reviews the applicable Bankruptcy Code provisions. Part III.C compares the operation of both spheres. Part IV reviews the approaches taken in recent court decisions to extinguish the state-based right of redemption.

---

6. *See infra* text accompanying notes 34-40, 58.

7. *See infra* part III.B.

8. *See infra* text accompanying notes 40-42, 60.

9. *See infra* notes 18-23 and accompanying text.

10. 11 U.S.C. § 301 (voluntary filings); *id.* § 302 (joint filings); *id.* § 303 (involuntary filings).

11. U.S. CONST. art. I, § 8, cl. 4 ("The Congress shall have Power . . . [t]o establish . . . uniform Laws on the subject of Bankruptcies throughout the United States . . . .").

12. *See* 11 U.S.C. § 541 (defining property of the estate); *id.* § 1306 (defining property of the estate).

II. A HOMEOWNER'S HOBSON'S CHOICE

The Paytons purchased a home, obtaining a loan and a mortgage from the local bank. When the house burned down, the Paytons, unable to continue timely payments due to additional living expenses and the confusion following the loss of their home, subsequently defaulted on the mortgage. During negotiations with the insurance company, which took longer than they had anticipated, the house was sold at the foreclosure auction. The mortgagee was the only bidder and purchased the home for the value of its mortgage.

The Paytons, with no place to live, met with an attorney who advised them to file a petition under Chapter 13 of the Bankruptcy Code. The state in which their former home is located has a one-year statutory right of redemption, and the attorney explained that this state statute provided a legal right to redeem, or buy back, their home within one year following the sale. The attorney then filed a reorganization plan, which provided for payment in full of all arrearages and reinstatement of the original mortgage payments. The insurance company meanwhile settled the claim, and the forthcoming proceeds were to fund the plan.

Should the bankruptcy court approve the plan and allow the Paytons to rebuild their house, or has the sale "cut off" the state right to redeem once protection under the federal scheme has been invoked?

III. THE BASIC FRAMEWORK

A. *State Law*

State procedures for the treatment of the homeowner following default and leading up to foreclosure sale are lengthy and are not uniform in all states.[13] Common points along the spectrum are the event of default,

---

13. A typical action in equity to foreclose and sell involves a long series of steps: a preliminary title search to determine all parties in interest; filing of the foreclosure bill of complaint and lis pendens notice; service of process; a hearing, usually by a master in chancery who then reports to the court; the decree or judgment; notice of sale; actual sale and the issuance of certificate of sale; report of the sale; proceedings for determination of the right to any surplus; possible redemptions from foreclosure sale; and the entry of a decree for a deficiency.

Douglas A. Winthrop, Note, *The Chapter 13 Cure Provisions: A Doctrine in Need of a Cure*, 74 MINN. L. REV. 921, 922 n.9 (1990) (citation omitted).

acceleration of the obligation under the note accompanying the mortgage, state court foreclosure judgment, and foreclosure sale.[14]

Under the real-property law of all states, a mortgagor is entitled to exercise an "equitable right of redemption" following default on a mortgage of real property.[15] This redemption right is the "mortgagor's right after *default* in every jurisdiction, title, lien or intermediate, to perform his obligation under the mortgage and have the title to his property restored free and clear of the mortgage."[16] Notwithstanding contrary language in the mortgage documents, the mortgagor and junior encumbrancers have an implied right to redeem the property prior to foreclosure.[17]

Foreclosure was the point established at common law to cut off or "foreclose" the mortgagor's equity of redemption.[18] Due to the potential abuses and hardship to mortgagors faced with a forced sale and potentially large deficiency judgments, a majority of states have provided a "statutory right of redemption."[19] The purpose of this state-created right is to allow the mortgagor and junior lienors, in order of seniority, to redeem the property *following the foreclosure sale* for a specified period of time at the sale price plus costs and interest.[20]

The statutory right to redeem can extend up to two years.[21] This homeowners' right is meant to encourage bidding at the foreclosure sale[22] and discourage sharp practices, such as rigged bidding,[23] because

---

14. *See id.* at 921-22.

15. GRANT S. NELSON & DALE A. WHITMAN, REAL ESTATE FINANCE LAW § 7.1, at 478 (2d ed. 1985 & Supp. 1989).

16. *Id.* (emphasis added).

17. *See id.* at 478-79.

18. Robert K. Lifton, *Real Estate in Trouble: Lender's Remedies Need an Overhaul*, 31 BUS. LAW. 1927, 1936 (1976).

19. *Id.* at 1938-39; *see also* NELSON & WHITMAN, *supra* note 15, § 7.1, at 479 (providing a brief description of statutory redemption).

20. *See* Lifton, *supra* note 18, at 1938-39.

21. ALLAN AXELROD ET AL., LAND TRANSFER AND FINANCE 296 (3d ed. 1986 & Supp. 1991).

22. Lifton, *supra* note 18, at 1939 ("These statutes are intended as a threat to force the mortgagee and other potential bidders to bid the full value of the property on the foreclosure sale in order to preclude the owner from later seeking to redeem the property at the below-market sales price.").

23. Also referred to as "chilled" bidding, this practice involves locking up potential bidders to allow a below-market foreclosure sale to conclude. *See generally* Manoog v. Miele, 213 N.E.2d 917 (Mass. 1966) (allowing a mortgagee to contract with a potential buyer before the sale at a fixed price). The *Manoog* court noted that a "knowledgeable

unusually low purchase prices would encourage mortgagors to exercise their rights and redeem their property. There is considerable debate concerning the effectiveness of the statutory right of redemption.[24]

Even in a state providing a post-foreclosure sale redemption right, defaulting homeowners may be unable to redeem due to the requirement that the foreclosure sale price plus expenses must be paid in full at redemption.[25] A homeowner most likely would have redeemed during the equitable period if refinancing was possible or additional funds were forthcoming. The function of the statutory right, as opposed to the equitable right to redeem, may be limited to its ability to encourage bidding because it is a rare turn of events that brings sufficient money to a foreclosed debtor to repay the mortgage debt plus costs. One type of situation in which the statutory right may be used for its redemption value is when insurance proceeds are forthcoming, but not soon enough to forestall a foreclosure sale.

An alternative to redemption under state law is filing a petition under Chapter 13 of the Bankruptcy Code, under which the accelerated defaulted mortgage can be decelerated, reinstated, and the arrearage "cured."[26]

B. *Federal Law*

The Bankruptcy Code[27] permits a debtor to stay creditor activity and allows the bankruptcy court to collect into the estate all property in which the debtor holds an equitable or legal title.[28] The Bankruptcy Code promotes creditor equality by permitting consensual plans of reorganization, but insures that dissenting classes of creditors are treated

---

mortgagee should not be allowed to assume a position such that he preempts the field of bidders and discourages other potential bidders at a sale." *Id.* at 920. The court focused on the unavailability of similar financing, which permitted the bidder to expect a better price than the price at auction from the eventual buyer. *Id.*

24. *Compare* United States v. Stadium Apartments, Inc., 425 F.2d 358, 365 (9th Cir. 1970) (majority "not convinced" that statutory right of redemption accomplishes purpose of forcing full market price at sale) *with* United States v. Ellis, 714 F.2d 953, 956 (9th Cir. 1983) ("Statutory rights of redemption give the mortgagor power to force the sale price closer to true market value.").

25. AXELROD ET AL., *supra* note 21, at 297; NELSON & WHITMAN, *supra* note 15, § 7.3, at 481-83.

26. *See generally* 11 U.S.C. §§ 1301-1330 (describing methods of adjusting debts of a person with a regular income); *infra* notes 27-42 and accompanying text (describing relief under the "cure" provisions in § 1322(b)(5)).

27. 11 U.S.C. §§ 101-1330 (1988).

28. *See generally id.* § 362 (providing an automatic stay upon filing); *id.* § 541 (collecting all legal or equitable interests of the debtor into the estate).

fairly and equitably—avoiding a rush to the state courthouse to obtain and collect judgments.[29] The Bankruptcy Code establishes a collective proceeding by which debtor rehabilitation can be balanced with the best interests of all the creditors.[30]

Chapter 13 of the Bankruptcy Code provides relief to wage earners who qualify under § 109(e).[31] The primary beneficiaries of Chapter 13 are homeowners who would be able to retain ownership of their principal residence under a plan of reorganization.[32]

> The benefit to the debtor of developing a plan of repayment under chapter 13, rather than opting for liquidation under chapter 7, is that it permits the debtor to protect his assets. In a liquidation case, the debtor must surrender his nonexempt assets for liquidation and sale by the trustee. Under chapter 13, the debtor may retain his property by agreeing to repay his creditors.[33]

Section 1322(b)(5) allows qualifying debtors to cure defaults on long-term debt, such as mortgage debt.[34]

Under Bankruptcy Code § 1322(b)(2), the reorganization plan may modify a secured claim,[35] but not one that is secured by real property

---

29. *See, e.g., id.* § 362 (noting that at the filing of a bankruptcy petition, an automatic stay against creditor activity comes into effect); *id.* § 1129(b)(1) (requiring that a debtor using the "cramdown" provision against a creditor must propose a plan that, among other things, does "not discriminate unfairly, and is fair and equitable").

30. *See, e.g., id.* § 1325(a)(4) (stating that the value of the property distributed under the plan cannot be less than the amount paid under a Chapter 7 liquidation); *see also id.* § 1129(a)(7) (describing the "best interests of the creditors" test for confirmation of a Chapter 11 plan).

31. "Only an individual with regular income that owes, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts of less than $100,000 and noncontingent, liquidated, secured debts of less than $350,000, or an individual with regular income . . . ." *Id.* § 109(e).

32. "Section 1322(b)(5) is concerned with relatively long term debt, such as a security interest or mortgage debt on the residence of the debtor . . . its most common use by far is to cure defaults on residential mortgages." 5 COLLIER ON BANKRUPTCY ¶ 1322.09[1] (Lawrence P. King ed., 15th ed. 1993).

33. H.R. REP. No. 595, 95th Cong., 1st Sess. 118 (1977), *reprinted in* 1978 U.S.C.C.A.N., 5787, 6079. An individual may also file under Chapter 11. *See* Toibb v. Radloff, 111 S. Ct. 2197, 2202 (1991).

34. 5 COLLIER ON BANKRUPTCY, *supra* note 32, ¶ 1322.09[1].

35. A "claim" is broadly defined as any "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured or unsecured." 11 U.S.C.

that is the debtor's principal residence.[36] The lender's secured interest is protected against unconsented modification, protecting mortgagees and consequently the mortgage market.[37] Nevertheless, a claim secured by the debtor's principal residence may be "cured" under § 1322(b)(5).[38]

Section 1322(b)(5) provides for the "*curing of any default* within a reasonable time and maintenance of payments while the case is pending on any unsecured claims or secured claim on which the last payment is due after the date on which the final payment under the plan is due."[39]

The timing of the cure was not addressed in the Congressional Record discussing the "cure" provisions in § 1322(b)(5).[40] "Our problem is that we have little help from the words of the statute or its legislative history, so we must try to reconcile the policies of section 1322(b) and state mortgage foreclosure law."[41] Indeed, congressional silence as to the point after which the timing cure can no longer be applied, whether after the

---

§ 101(5)(A). A secured claim arises as the result of a perfected security interest or agreement or judicial lien. A security interest is defined under the Code as a "lien created by agreement." *Id.* § 101(45).

36. Section 1322(b)(2) of the Bankruptcy Code states:

> (b) Subject to subsection (a) and (c) of this section, the plan may . . .
> (2) 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. § 1322(b)(2).

37. Undersecured claims may be bifurcated, and the unsecured portion modified. *Id.* § 506(a). *See, e.g.*, Wilson v. Commonwealth Mortgage Corp., 895 F.2d 123 (3d Cir. 1990) (agreeing with the Ninth Circuit to allow bifurcation of unsecured claims); *In re* Hougland, 886 F.2d 1182 (9th Cir. 1989) (holding that a creditor's rights under unsecured claims could be modified after bifurcation). The Bankruptcy Court in *In re* Richards, 151 B.R. 8 (Bankr. D. Mass., 1993), held that Chapter 13 debtors may use § 506 to bifurcate home mortgages and "strip down" the undersecured portion. *See id.* at 12; *see also In re* Bellamy, 962 F.2d 176 (2d Cir. 1992) (holding that Chapter 13 debtor could bifurcate creditor's claim when claim was secured solely by interest in debtor's principal residence under § 506(a)). *But see* Dewsnup v. Timm, 112 S. Ct. 773 (1992) (holding that Chapter 7 debtor could not "strip down" lien under § 506(d)).

38. Bankruptcy Code § 1322(b)(5) begins with "notwithstanding paragraph (2) of this subsection." 11 U.S.C. § 1322(b)(5).

39. *Id.* (emphasis added).

40. *See In re* Glenn, 760 F.2d 1428, 1432 (6th Cir. 1985) ("The legislative history of section 1322(b) is ambiguous about the scope of the right afforded the debtor to cure a mortgage default."); Winthrop, *supra* note 13, at 928 ("Unfortunately, neither the Commission nor the Congress addressed the relationship between the cure provisions of section 1322(b)(5) and the various stages of foreclosure.").

41. *In re* Thompson, 894 F.2d 1227, 1230 (10th Cir. 1990).

event of default, acceleration, judgment, or foreclosure, is the source of the confusion in the bankruptcy and appellate-level courts.[42]

C. *Conflict or Accommodation*

While the Bankruptcy Code governs the ordering of rights to, and disposition of, property of the estate, a basic premise pervades the interaction between state and federal law: absent a conflict between state property and federal bankruptcy law, state law governs questions of property rights.[43]

> Property rights are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding. Uniform treatment of property interests by both State and federal courts within a state serves to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving "a windfall merely by reason of the happenstance of bankruptcy."[44]

The *Thompson* court noted that no court has asserted that the debtor retains an interest in the property following the foreclosure sale if the state does not provide a statutory right of redemption.[45] But, if the state does provide a period of time following sale to exercise a redemption right, the bankruptcy courts are directed to allow the "curing of any default" under § 1322(b)(5). When the debtor retains a property interest under state law that is not expressly divested by statute, legislative history, or overriding federal policy, the mandate of the Bankruptcy Code seems clear.

Nevertheless, courts have disallowed the right to cure following foreclosure sale. Two basic lines of reasoning are followed. First, courts acknowledge that there is no conflict, otherwise federal law would prevail.[46] If federal law applies, then the right to cure would trump the state requirement of full payment.[47] In the absence of a conflict, the right

---

42. *See generally id.* at 1228 (reviewing various approaches in each jurisdiction and concluding that beyond the point of acceleration "there is little agreement between the circuits on when the right to cure ends").

43. Butner v. United States, 440 U.S. 48, 55 (1979).

44. Johnson v. First Nat'l Bank, 719 F.2d 270, 274 (8th Cir. 1983) (quoting Butner v. United States, 440 U.S. 48, 55 (1979) (citation omitted)), *cert. denied*, 465 U.S. 1012 (1984).

45. *In re Thompson*, 894 F.2d at 1229.

46. *See Butner*, 440 U.S. at 55-56.

47. *Id.* at 54.

to redeem under state law may be exercised, but the mortgagee may not benefit from the federal "cure" right.[48] Although these courts preserve the *Butner*[49] rule that property interests are defined by state law in the absence of a conflict with a federal interest,[50] the courts do not allow a debtor to "cure" during a state redemption period.[51] Second, the courts use state property law definitions to work a change in the mortgagor–mortgagee relationship following the sale, which defines away and extinguishes the ability to "cure" any "default."[52] These approaches will be discussed seriatim in recent cases.

IV. RECENT CASES ADDRESSING THE RIGHT TO CURE PREPETITION FORECLOSURE SALES UNDER § 1322(B)(5)

Due to congressional silence, the Sixth Circuit in 1985 recognized the difficulty in determining when a debtor is entitled to "cure" under § 1322 in *In re Glenn*.[53] The case consolidated three debtor petitions and dealt with "the point in the foreclosure process at which a Chapter 13 debtor loses the right to cure a default on a real estate mortgage on his principal residence."[54] In the second case of the trilogy, Ralph Miller filed a petition after the sale of the property but prior to the expiration of the statutory redemption period.[55] The District Court for the Eastern District of Michigan reversed the bankruptcy court decision and permitted Miller to set aside the foreclosure sale, pay the arrearage, and reinstate the mortgage.[56] The Sixth Circuit reversed, holding that the right to cure a default ceases upon sale of the property.[57]

The Sixth Circuit reviewed five positions held by courts in the various circuits that had addressed the timing of mortgage cure.[58] The relevant

---

48. *See infra* text accompanying notes 154-78.

49. *Butner*, 440 U.S. at 48.

50. *See supra* notes 43-44 and accompanying text.

51. *Id.*

52. *See infra* text accompanying notes 67-69, 71, 81-83, 104-07.

53. 760 F.2d 1428, 1432 (6th Cir. 1985).

54. *Id.* at 1429.

55. *Id.* at 1430-31.

56. *Id.* at 1431.

57. *See id.* at 1442.

58. *See id.* at 1432. The five categories are:

(1) courts that hold that a debtor may not cure a default once a mortgage debt has been accelerated[;] (2) courts that hold that a debtor may cure a default where the mortgage debt has been accelerated provided that no foreclosure judgment has been entered[;] (3) courts [that] hold that a debtor may cure a

points along the default spectrum were acceleration, foreclosure judgment, sale, and expiration of state redemption rights.[59] Judge Engel concluded that, in the absence of congressional direction with respect to acceleration, judgment, or sale, "the statute itself provides no clear cut-off point except that which the courts may see fit to *create*."[60]

Judge Engel used this as a springboard from which to formulate a balancing of equities between lenders and borrowers.[61] By finding license to "create" the foreclosure sale as the clear cut-off, the court readily admitted that "we avoid any effort to analyze the transaction in terms of state property law."[62] The court ignored the basic premise that state law governs in the absence of a federal mandate, preferring to sidestep the labyrinth of title, lien, or merger doctrines that applying state law required.[63]

In a recent bankruptcy case in the First Circuit, *In re Tucker*,[64] the court relied on *Glenn* to provide a debtor with the power to cure following foreclosure judgment.[65] The case involved a petition following foreclosure judgment but prior to sale in Maine, which allows a ninety-day period of redemption.[66] The bank relied on the argument that the state merger law reduced the mortgage and note to a judgment, which left the debtor nothing to cure.[67]

Judge Goodman in *Tucker* agreed with the *Glenn* analysis, without remark, but went further: "While a state law is certainly relevant, it simply dictates what property rights and interests a debtor holds. Despite the doctrine of merger, state law still provides the debtor sufficient property rights in order to confer upon this court the jurisdiction to determine the bankruptcy issue regarding those rights."[68]

---

default where a state court judgment of foreclosure has been entered provided that no sale has taken place[;] (4) courts that place no express limitation on the debtor's right to cure a default after acceleration [; and] (5) courts that hold that a debtor may cure a default where a foreclosure sale has been held provided that the debtor's right of redemption under state law has not expired.

Id. (citations omitted).

59. *See id.*

60. *Id.* at 1435 (emphasis added).

61. *See id.*

62. *Id.* at 1436.

63. *See id.*

64. 131 B.R. 245 (Bankr. D. Me. 1991).

65. *See id.* at 245.

66. *See id.*

67. *See id.*

68. *Id.*

In reviewing the *Tucker* reasoning, it is clear that if state law indeed "dictates" property rights, as *Tucker* states, it follows that a debtor with a statutory redemption right has state-based property rights. In the case of a statutory right of redemption, the theory that this right is eliminated at judgment and merger negates the very existence of the right. It is a mere tautology to grant a post-foreclosure right that is merged out of existence at judgment. Rather, the mortgagor's property interest is left intact if the state provides a grace period after a sale in which the property can be redeemed.

With this property right as the starting point, the debtor filing a Chapter 13 petition has some "legal or equitable interest" in which to apply the "cure" power.[69] In the states that do not have a statutory right of redemption, no state-defined property interests exist after the foreclosure sale, and the Bankruptcy Code does not recreate interests that have expired or did not exist at filing.[70] This approach attempts to eliminate the property interest itself by redefining it out of existence after filing. But if the state right exists before filing, it is a valid property interest upon which the Bankruptcy Code may operate.

Judge Goodman's position in *Tucker* recognized the primacy of the Code's right to cure, yet found that it did not apply under the state's merger law.[71] He supported his position by misusing the often-quoted language from *In re Taddeo*[72] to support the statement that a Chapter 13 debtor has a right to cure controlled by the Bankruptcy Code, not state law: "We do not believe that Congress labored for five years over this controversial question only to remit consumer debtors—intended to be the primary beneficiaries of the new code—to the harsher mercies of state law."[73]

The *Taddeo* court was concerned with the effect of disallowing deceleration by the use of an acceleration clause in a mortgage agreement under Chapter 13.[74] If lenders were able to include an acceleration clause in a note that could *ipso facto* defeat the benefits of a Chapter 13 filing, debtors would as a matter of course be subject to standard acceleration

---

69. The broad sweep of § 541 brings in all "legal and equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541. Also, § 1306 expressly incorporates § 541, and brings § 1322 to bear upon a default on a debtor interest in her principal residence. *See id.* § 1306.

70. *See In re* Thompson, 894 F.2d 1227, 1229 (10th Cir. 1990) ("No court has held that debtors can use the bankruptcy cure provisions to recover property in which they no longer have any interest under state law.").

71. *In re Tucker*, 131 B.R. at 245.

72. 685 F.2d 24 (2d Cir. 1985).

73. *In re Tucker*, 131 B.R. at 245.

74. *In re Taddeo*, 685 F.2d at 28.

clauses.[75] Such a holding would indeed leave debtors to the "harsher mercies" of state law, without the "cure" remedy made available by Congress under the Bankruptcy Code.[76] If state law dictates property rights and interests, and the Bankruptcy Code controls the right to cure, it is a simple syllogism to preserve a state statutory right to redeem to allow a "cure" under the Bankruptcy Code. This avoids the harsh effect of losing the homestead that is capable of cure under the Bankruptcy Code.

In effect, the Third and Eighth Circuits applied state definitions of mortgage and judgment[77] and discovered that state law can be applied to defeat a federal entitlement that, in the absence of a bankruptcy petition, would have been a state-law entitlement.[78]

The Eighth Circuit decided a Chapter 12 petition in *Justice v. Valley National Bank*[79] by construing the post-foreclosure sale right to cure under § 1322.[80] The principal rationale applied to remove the right to cure from the debtor was that the foreclosure sale extinguished the mortgage contract and worked a substantial change in the relationship of the parties under state law.[81] "The restriction in § 1322(b)(2) refers to claims 'secured only by a security interest,' but in this case the foreclosure judgment and sale extinguished Prudential's security interest."[82] The court then focused on what would be a modification of a state court

---

75. *See id.*

76. *See In re* Roach, 824 F.2d 1370, 1377 (3d Cir. 1987) ("Given the availability and prevalence of automatic acceleration clauses, if section 1322(b)(5) is found to be available only before acceleration, it will be virtually meaningless in the home mortgage context."); *see also In re* Thompson, 894 F.2d 1227, 1232 (10th Cir. 1990) (Badlock, J., concurring in judgment only) ("[A]ny application of state law is impermissible where such law conflicts with a federal statute, its legislative history, or an underlying federal interest.").

77. *See, e.g.*, Justice v. Valley Nat'l Bank, 849 F.2d 1078 (8th Cir. 1988). The court gently disagreed with the *Glenn* court's solution to the timing problem, finding that "in light of our analysis of the state and federal interests implicated in this area, we believe that Congress' silence is better interpreted as evidence of its intent to leave state law undisturbed." *Id.* at 1088 n.10.

78. *See infra* notes 79-126 and accompanying text.

79. 849 F.2d 1078 (8th Cir. 1988).

80. *Id.* at 1081-83. Unlike § 1222(b)(2), § 1322(b)(2) prohibits modification of the rights of a holder of a claim secured only by a security interest in real property that serves as the principal residence of the debtor. *See* 11 U.S.C. § 1322. "Nor can we ignore the fact that the relevant provisions of section[ ] 1222(b) . . . (5) [is] identical to those found in section 1322." *Justice*, 849 F.2d at 1086.

81. *Justice*, 849 F.2d at 1085.

82. *Id.* at 1083.

judgment and found no support for the proposition that Congress had intended this result.[83]

The search for this congressional support became the strawman. "Nothing in the language or history of subsection (2) or its predecessors suggests that Congress intended the provision to be used for that purpose . . . . Moreover, where Congress elsewhere intended bankruptcy courts to intrude in state judicial proceedings, it explicitly directed them to do so, using unambiguous language."[84]

The search was fruitless, however, because Congress was not concerned with state mortgage and foreclosure regulations. Using the court's logic, if Congress meant to limit the right, Congress would have unambiguously determined a point in the state court procedures after which the right to cure would no longer exist.

The court acknowledged the general principle that state laws are suspended only to the extent of actual conflict with the federal bankruptcy system.[85] The court also acknowledged that when no conflict exists, unless some federal interest requires a different result, the law of the state where the property is situated governs property rights.[86] The court did not find any actual conflict between § 1222 and a South Dakota law that required an override of the state redemption laws.[87] Applying the state law, the court, following *Roach*, determined that "cure" and "default" refer to contractual relationships and that under South Dakota law the contractual relationship ends when the property is sold to a third party.[88]

The *Justice* court briefly addressed the preemption argument that the Bankruptcy Code establishes a federal common law covering the "right to cure."[89] The court, however, was unwilling to decide that issue: "We need not decide today whether the right to cure under § 1222(b)(3), (b)(5) is a federal right, because we are satisfied that even if it is, state law should be adopted in these circumstances as the federal rule of decision."[90]

The dissent in *Justice* provided the common-sense response to this hypertechnical reading of *Butner*—that the application of state law would require the debtor to modify impermissibly a state court judgment

---

83. *See id.*

84. *Id.*

85. *See id.* at 1087.

86. *Id.*

87. *See id.* at 1088.

88. *See id.* at 1087.

89. *Id.*

90. *Id.*

following sale.[91] Judge Heaney recognized that state court judgments must yield to a right granted under the Bankruptcy Code.[92] "Yet, to the extent the judgment conflicts with specific rights granted the debtor under the Bankruptcy Code, contrary provisions of the state court judgment must give way."[93]

The property rights under state law are sacred only to the extent of their creation, but not to their full application.[94] If a right exists under state law, the Bankruptcy Code often modifies the state right, unless expressly preserved under federal law.[95] Because a judgment is a state-created right, the modification of a foreclosure judgment is not denied under the Bankruptcy Code but is merely preserved following petition for possible modification.[96]

Judge Heaney also rejected the majority's definitions of "cure" and "default" as presupposing a contractual relationship. Again, he used common sense:

> Yet, the language of section 1222(b)(5) does not limit the right to cure to those debts arising out of an existing contractual relationship. One would think that if Congress had been aware of such an important distinction, it would have clearly expressed its intention to limit the debtor's right to cure a default to a time before acceleration, judgment, or sale. It did not. I see no reason for the Court to impose a limitation on the right to cure that is not supposed by the broad language of section 1222(b)(5).[97]

The same analysis applies to § 1322(b)(5) with equal force.

---

91. *Id.* at 1088-89 (Heaney, J., dissenting).

92. *See id.* at 1089.

93. *Id.*

94. The basic premise expressed in *Butner* is that state law creates and defines the property interest held by the debtor, and that state laws are suspended only to the extent of an actual conflict with the bankruptcy provisions. *See* Butner v. United States, 440 U.S. 48, 54 (1979). Referring to the Bankruptcy Act, the Court held that certain provisions invalidate interests as fraudulent or preferences, but "Congress has generally left the determination of property rights in the assets of a bankrupt's estate to state law." *Id.* The Code should not provide more to a debtor as far as substantive property interests than the debtor otherwise has outside of the protection of the bankruptcy court. *See id.* at 55.

95. *See, e.g.*, 11 U.S.C. § 1322(b)(2) (1988).

96. *Justice*, 849 F.2d at 1089 (Heaney, J., dissenting) ("Much of the Bankruptcy Code involves modification of state created property rights. Such modifications are not prohibited merely because the rights involved are embodied in a state court judgment.").

97. *Id.* at 1090.

One purpose behind Chapter 13 is to benefit homeowners.[98] This purpose is furthered by a broad reading of § 1322(b)(5)—"[t]he plan may . . . provide for the curing of any default,"—not the tortured interpretation of contract-based state remedies neither addressed by Congress nor the language of § 1322(b)(5).[99]

In *In re Roach*,[100] the Third Circuit faced a Chapter 13 filing after the sale but prior to the expiration of the state statutory period.[101] The *Roach* court flatly disagreed with the *Glenn* cutoff designation.[102] Judge Stapleton focused on the importance of state sovereignty, citing *Butner* for the principle that "the basic federal rule is that state law governs."[103]

The court followed New Jersey law, holding that the right to cure terminates once a foreclosure judgment is entered.[104] Under state law, the mortgage merges into the judgment and ceases to exist, and no mortgage exists at petition to be cured under the Bankruptcy Code.[105] After the entry of a foreclosure judgment, "no contractual relationship remains."[106] The court concluded that "beyond that point in the foreclosure process there are no substantial federal interests that would justify ignoring property interests created by the judgment of a New Jersey Court."[107]

Judge Stapleton acknowledged in small measure that the purposes of Chapter 13 are not furthered by this pro-lender stance.[108] The termination of the right of cure at the entry of foreclosure judgment, however, "does not *significantly threaten* the interests that Chapter 13 was designed to protect."[109]

Although the *Glenn* court created substantive law based on equity by ignoring state law,[110] the *Roach* court slavishly adhered to state law,

---

98. *See supra* text accompanying notes 31-34.

99. *See supra* text accompanying notes 35-39.

100. 824 F.2d 1370 (3d Cir. 1987).

101. *See id.* at 1371.

102. *Id.* at 1373 ("[Our] conclusion conflicts with the position of the Sixth Circuit that the right to cure defaults on residential property in every state survives until a foreclosure sale is held.").

103. *Id.* at 1374.

104. *See id.* at 1379.

105. *See id.*

106. *Id.* at 1377.

107. *Id.*

108. *See id.* at 1378.

109. *Id.* (emphasis added).

110. *See supra* text accompanying notes 53-63.

as did the Seventh Circuit in *In re Clark*.[111] By redefining the relationships held by the parties under state law, these courts were able to circumvent the application of the federal right to cure "any default."[112] Neither the *Roach* nor *Glenn* courts balanced state and federal entitlements. These courts, at each end of the spectrum, deny the federal right to cure to parties holding a valid state-law redemption right.[113]

Recently, the Third Circuit in *First National Fidelity Corp. v. Perry*,[114] continued its strict reading of the right to cure any default.[115] The court held that the Bankruptcy Code does not preempt a New Jersey creditor's state-law right to immediate payment of the foreclosure judgment following default.[116] The court reaffirmed *Roach*:

> Since the change which the Roaches' plan sought to make in the rights of their home mortgage lender was not a "cure" within the meaning of section 1322(b)(5) and since section 1322(b)(2) prohibited any material alteration in the rights of such a lender other than those affected in a "cure," we found no federal authorization for preempting the state rights created upon the entry of the foreclosure judgment.[117]

The focus in the Third Circuit is creditor protection. The logic that extinguished the "mortgage" and replaced it with the "judgment"—a noncurable entity—runs into difficulty when the use of the "judgment" comes into collision with the definition of "security interest."[118] Under § 1322(b)(2), secured claims can be modified, other than a claim secured "by a *security interest* in real property that is the debtor's principal residence."[119] The court seems to be contending that a debtor's mortgage

---

111. 738 F.2d 869 (7th Cir. 1984) (finding that transfer of title determines cutoff point for the right to cure under § 1322(b)(5)).

112. *See infra* notes 190-93.

113. *In re Roach*, 824 F.2d at 1373 ("[Section] 1322(b) must be read in the context of state law and that its right to cure a default on a mortgage on a home located in New Jersey terminates upon entry of foreclosure judgment."); *In re Glenn*, 760 F.2d at 1436 ("[I]n construing this federal statute, we think it unnecessary to justify our construction by holding that the sale 'extinguishes' or 'satisfies' the mortgage of the lien, or that the mortgage is somehow 'merged' in the judgment or in the deed of sale under state law.").

114. 945 F.2d 61 (3d Cir. 1991).

115. *See id.*

116. *See id.* at 62.

117. *Id.* at 63.

118. *See id.* at 64, 66.

119. 11 U.S.C. § 1322(b)(2) (emphasis added).

is extinguished at judgment, but the lender's security interest survives judgment to prevent modification. "We hold that a New Jersey home mortgage lender retains a security interest for the purpose of § 1322(b)(2) following the entry of foreclosure judgment."[120]

The *Perry* court recognized the reality that foreclosure is "an inherent part of the mortgagor-mortgagee relationship" when upholding the lender's interest.[121] But, the court did not allow modification of a judgment because the court is "confident that Congress must have had this fact in mind when it sought to provide special assurance to home mortgage lenders that their expectations would not be frustrated."[122]

Because the judgment has been entered, the debtors in New Jersey cannot be restored to predefault status under the right to cure.[123] Lenders' prepetition security interests are protected against modification after entry of judgment, but debtors' prepetition rights of redemption are not, leaving them without the remedy that Chapter 13 was designed to provide them—to cure any default.[124]

The *Perry* court recognized the mortgagor-mortgagee relationship even after that relationship was reduced to judgment, in the context of a secured creditor's right to full and immediate payment.[125] The court did not acknowledge, though, the reality of the ongoing mortgagor-mortgagee relationship for the purpose of recognizing the debtor's continuing interest in the property to reinstate her predefault status.[126]

In another recent case, the Bankruptcy Appellate Panel in the Ninth Circuit ruled that a prepetition foreclosure sale cannot be cured.[127] *In re Braker*[128] disapproved of the well-reasoned minority position by the District of Oregon Bankruptcy Court in *In re Ivory*.[129]

In *Ivory*, the lender, the Department of Veterans Affairs, opposed a cure in the debtor's plan that consisted of a lump-sum payment from

---

120. *Perry*, 945 F.2d at 61. *But see In re* Ivory, 32 B.R. 788 (Bankr. D. Or. 1983) ("To be consistent with the intent of Congress to provide special protection to home mortgages, a foreclosure judgment should retain the character of a 'security interest' or lien created by an agreement and therefor [sic] not a lien which could be modified under 1322(b)(2).").

121. *Perry*, 945 F.2d at 64.

122. *Id.*

123. *See id.* at 65.

124. *See id.* at 64.

125. *See id.* at 67.

126. *See id.*

127. *See In re* Braker, 125 B.R. 798 (Bankr. 9th Cir. 1991).

128. *Id.*

129. 32 B.R. 788 (Bankr. D. Or. 1983).

insurance proceeds (upon confirmation) and monthly payments for the life of the plan.[130] The case presented the issue whether a Chapter 13 debtor can cure a default after a final decree of foreclosure and sale.[131]

Ivory was a case of first impression for the District of Oregon Bankruptcy Court.[132] The court reviewed the five positions relative to the timing of mortgage cure in the various jurisdictions, which the *Glenn* court reproduced in its decision.[133] Judge Hess provided perhaps the best and simplest analysis of the prepetition sale, reviewing the state statute for when legal title passes and applying Bankruptcy Code § 541 to determine if the debtor retains any interest after the sale.[134]

Under Oregon law, the purchaser at a foreclosure sale receives a certificate of sale, evidencing a right to possession.[135] Legal title passes to the purchaser after the one-year statutory right of redemption has expired and a sheriff's deed is delivered.[136] The debtor, therefore, retains an interest in the sold property until the statutory redemption period runs out.[137] By applying the broad reach of Bankruptcy Code § 541, the right of redemption becomes property of the estate.[138]

Section 541,[139] in the absence of any express limitation on § 1322(b)(5)'s right to "cure any default," provides a compelling rationale for the *Ivory* court's holding. Judge Hess made a simple and logical conclusion: "The fact that the debtor still retains an interest in the sold property gives them the right to effect a cure under 11 U.S.C. 1322(b)(5)."[140] This approach involves no judicial creation of rights through equity and no judicial legislating.

The court did not follow the line of cases that deems the entry of a foreclosure judgment under state law a merger and extinguishment of the

---

130. *See id.* at 789.

131. *Id.*

132. *Id.*

133. *See id.* at 790; *supra* text accompanying notes 58-59.

134. *See In re Ivory*, 32 B.R. at 791.

135. *See id.*

136. *See id.*

137. *See id.*

138. *See id.* ("[T]he debtor's right of redemption became property of the estate at the time of the debtor's filing.").

139. Section 541 reads: "The commencement of a case . . . creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held: (a) . . . all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541.

140. *In re Ivory*, 32 B.R. at 791.

mortgage, leaving nothing for the debtor to cure.[141] Judge Hess determined that state laws that would limit the right to cure did not affect § 1332(b)(5), finding that "the Bankruptcy Code establishes its own redemption design in lieu of state laws."[142] As long as the debtor retains an interest that becomes property of the estate, the Bankruptcy Code provides certain rights to the debtor, including the right to cure.[143]

In contrast to the pro-lender position of the Third Circuit, which found that lenders have state-law rights to full payment unaffected by the Bankruptcy Code, lenders in *Ivory* got the appropriate treatment intended under the Bankruptcy Code: *adequate protection.*[144] Relying on *In re Thompson*[145] the court found that Congress, under the Bankruptcy Act, did not intend to alter prior case law that determined that "a secured creditor was not entitled to all rights afforded him under contract terms or state law, but rather need only have his secured position protected while the reorganization proceeded."[146] In addition, § 1322(b)(5) does not contain any limitations in its expansive language—"the curing of *any* default"[147]—or in the legislative history. "If Congress had intended to limit cure to preacceleration, prejudgment or presale defaults, it could have done so. It did not."[148] Again, the underlying purpose of Chapter 13 does not compel a strict reading.[149] Section 1322(b)(5) places a special emphasis on the preservation of the homestead; a strict reading runs counter to this goal.[150]

---

141. *See id.* at 790-92. The court used the analysis starting with property of the estate under section 541. *See id.* at 791

142. *Id.* at 791; *see also* 5 COLLIER ON BANKRUPTCY, *supra* note 32, ¶ 1322.09[2] (describing the scope of the Code's reach as to long-term debts the debtor is unwilling or unable to pay during the terms of the plan).

143. *See In re Ivory*, 32 B.R. at 792 ("Had Congress intended state laws limiting cure to apply, section 1322(b) would have been unnecessary.").

144. *See* 11 U.S.C. § 362(d)(1) (allowing a party in interest to make a motion to lift the automatic stay in order to obtain possession of the security if the party is not provided adequate protection of his or her interest in the security); *id.* § 361 (1988) (prescribing three methods by which secured lenders can be provided adequate protection, including granting the indubitable equivalent of his or her interest in the security).

145. 17 B.R. 748 (Bankr. W.D. Mich. 1982).

146. *In re Ivory*, 32 B.R. at 791-92 (quoting *In re Thompson*, 17 B.R. at 752).

147. 11 U.S.C. § 1322(b)(5) (emphasis added).

148. *In re Ivory*, 32 B.R. at 792.

149. *See id.*

150. *See id.*

In the absence of a clear federal mandate regarding timing, state law governs the creation and interest in property.[151] The operation of the state mortgage and foreclosure laws, though, has been used by the Third and Eighth Circuits to limit the scope of the federal right to cure under § 1322(b)(5).[152] Is this a conflict, or were limitations on the right to cure implicitly built into § 1322(b)(5), although the language of that section does not contain any express limitations? Do the courts require authorization to apply federal law in the absence of express limitations or to apply state law when the Bankruptcy Code is silent?[153] The question becomes: Is there a real conflict when state law limits the scope of the federal cure power, which is not expressly limited?

The most satisfactory response is that silence does not mean that limitations on the right to cure exist. There are numerous examples in which the Bankruptcy Code allows non-bankruptcy law to apply.[154] If the language or legislative record reveals no intention to limit bankruptcy powers, and underlying bankruptcy policy favors a broad application, Congress must have intended the right to cure to apply when a state-based property interest properly comes under the jurisdiction of the bankruptcy court.[155] In this way, a proper balance between state-created property interests and the federal intervention is struck with that interest embodied in the "cure" right.

The *Ivory* court's holding that all the steps following default until the final divestment of the debtor's interest may be cured under § 1322(b)(5) was effectively overruled by the Appellate Panel of the Ninth Circuit in the 1991 decision *In re Braker*.[156] The court held that a prepetition foreclosure sale prevented the application of § 1322(b)(5) to cure the default.[157] The Department of Veterans Affairs was again the lender. Following default, a decree of foreclosure and writ of execution were

---

151. *See supra* notes 43-44.

152. *See supra* notes 79-126 and accompanying text.

153. *See In re Ivory*, 32 B.R. at 792 ("These courts reason that express authority is required to negate the application of state law and void state court judgments.").

154. *See, e.g.*, 11 U.S.C. § 522(b) (allowing states to opt out of federal exemption scheme); *id.* § 544(b) (allowing a trustee to use state fraudulent-conveyance statute under the strong-arm power).

155. This is a deduction based on the discussion in *Ivory* and throughout this paper. *See In re Ivory*, 32 B.R. at 788.

156. 125 B.R. 798 (Bankr. 9th Cir. 1991). For a recent analysis of *Braker* and of the Ninth Circuit's interpretation of § 1322(b)(3) and (5) see *In re Hurt*, 158 B.R. 154, 158-60 (Bankr. 9th Cir. 1993) (holding that the right to cure under § 1322(b)(5) is cutoff at the foreclosure sale).

157. *See id.* at 801.

issued.[158] Two days after the Braker property was sold, the Chapter 13 petition was filed.[159] The plan was confirmed allowing a cure through and during the life of the plan.[160] The lower court relied on the *Ivory* decision.[161]

Judge Ollason, in the first paragraph of the short opinion, acknowledged § 541 of the Bankruptcy Code, stating that the 180-day Oregon statutory period for redemption is either a legal or equitable right held by the debtor.[162] The court also recognized the *Ivory* distinction that state laws that limit the federal right to cure must yield to the Bankruptcy Code.[163] Without distinguishing *Ivory*, the court disapproved of it and proceeded to cite the line of cases that rely on state real-property procedure law.[164] The court declined to adopt the § 541 reasoning, which applies the right to cure under § 1322(b)(5) to the debtor's statutory interest in the sold property.[165] Instead, the court adopted state law *in toto*, arguing that an Oregon decree of foreclosure extinguishes the mortgage contract, and played the state-law definitional game.[166] "To have a cure, there must be a default, and to have a default, there must be a contract."[167] By adopting state law, the court limited the scope of the right to cure, which is in direct conflict with the language of § 1322(b)(5).

---

158. *Id.* at 799.

159. *Id.*

160. *See id.*

161. *Id.*

162. *See id.*

163. *See id.* at 800.

164. *See id.*; *see also In re* Mann Farms, Inc., 917 F.2d 1210 (9th Cir. 1990) (stating the right of the debtor, trustee, or other estate representative to pursue, retain, or enforce any cause of action at the time the petition was filed); Justice v. Valley Nat'l Bank, 849 F.2d 1078 (8th Cir. 1988) (stating that sections of Chapter 12 do not authorize the extension of state redemption periods); *In re* Roach, 824 F.2d 1370 (3d Cir. 1987) (upholding state-law time limits of debtor's right to cure home mortgage default); *In re* Tynan, 773 F.2d 177 (7th Cir. 1985) (stating that the automatic stay provisions of the Bankruptcy Code do not toll the running of state statutory redemption periods); *In re* Glenn, 760 F.2d 1428 (6th Cir.), *cert. denied*, 474 U.S. 849 (1985) (holding that foreclosure sale extinguishes debtor's right to cure default and reinstate mortgage, and that automatic stay provisions of the Bankruptcy Code do not toll or extend running of state statutory periods of redemption after a foreclosure sale).

165. *See In re Braker*, 125 B.R. at 801.

166. *See id.* at 800-01 ("The circuit courts concluded that the curing of a default under 11 U.S.C. section 1322(b)(5) requires an existing contractual relationship.").

167. *Id.* at 801.

The Bankruptcy Code cannot create an interest that has expired under state law prior to a bankruptcy petition.[168] The *Braker* court's reliance on *In re Seidel*,[169] therefore, was inapposite because the case dealt with a prepetition matured debt in the absence of an acceleration clause.[170] The statutory period in *Braker* had not yet expired.[171] No circuit has argued yet for a post-sale cure when the state does not provide a statutory right of redemption.[172]

By ignoring the reality of the continuing mortgagor-mortgagee relationship, and by ignoring its own opening paragraph focusing on the legal interest of the debtor in the property under § 541, the *Braker* court determined that allowing a postsale cure would "create new rights for the debtors while taking vested rights from the DVA [Department of Veterans Affairs]."[173] The focus became skewed. Is the court taking away property rights from the creditor or from the debtor?

The court acknowledged a prepetition § 541 legal or equitable interest in the property in the debtor.[174] The court also acknowledged that the § 1322(b)(5) right to cure gives the parties "the equivalent of their state law rights."[175] Oregon law gives the debtor 180 days to redeem the property following sale.[176] The Bankruptcy Code allows the debtor to cure "any default" in the home mortgage.[177] The Oregon statute allows the debtor to redeem after the foreclosure decree, yet the Appellate Panel interpreted the Bankruptcy Code as not allowing the debtor to take that redemption power and apply the § 1322(b)(5) right to cure to it.[178] In state court, redemption privileges are provided, but in bankruptcy court, the redemption cure is denied. This result should not be.

---

168. This runs counter to the express limitation in § 541, bringing into the estate all "legal and equitable" interests of the debtor, but not ones after which a legal or equitable interest in the debtor has expired prior to the petition. *See* 11 U.S.C. § 541.

169. 752 F.2d 1382 (9th Cir. 1985).

170. *See In re Braker*, 125 B.R. at 801.

171. *See id.* at 799.

172. *See In re* Thompson, 894 F.2d 1227, 1229 (10th Cir. 1990) ("No Court has held that debtors can use the bankruptcy cure provisions to recover property in which they no longer have any interest under state law.").

173. *See In re Braker*, 125 B.R. at 801.

174. *See id.* at 799.

175. *Id.* at 801.

176. *Id.* at 800.

177. 11 U.S.C. § 1322(b)(5).

178. *See In re Braker*, 125 B.R. at 801.

Judge Ollason explained that under Oregon law, redemption cannot revive the mortgage, but can only pay the debt.[179] The debtor can pay the debt in full and keep the home, but cannot keep the mortgage in place. The new relationships following this decree are that "the DVA has a judgment arising from a judicial mortgage foreclosure, and debtors have a claim against the DVA based on their statutory redemption rights."[180] So, application of state law, without a conflict with the federal right to cure, leaves the debtor with only the right to pay in full.

But the analysis must be pushed further. Indeed, under state law, the presale equitable right of redemption allows the debtor to pay the amount *in full* to salvage the homestead.[181] Established bankruptcy practice recognizes that, as an alternative to losing their homes due to financial insolvency, qualifying debtors may file a petition for protection under Chapter 13.[182] The all-important § 1322(b)(5) right to cure "any default" allows the homeowner to reverse the default-and-foreclosure process, in effect, keeping the mortgage on foot.[183] Section 1322(b)(5) gives the power to the debtor to decelerate, reinstate, and keep the mortgagor–mortgagee relationship in place, state law notwithstanding.[184] Yet, the court explained that, after sale, the state-law principle of merger trumps the mortgagor–mortgagee relationship and cure right, and makes revival of the mortgage impossible.[185]

Although the debtor retains the right to regain possession of the property, the court would prefer to make that right incurable and essentially impossible to exercise.[186] Certainly, if the estate were capable of paying the full amount, there would be no need for an estate in the first place and no need for a Chapter 13 filing to save the homestead, which, under this interpretation, could not be cured and saved anyway.[187] As

---

179. *See id.*

180. *Id.*

181. NELSON & WHITMAN, *supra* note 15, at 478.

182. *See supra* part III.B.

183. *See id.*

184. *See id*; *see also* David J. Oliveiri, Annotation, *Right of Debtor to "De-Acceleration" of Residential Mortgage Indebtedness Under Chapter 13 of Bankruptcy Code of 1978 (11 U.S.C.S. § 1332(b))*, 67 A.L.R. FED. 217 (1984 & Supp. 1989).

185. *See In re Braker*, 125 B.R. at 801.

186. *See id.*

187. The homeowner-debtor defaults on her loan payments and the home is foreclosed and sold at auction. The statutory right of redemption under state law allows her to regain possession, but at the cost of the principal amount of debt plus costs, a substantial amount of money considering the homeowner-debtor was unable to continue timely payments on the debt. *See* AXELROD ET AL., *supra* note 21, at 297. By

the *Taddeo* court recognized, requiring the debtor to pay the amount in full, as provided by state law, leaves the debtor with a severely limited right to cure.[188] There is no legislative or policy support for the *Braker* court's tortured interpretation.[189]

In the Tenth Circuit case, *In re Thompson*,[190] Judge Logan properly recognized that delimiting the § 1322(b) right to cure, which has no express time limitation, "determines the deadline by which debtors must file a bankruptcy petition in order to avail themselves of the bankruptcy cure provisions."[191] One must ask whether a deadline of such importance would have not been specified by Congress had it thought to establish one in derogation of state law.

Judge Logan wrestled with the problem left by the *Roach*, *Clark*, and *Justice* courts. These courts, among others[192] characterized by Logan as "state law" courts, were unable to interpret and apply state mortgage and foreclosure law and the right to cure in a consistent manner.[193]

---

interpreting § 1322(b)(5) as leaving undisturbed the operation of the state right to redeem, but without the federal right to cure, the scope of the state right effectively wipes out the debtor's ability to reorganize and clearly impinges on the Bankruptcy Code's sphere of operation. So, it is a strange interpretation that preserves the *Butner* recognition of the scope of state property interests, but to the extent that the right to cure is effectively emasculated. This is another way of arguing that there is no conflict between the two spheres—state and federal. There is no conflict only if the Bankruptcy Code right to cure is interpreted out of existence by using state-based definitions and regulations, such as judgment and merger. *See supra* text accompanying notes 67-69, 71, 81-83, 104-07.

188. *See In re* Taddeo, 685 F.2d 24, 29 (2d Cir. 1982) ("[B]ecause she can accelerate her mortgage under state law, the Taddeos can cure only as provided by state law. This interpretation of § 1322(b) would leave the debtor with fewer rights under the new Bankruptcy Code than under the old Bankruptcy Act of 1898.").

189. *See supra* notes 32-42 and accompanying text.

190. 894 F.2d 1227 (10th Cir. 1990).

191. *Id.* at 1228.

192. *See, e.g.*, *In re* Schnupp, 64 B.R. 763 (Bankr. N.D. Ill. 1986) (title passes at end of statutory redemption period); *In re* Tynan, 773 F.2d 177 (7th Cir. 1985) (title passes at date of foreclosure judgment).

193. *In re Thompson*, 894 F.2d at 1229 ("The courts that purport merely to apply state law have themselves had difficulty fitting state mortgage and foreclosure concepts to the bankruptcy power to cure."). The *Thompson* court reviewed the "state court" inconsistencies. *See id.* First, it described how *In re* Roach, 824 F.2d 1370 (3d Cir. 1987), ended the right to cure at judgment even though the mortgagee possessed independent rights by virtue of its judgment. *See In re Thompson*, 894 F.2d at 1229. Second, it described how *In re* Clark, 738 F.2d 869 (7th Cir. 1984), allowed cure following judgment because title did not pass until foreclosure sale. *See In re Thompson*, 894 F.2d at 1229. Finally, it described how Justice v. Valley Nat'l Bank, 849 F.2d 1078

As in the *Ivory* decision, the proper approach, applied by the *Thompson* court following a bankruptcy petition, began with the concept of property of the estate under Bankruptcy Code § 541.[194] "The Bankruptcy Code . . . settled on an expanded concept encompassing any interest under state law, legal or equitable."[195]

Judge Logan was concerned by the introduction of a third party into the mortgagor–mortgagee relationship—the good faith purchaser.[196] "We hesitate to further cloud the interests and expectations of a third-party purchaser through an expansive right of bankruptcy cure."[197] The purpose of the statutory right of redemption, ostensibly, is to bring a fair price at sale, while the equitable right of redemption provides additional time to secure new financing.[198] Based on these factors, the *Thompson* court determined that the foreclosure sale was the point at which to end the right to cure in bankruptcy.[199]

Nevertheless, Judge Logan distinguished *Thompson* on its facts and effectively ruled that beyond equitable considerations of third-party purchasers, statutory rights in the debtor are curable.[200]

> We do not have before us and do not now decide whether the right to cure should continue during a state's extended statutory redemption period when the mortgagee purchases at the foreclosure sale. Often the mortgagee will purchase the property by bidding in the amount of the mortgage debt. In such a case, the mortgagor–mortgagee relationship is essentially unchanged by the foreclosure sale, and an argument can be made that the *right of bankruptcy cure should last until the end of any statutory redemption period state law would allow.*[201]

(8th Cir. 1988), did not allow postsale cure because it interpreted a Congressional intent not to allow cure once the mortgage contract was ended. *See In re Thompson*, 894 F.2d at 1229. The *Thompson* court concluded that "it is often hard to determine exactly which state law event these courts consider to be controlling." *Id.*

194. *See In re Thompson*, 894 F.2d at 1229.

195. *Id.*; *see also* 4 COLLIER ON BANKRUPTCY, *supra* note 32, ¶ 541.02[1] (outlining "the substantial departure under the Code from the extensive reliance of the Bankruptcy Act on nonbankruptcy law . . . to determine what property will come into the estate").

196. *See In re Thompson*, 894 F.2d at 1230.

197. *Id.*

198. *See supra* note 23 and accompanying text.

199. *See In re Thompson*, 894 F.2d at 1230.

200. *See id.*

201. *Id.* at 1230 n.6 (emphasis partially added) (citation omitted).

The concurrence in the *Thompson* case highlighted the majority's acknowledgment that the statute's language and legislative history did not put a time limitation on the exercise of the right to cure and that the court was acting on the basis of equitable consideration.[202] The concurrence had considerable difficulty with the circuitous reasoning of previous courts that have slavishly applied mind-bending state mortgage laws but blinded themselves to a simple application of the right to cure.[203] "Oddly enough, the court is willing to discuss the mortgage redemption laws of the fifty states to justify its result, but declines to address the problem of whether the right to cure should continue during a state's statutory redemption period when the . . . mortgagor–mortgagee relationship is essentially unchanged."[204]

In the serial petition case, *In re Saylors,*[205] the Eleventh Circuit addressed the parties' respective rights to the petitioner's home.[206] Foreshadowing how the Court would rule in the prepetition sale case, Judge Vance recognized that "[t]he Alabama statutory right of redemption is a property right of the debtor within the jurisdiction of the bankruptcy court."[207] Two years later, in April 1991, the Bankruptcy Court for the Southern District of Alabama was presented with this precise situation in *In re Dickerson.*[208] The Federal National Mortgage Association (Fannie Mae) foreclosed on a mortgage at public auction, followed four days later by a Chapter 13 filing.[209] The *Dickerson* court relied on *Saylors* to find that the statutory right of redemption brought the disputed property into the bankruptcy estate.[210] Without elaboration, the court read § 1322(b) as allowing the debtor to propose a plan that may cure any default.[211] The definition of "cure," based on the Second Circuit *Taddeo* decision, allowed deceleration and reinstatement of the payment schedule.[212]

What appears to be a simple analysis for many bankruptcy courts, but more involved at the appellate and circuit level, will be a matter of first impression for the Eleventh Circuit when it faces this issue. Based on the

---

202. *See id.* at 1231 (Baldock, J., concurring).

203. *See id.* at 1232-33.

204. *Id.* at 1233.

205. 869 F.2d 1434 (11th Cir. 1989).

206. *See id.* at 1435.

207. *Id.* at 1437.

208. 130 B.R. 110 (Bankr. S.D. Ala. 1991).

209. *Id.* at 111-12.

210. *See id.* at 112 (citing *In re Saylors*, 869 F.2d at 1437).

211. *See id.*

212. *See id.*

Saylors analysis, it is likely the court will recognize that a debtor's state court right to redeem, when brought under the Bankruptcy Code, is curable.

V. CONCLUSION

State property law determines the interests held by the debtor in property at the time of the filing of a bankruptcy petition.[213] Once the bankruptcy court obtains jurisdiction, the Bankruptcy Code provides certain rights to the debtor, among them, the right to cure any default under § 1322(b)(5).[214] In a majority of states, the statutory right of redemption is a property right, which debtors retain following the foreclosure sale of their property.[215] This interest in their property becomes part of the bankruptcy estate under § 541 and is therefore eligible for the cure right under Chapter 13.[216]

The courts cited in this note recognize the importance of applying state property law in bankruptcy.[217] But instead of using state law to determine the inception and creation of the interest in property, state law is applied *in toto*. By doing so, state law limits the scope of the federal right to cure, which has no explicit point after which the right may not be exercised. Once the state merger and foreclosure law impinges on the Bankruptcy Code's right to cure, the Bankruptcy Code must prevail.[218] In addition, by allowing the redemption right to survive, but not allowing the right to cure to apply, the courts use state-based definitions to limit the application of the cure right that Congress did not intend to limit.[219] Again, state law is used to limit the scope of the cure right and is therefore impermissible.

The statutory right of redemption should be given the same weight as preforeclosure sale property rights and the debtor given the full scope of the Bankruptcy Code right to cure any default and reinstate the mortgage to predefault status.

Gary A. Saunders

---

213. *See supra* text accompanying notes 43-45.

214. *See supra* text accompanying notes 32-39.

215. *See supra* text accompanying note 19.

216. *See supra* text accompanying notes 138-39.

217. *See supra* part IV.

218. *See* U.S. CONST. art. VI, cl. 2; *id.* art. I, § 8, cl. 4.

219. *See, e.g., In re* Ivory, 32 B.R. 788, 792 (Bankr. D. Or. 1983) ("Had Congress intended state laws limiting cure to apply, § 1322(b) would have been unnecessary.").