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Modification of an Undersecured Home Mortgage in a Chapter 13 Proceeding

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Modification of an Undersecured Home Mortgage in a Chapter 13 Proceeding

Hougland v. Lomas & Nettleton Co. (In re Hougland)[1]

In *Hougland v. Lomas & Nettleton Co. (In re Hougland)*,[2] the Ninth Circuit Court of Appeals held that 11 U.S.C. section 1322(b)(2),[3] which provides for modification of the rights of holders of secured claims other than a claim secured only by a debtor's principal residence, did not protect the unsecured portion of an undersecured claim in the residence from modification pursuant to 11 U.S.C. sections 506(a) and (d).[4] In so holding, it was the first circuit court to address the interplay between section 1322(b)(2) and section 506 of the Bankruptcy Code.

Since *Hougland*, both the Third Circuit and the Tenth Circuit Courts of Appeal have addressed the issue and reached the same result.[5] While no

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1. 886 F.2d 1182 (9th Cir. 1989) [hereinafter *Hougland II*].
2. *Id.*
3. 11 U.S.C. § 1322(b)(2) (1988) provides:

> (b) Subject to subsections (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.

4. *Hougland II*, 886 F.2d at 1184. 11 U.S.C. § 506(d) (1988) provides in pertinent part: "(d) To the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void . . . ." *Id.*
11 U.S.C. § 506(a) (1988) provides in pertinent part:

> An allowed claim of a creditor secured by a lien on property in which the estate has an interest . . . is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property . . . and is an unsecured claim to the extent that the value of such creditor's interest . . . is less than the amount of such allowed claim . . . .

Id.

5. *See* Eastland Mortgage Co. v. Hart (*In re* Hart), 923 F.2d 1410 (10th Cir. 1991) (an undersecured mortgage is protected by section 1322 (b)(2) only to the extent of the secured claim, and bifurcation is a recognition of the legal status of creditor's interest and not a modification of the mortgage); Wilson v. Commonwealth Mortgage Corp., 895 F.2d 123 (3d Cir. 1990) (section 1322(b)(2) does not preclude the modification of any unsecured portion of an undersecured claim in a debtor's principal residence.).

other circuit courts have ruled on this issue, district courts and bankruptcy courts from other circuits reflect a split of authority.[6] Courts in the Second, Fourth, Sixth, and Seventh Circuits have followed *Hougland*,[7] while bankruptcy courts in the First, Fifth, Eighth, and Eleventh Circuits have held that such bifurcation is inappropriate.[8]

This Note will explain and analyze the theory used in *Hougland* and the theories used by other courts addressing the issue, and will then conclude that the *Hougland* court's result is fair, logical, and should be adopted by all courts.

I. FACTS AND HOLDING

In January 1983, Estel and Ruth Hougland ("Debtors") obtained a loan from The Lomas & Nettleton Company ("L & N").[9] The parties executed a promissory note and a deed of trust secured solely by Debtors' principal residence.[10] Debtors fell behind on their payments and L & N commenced foreclosure proceedings.[11] Debtors filed a petition for relief under Chapter 13 of the Bankruptcy Code, thereby staying the foreclosure action.[12] At the time the bankruptcy petition was filed, the value of Debtors' property was approximately $47,000, and the outstanding loan balance was approximately $51,000.[13]

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6. *Hart*, 923 F.2d at 1414.

7. *See In re* Frost, 123 Bankr. 254 (S.D. Ohio 1990); *In re* Harris, 94 Bankr. 832 (D.N.J. 1989); *In re* Bellamy, 122 Bankr. 856 (Bankr. D. Conn. 1991); *In re* McNair, 115 Bankr. 520, 523 (Bankr. E.D. Va. 1990); *In re* Demoff, 109 Bankr. 902, 915 (Bankr. N.D. Ind. 1989).

8. *Hart*, 923 F.2d at 1414 (citing *In re* Chavez, 117 Bankr. 733, 736-37 (Bankr. S.D. Fla. 1990); *In re* Sauber, 115 Bankr. 197, 199 (Bankr. D. Minn. 1990); *In re* Schum, 112 Bankr. 159, 162 (Bankr. N.D. Tex. 1990); *In re* Kaczmarczyk, 107 Bankr. 200, 202-03 (Bankr. D. Neb. 1989); *In re* Russell, 93 Bankr. 703, 705 (D.N.D. 1988)). *See also In re* Mitchell, Nos. 90-11369, 90-11289 (Bankr. D.N.H. Feb. 13, 1991) (WESTLAW, FBKR-CS database).

9. *Hougland II*, 886 F.2d at 1182 (9th Cir. 1984).

10. *Id.*

11. *In re* Hougland, 93 Bankr. 718, 719 (D. Or. 1988) [hereinafter *Hougland I*].

12. *Id.*

13. *Hougland II*, 886 F.2d at 1182-83. The Debtors' loan was obtained under an Oregon program for veterans of the United States Armed Forces permitting negative amortization for a period of time before the principal decreases. *Id.* at 1182. At the time of filing, the value of the property was $47,240 while the outstanding balance of the debt was $51,090, including arrearages, interest, foreclosure fees, and late fees. *Hougland I*, 93 Bankr. at 719.

Debtors' plan sought to avoid the unsecured portion of L & N's lien[14] pursuant to 11 U.S.C. section 506(d).[15] L & N objected to the plan as violative of 11 U.S.C. section 1322(b)(5), which allows the modification of the rights of holders of secured claims, other than a claim secured only by a security interest in a debtors' principal residence.[16] L & N contended that the plan impermissibly modified L & N's rights as a creditor holding a debt secured only by a security interest in Debtors' principal residence.[17] The bankruptcy court denied confirmation of the plan and denied Debtors' motion for reconsideration.[18] Debtors then appealed the bankruptcy court's decision to the United States District Court of Oregon.[19]

On appeal, Debtors argued that section 1322(b)(2) only afforded protection to the fully secured portion of L & N's claim.[20] They contended that the plan did not impermissibly modify the secured portion of L & N's claim; rather, it avoided only the portion of L & N's claim defined as unsecured by 11 U.S.C. section 506(a).[21] Debtors further argued that section 506(a) and section 1322(b)(2) were not in conflict and could be read together.[22]

L & N again argued that avoidance of a portion of its claim, through the operation of section 506(d), was an impermissible modification of its rights as a creditor under section 1322(b)(2).[23] L & N contended that the more specific provisions of section 1322, which apply only to cases under Chapter 13, should prevail over the general provisions of section 506, which apply to cases under Chapters 7, 11, 12 and 13.[24]

The district court noted there were three groups of cases analyzing the interplay between these two sections.[25] The first group of cases held that section 1322(b)(2) did not protect the unsecured portion of undersecured junior mortgages.[26] The court stated, however, that those cases provided

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14. The unsecured portion was the difference between the amount of the claim, $51,090, and the value of the property, $47,240. *Hougland I*, 93 Bankr. at 719.

15. *Id.* *See supra* note 4 and accompanying text.

16. *Hougland I*, 93 Bankr. at 719. *See supra* note 3 and accompanying text.

17. *Hougland I*, 93 Bankr. at 719.

18. *Id.* at 720.

19. *Id.*

20. *Id.* at 721.

21. *Id.* *See supra* note 4 and accompanying text.

22. *Hougland I*, 93 Bankr. at 721.

23. *Id.*

24. *Id.*

25. *Id.*

26. *Id.* (citing *In re* Simmons, 78 Bankr. 300 (Bankr. D. Kan. 1987) (where second mortgage was under-collateralized, mortgagee was not protected by no-

only indirect support for Debtors' position because they did not involve undersecured first mortgage claims.[27] The second group of cases, which Debtors relied on, held that the unsecured portion of a first mortgage could be avoided by the operation of section 506(d) without creating an impermissible modification of the mortgagee's rights under section 1322(b)(2).[28] The court also noted that a leading bankruptcy treatise[29] supported this approach.[30] The third group, upon which L & N relied, held that the unsecured portion of a junior lienholder's claim could not be avoided by the operation of section 506(d).[31] The court noted that this reasoning did not directly support L & N's position, but the court did recognize that *In re Russell*[32] had applied that reasoning to an undersecured first mortgage.[33]

The court then concluded that the second group of cases and the treatise *Collier on Bankruptcy* provided the "better-reasoned" view[34] and held that the no-modification clause of section 1322(b)(2) protected L & N's security interest in the Debtors' principal residence only to the extent that the claim

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modification provision of section 1322(b)(2), and undersecured portion of claim could be avoided under section 506(d)).

27. *Hougland I*, 93 Bankr. at 721.

28. *Id.* at 722. (citing Caster v. United States (*In re* Caster), 77 Bankr. 8 (Bankr. E.D. Pa. 1987) (bifurcation of the allowed claim is proper pursuant to section 506 because section 1322(b)(2) should only protect those security interests which really exist); Kehm v. Citicorp Homeowners Serv. (*In re* Kehm), 90 Bankr. 117 (Bankr. E.D. Pa. 1988) (application of section 506 to an undersecured first mortgage did not create the type of modification prohibited by section 1322 (b)(2)). The view in *Caster* was expressed as dicta. *Hougland I*, 93 Bankr. at 722.

29. 5 COLLIER ON BANKRUPTCY § 1322.06[1][a] (18th ed. 1988).

30. *Hougland I*, 93 Bankr. at 722; 5 COLLIER ON BANKRUPTCY § 1322.06[1][a] (15th ed. 1988) provides:

> [S]ince this section [1322(b)(2)] only applies to the modification of the rights of holders of claims by the Chapter 13 plan, it does not affect the determination of the allowed secured claim through operation of section 506. Hence an undersecured claim secured only by a security interest in the debtor's principal residence may still be divided into an allowed secured claim and an allowed unsecured claim, with the lien declared void to the extent it secures a claim in excess of the allowed secured claim.

Id.

31. *Hougland I*, 93 Bankr. at 721-22. (citing *In re* Hynson, 66 Bankr. 246 (Bankr. D.N.J. 1986) (the specific provision of section 1322 prevails over the general provision of section 506)).

32. 93 Bankr. 703 (D.N.D. 1988).

33. *Hougland I*, 93 Bankr. at 722.

34. *Id.*

was actually secured, and did not prohibit Debtors' avoidance of the unsecured portion of L & N's claim under section 506(d).[35]

L & N appealed the district court's decision.[36] The Ninth Circuit Court of Appeals affirmed, holding that when a mortgagee has an undersecured claim in a debtor's principal residence, the court could bifurcate the lender's claim into secured and unsecured portions, with only the secured portion receiving the special protection provided by the no-modification provision of section 1322(b)(2).[37]

II. LEGAL BACKGROUND

A. The Bankruptcy Code Provisions

Congress has provided for the classification and modification of a creditor's claims against a debtor in 11 U.S.C. section 506. In *United States v. Ron Pair Enterprises*,[38] the Supreme Court held that section 506(a) classifies a claim as secured only to the extent of the value of the property on which the lien is fixed, and then the remainder of the claim is considered unsecured.[39] Once the claim is classified, section 506(d) provides for the reduction or elimination of the unsecured portion of the creditor's claim.[40] Under 11 U.S.C. section 103(a), section 506 applies to Chapter 13 proceedings.[41]

The modification of a creditor's claim in a Chapter 13 proceeding is addressed in 11 U.S.C. section 1322(b)(2).[42] This section provides that the debtor's bankruptcy plan may modify the rights of holders of both secured and

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35. *Id.* at 722-23. The Court also held that language in the deed of trust granting L & N additional security in rents, issues, royalties, and profits of the Debtors' principal residence did not prevent L & N's claim from being secured "only" by a security interest in real property that was Debtors' principal residence so to be within the no-modification clause of section 1322(b)(2), where the deed of trust did not contain language granting L & N a mortgage security interest in specific personalty. *Id.* at 720-21.

36. *Hougland II*, 886 F.2d at 1182.

37. *Id.* at 1184.

38. 489 U.S. 235 (1989).

39. *Id. See supra* note 4 and accompanying text.

40. *See supra* note 4 and accompanying text.

41. *Hougland II*, 886 F.2d at 1184. 11 U.S.C. § 103(a) (1988) provides: "Except as provided in section 1161 of this title, chapters 1, 3, and 5 of this title apply in a case under Chapter 7, 11, 12, or 13 of this title." *Id.*

42. *See supra* note 3 and accompanying text.

unsecured claims, with one exception.[43] The bankruptcy plan may not modify a claim secured only by a security interest in the debtor's principal residence.[44] This provision's purpose was to respond to perceptions or suggestions advanced in the legislative hearings that home mortgage lenders were performing a valuable social service through their loans and needed special protection against modification of their claims.[45]

B. Judicial Interpretation

Courts have analyzed many factors to determine whether section 1322(b)(2) protects from modification that portion of an undersecured claim in a debtor's principal residence that is considered unsecured under section 506(a). The most common factor considered by the courts is statutory construction. The language of section 1322(b)(2) provides that a bankruptcy 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 . . . ."[46] Since 11 U.S.C. section 101(4) defines "claim" as including both secured and unsecured claims, courts must determine whether the word "claim" in the "other than" clause refers to secured claims, unsecured claims, or both.[47]

Courts whose opinions are typified by *Hougland* made their determination by construing the plain language of the statute itself.[48] In so doing, most

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43. *See supra* note 3 and accompanying text.

44. *See supra* note 3 and accompanying text.

45. Grubbs v. Houston First American Savings, 730 F.2d 236, 246 (5th Cir. 1984).

46. *See supra* note 3 and accompanying text.

47. 11 U.S.C. § 101(4)(A) (1988) provides: "'claim' means . . . 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* . . . ." *Id.* (emphasis added).

48. *See In re* Hart, 923 F.2d 1410, 1415 (10th Cir. 1991) ("In interpreting any statute, we 'begin with the language employed by Congress and the assumption that the ordinary meaning of that language accurately expresses the legislative purpose.'") (quoting Justice v. Valley Nat'l Bank, 849 F.2d 1078, 1084 (8th Cir. 1988)); Wilson v. Commonwealth Mortgage Corp., 895 F.2d 123, 127 (3d Cir. 1990) ("in determining the meaning of any statute, 'the words of the statute are the primary, and ordinarily the most reliable, source of interpreting' its meaning . . . .") (quoting Watt v. Alaska, 451 U.S. 259, 266 n.9 (1981)); *In re* Frost, 123 Bankr. 254, 257 (S.D. Ohio 1990); *In re* Harris, 94 Bankr. 832, 835 (D.N.J. 1989) (citing *Watt*, 451 U.S. at 266 n.9)); *In re* Bellamy, 122 Bankr. 856, 860 (Bankr. D. Conn. 1991); *In re* Demoff, 109 Bankr. 902, 919 (Bankr. N.D. Ind. 1989); Kehm v. Citicorp Homeowners Serv., 90 Bankr. 117, 120 (Bankr. E.D. Pa. 1988).

of these courts determined that "claim," in the section 1322(b)(2) "other than" clause,[49] applies only to the "secured claims" language that precedes it.[50] The court in *In re Harris*,[51] however, finding the language ambiguous, stated that legislative history supported its determination that only secured claims were prohibited from modification.[52]

Courts consistent with *Hougland* have often addressed the legislative history of section 1322(b)(2),[53] but with the exception of *Harris*,[54] legislative history has not been a determinative factor in the courts' decisions.[55] The courts, however, have often supported their result with such additional factors as the legislative purpose of the Bankruptcy Code to provide a "fresh

49. *See supra* note 3 and accompanying text.

50. *See Hart*, 923 F.2d at 1415 ("We find nothing in the plain language of section 1322(b)(2) which instructs us to go beyond the Code's statutory definition of the term 'secured claims' to protect the unsecured portion of an undersecured home mortgage."); *Wilson*, 895 F.2d at 127 ("[T]he 'other than' phrase should be read to limit modification only of that portion of the claim that is secured."); *Frost*, 123 Bankr. at 257 ("[T]he word 'claim' in the 'other than' phrase must be a secured claim because the words 'secured claim' precede and modify the entire phrase . . . ."); *Bellamy*, 122 Bankr. at 860-61 ("Because the 'other than' clause immediately follows 'holders of secured claims,' the secured claim language is the referent of the 'other than' clause. . . .") (quoting Wilshire Westwood Assoc. v. Atlantic Richfield Corp., 881 F.2d 801, 804 (9th Cir. 1989)); *Demoff*, 109 Bankr. at 919 ("[T]he later phrase refers to the prior phrase, and only the secured claim portion as defined in § 506(a) is protected from modification."); *Kehm*, 90 Bankr. at 119 ("The only logical, semantic interpretation of this section is that the § 1322(b)(2) prohibition against modification is limited to fully secured claims.").

51. 94 Bankr. 833, 835 (D.N.J. 1989).

52. *Id.* at 835.

53. *See, e.g., Hart*, 923 F.2d at 1412; *Wilson*, 895 F.2d at 127-28; *Bellamy*, 122 Bankr. at 861; *Demoff*, 109 Bankr. at 919-20.

54. *Harris*, 94 Bankr. at 836.

55. *See, e.g., Hart*, 923 F.2d at 1415 ("[L]egislative history . . . is not clear enough . . . to show a 'demonstrably' different congressional intent than that indicated by the plain meaning of the statute itself."); *Wilson*, 895 F.2d at 127 ("Unfortunately, our review of the history of the provision does not provide much insight into the critical question here."); *Bellamy*, 122 Bankr. at 861 ("The legislative history . . . is not completely unambiguous . . . ."); *Demoff*, 109 Bankr. at 919-20.

start" to the debtor,[56] or their doubt that the result will substantially affect creditors.[57]

Courts rejecting the *Hougland* court's reasoning find that the statutory provisions in sections 1322(b)(2) and 506(a) are in conflict,[58] or that modification of the unsecured claim would vitiate the purpose of section 1322(b)(2) to protect home-mortgage lenders.[59] The most prominent decisions in this area are *In re Hynson*,[60] which addressed both the statutory conflict and the purpose of section 1322(b)(2), and *In re Catlin*,[61] which only addressed the conflict issue. The *Hynson* and *Catlin* courts both held that since section 506(a) and section 1322(b)(2) conflicted, the specific provisions of section 1322(b)(2) should supersede the general provisions of section 506(a). Therefore, the no-modification prohibition in the "other than" clause should apply to both the secured and unsecured portions of the creditor's claim.[62] The *Hynson* court went on to hold that the application of the "cram-down" provisions of section 506 would vitiate the protections of section 1322(b)(2).[63] Many courts have used the reasoning in *Catlin* and *Hynson* to prohibit the modification of the unsecured portion of a creditor's claim secured by a debtor's principal residence.[64]

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56. *See, e.g., In re* Harris, 94 Bankr. 832, 836 (D.N.J. 1989); *In re* McNair, 115 Bankr. 520, 523 (Bankr. E.D. Va. 1990); *In re* Frost, 123 Bankr. 254, 257-58 (S.D. Ohio 1990).

57. *See, e.g., Harris*, 94 Bankr. at 835; *Demoff*, 109 Bankr. at 920-21.

58. *See, e.g., In re* Russell, 93 Bankr. 703, 705-06 (D.N.D. 1988); *In re* Mitchell, Nos. 90-11369, 90-11289 (Bankr. D.N.H. Feb. 13, 1991) (WESTLAW, FBKR-CS database); *In re* Chavez, 117 Bankr. 733, 734 (Bankr. S.D. Fla. 1990) (quoting *In re* Catlin, 81 Bankr. 522, 524 (Bankr. D. Minn. 1987)); *In re* Sauber, 115 Bankr. 197, 199 (Bankr. D. Minn. 1990); *In re* Schum, 112 Bankr. 159, 160-61 (Bankr. N.D. Tex. 1990); *In re* Kaczmarczyk, 107 Bankr. 200, 202 (Bankr. D. Neb. 1989); *In re* Hemsing, 75 Bankr. 689, 691-92 (Bankr. D. Mont. 1987).

59. *See, e.g., Russell*, 93 Bankr. at 706; *Mitchell*, Nos. 90-11369, 90-11289; *Chavez*, 117 Bankr. at 734; *Sauber*, 115 Bankr. at 199; *Schum*, 112 Bankr. at 162; *Kaczmarczyk*, 107 Bankr. at 202; *Hemsing*, 75 Bankr. at 692.

60. 66 Bankr. 246 (Bankr. D.N.J. 1986) *rejected by In re* Harris, 94 Bankr. 832 (D.N.J. 1989). Although *Hynson* was later overruled, its analysis influenced other courts.

61. 81 Bankr. 522 (Bankr. D. Minn. 1987).

62. *Catlin*, 81 Bankr. at 524; Hynson, 66 Bankr. at 250 (quoting *In re* Mahaner, 34 Bankr. 308, 309 (Bankr. W.D.N.Y. 1983)).

63. *Hynson*, 66 Bankr. at 252.

64. *See In re* Russell, 93 Bankr. 703, 705-06 (D.N.D. 1988); *In re* Mitchell, Nos. 90-11369, 90-11289 (Bankr. D.N.H. Feb. 13, 1991)(WESTLAW, FBKR-CS database); *In re* Chavez, 117 Bankr. 733, 734 (Bankr. S.D. Fla. 1990); *In re* Sauber, 115 Bankr. 197, 199 (Bankr. D. Minn. 1990); *In re* Schum, 112 Bankr. 159, 160-61 (Bankr. N.D.

One court has also looked at the prior Bankruptcy Act to determine that modification of an undersecured claim in the debtor's principal residence is prohibited.[65] The court found that since the prior Bankruptcy Act did not allow Chapter 13 debtors to modify any secured claims, this suggested that Congress did not want to change from that position with respect to home mortgages.[66]

Within this legal background, the *Hougland* court weighed the various factors and determined that the unsecured portion of the creditor's claim was not protected from modification by section 1322(b)(2).

III. INSTANT DECISION

The *Hougland* court[67] addressed L & N's contention that section 1322(b)(2) protected from modification the unsecured portion of L & N's undersecured claim.[68] The court first noted that the issue was one of statutory construction and then looked at the language of section 1322(b)(2) and the interpretation given section 506(a) by *Ron Pair Enterprises*.[69] In so doing, the court recognized that courts differed in their interpretation of section 1322 and whether the section affected the section 506(a) provision dividing the undersecured claim into a secured portion and an unsecured portion.[70] Some courts had held that nothing in section 1322 affected the classification of the claim as secured and unsecured under section 506(a),[71] while others had held that section 1322(b)(2) prevented the separate treatment of what would otherwise be an unsecured claim.[72]

Tex. 1990); *In re* Kaczmarczyk, 107 Bankr. 200, 202 (Bankr. D. Neb. 1989); *In re* Hemsing, 75 Bankr. 689, 691-92 (Bankr. D. Mont. 1987).

65. *Kaczmarczyk*, 107 Bankr. at 202-03.

66. *Id.*

67. Judge Fernandez wrote the majority opinion in which Judge Pregerson and Judge Trott joined.

68. *Hougland II*, 886 F.2d at 1183.

69. *Id.* at 1183. See *supra* note 38 and accompanying text for the *Ron Pair Enter.* court's definition of section 506(a).

70. *Hougland II*, 886 F.2d at 1183.

71. *Id.* at 1183 (citing *Harris*, 94 Bankr. at 832; *In re* Frost, 96 Bankr. 804 (Bankr. S.D. Ohio 1989), *aff'd*, 123 Bankr. 254; Kehm v. Citicorp Homeowners Serv., 90 Bankr. 117 (Bankr. E.D. Pa. 1988); *In re* Caster, 77 Bankr. 8 (Bankr. E.D. Pa. 1987); *In re* Bruce, 40 Bankr. 884 (Bankr. W.D. Va. 1984)).

72. *Hougland II*, 886 F.2d at 1183 (citing *In re Russell*, 93 Bankr. 703, 705 (D.N.D. 1988); *In re* Brown, 91 Bankr. 19 (Bankr. E.D. Va. 1988); *Catlin*, 81 Bankr. at 522; *In re* Hemsing, 75 Bankr. 689 (Bankr. D. Mont. 1987); *Hynson*, 66 Bankr. at 246).

In interpreting the two statutes,[73] the court stated that the language of the statute itself should be the guiding factor.[74] Since section 103(a) applied section 506(a) to Chapter 13 proceedings, there was no reason to believe that the phrases "secured claim" and "unsecured claim" in section 1322(b)(2) could have any other meaning than those given them by section 506(a).[75] Therefore, L & N's claim had a "secured" component and an "unsecured" component.[76] The court then addressed the "other than" clause of section 1322(b)(2)[77] and found that the clause addressed what preceded it, indicating that only the secured portion received special protection.[78] The court rejected the *Russell* court's finding that section 1322 is violated if the unsecured portion of the claim is affected by the plan[79] because that suggests that the "other than" clause also referred to the unsecured portion of the claim.[80]

The court then determined that section 506(a) and section 1322(b)(2) were "in harmony when read in the context of the whole statute," rejecting *In re Hemsing*,[81] which had held that the statutes conflicted.[82] The court also noted that *Green v. Bock Laundry Machine Co.*[83] required the court to look for other guidance if the court's construction would lead to an absurd result.[84] The court concluded, however, that since the truly secured portion of the lender's claim would still receive protection, no absurdity existed.[85] This construction was also supported by a leading treatise on bankruptcy law.[86] In response to other courts' concerns that such a construction would severely undermine the statute,[87] the court suggested that most residential

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73. *See supra* section II.B. of this Note.

74. *Hougland II*, 886 F.2d at 1183 (citing United States v. Ron Pair Enter., 489 U.S. 235 (1989)).

75. *Id.* at 1183-84.

76. *Id.* at 1184.

77. *See supra* note 3 and accompanying text.

78. *Hougland II*, 886 F.2d at 1184.

79. *In re* Russell, 93 Bankr. 703, 705-06 (D.N.D. 1988).

80. *Hougland II*, 886 F.2d at 1184.

81. 75 Bankr. 689, 691 (Bankr. D. Mont. 1987) (section 1322 and section 506 are in conflict).

82. *Hougland II*, 886 F.2d at 1184 (citing Davis v. Michigan Dept. of Treasury, 489 U.S. 803 (1989)).

83. 490 U.S. 504 (1989).

84. *Id.*

85. *Hougland II*, 886 F.2d at 1184.

86. Id. (citing 5 COLLIER ON BANKRUPTCY § 1322.06[a] (18th ed. 1988).

87. *E.g., In re* Russell, 93 Bankr. 703, 706 (D.N.D. 1988); *In re* Hynson, 66 Bankr. 246, 252 (Bankr. D.N.J. 1986).

mortgage lenders would ensure that they had a sufficient cushion to avoid being in an undersecured position.[88]

Finally, the court noted that courts who had addressed the legislative history of the statute found that the purpose of the statute was to benefit residential real estate lenders, which was already made obvious by the "other than" clause.[89] Additionally, there was no need to concentrate on the legislative history if the statute was internally consistent and could be construed according to its plain language.[90] The court then held that Congress plainly provided for the separation of undersecured claims into a secured portion and an unsecured portion and that the unsecured portion did not receive protection from modification under section 1322(b)(2).[91]

IV. COMMENT

The *Hougland* court reached a fair and logical result. As a result, the *Hougland* decision on the issue of modification of undersecured claims in a Chapter 13 proceeding has become the majority position among the courts and is consistent with the leading treatise on bankruptcy law.[92] Moreover, the *Hynson* decision, which influenced other courts to reject *Hougland*,[93] has itself been overruled.[94]

Courts consistent with *Hougland* have reached a logical result in construing the interplay between section 1322 and section 506. "In analyzing the construction of the statute, 'the starting point' is the 'language itself'."[95] "In addition, the 'plain meaning' of the language is the 'primary, and ordinarily the most reliable, source of interpreting the meaning of a statute'."[96] Section 506 treats an undersecured creditor as a holder of two entirely separate claims.[97] Section 1322 then allows for modification of "the

88. *Hougland II*, 886 F.2d at 1184-85.

89. *Id.* at 1185.

90. *Id.*

91. *Id.*

92. *See* 5 COLLIER ON BANKRUPTCY § 1322.06[1][a] (18th ed. 1988).

93. *See, e.g., In re* Russell, 93 Bankr. 703, 705-06 (D.N.D. 1988); *In re* Chavez, 117 Bankr. 733, 734 (Bankr. S.D. Fla. 1990); *In re* Schum, 112 Bankr. 159, 162 (Bankr. N.D. Tex. 1990); *In re* Kaczmarczyk, 107 Bankr. 200, 202 (Bankr. D. Neb. 1984); *In re* Hemsing, 75 Bankr. 689, 691-92 (Bankr. D. Mont. 1987).

94. *See In re* Harris, 94 Bankr. 832, 836 (D.N.J. 1989).

95. *Harris*, 94 Bankr. at 835 (quoting Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 756 (1975) (Powell, J., concurring)).

96. *Harris*, 94 Bankr. at 835 (quoting Watt v. Alaska, 451 U.S. 259, 266 n.9 (1981)).

97. *In re* Bellamy, 122 Bankr. 856, 860 (Bankr. D. Conn. 1981) (citing Goins v.

rights of holders of a secured claim, 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."[98] From this plain language, only the secured portion of the claim would be subject to the protection of section 1322(b)(2).[99]

In *Wilshire Westwood Association v. Atlantic Richfield Corp.*,[100] the court stated that a qualifying phrase must be applied to words or phrases immediately preceding it.[101] Using this reasoning, the word "claim" in the "other than" clause of section 1322(b)(2) would refer only to the "secured claim" phrase immediately preceding it.[102]

In addition, the court in *In re Bellamy*[103] has noted that if Congress had intended an exception to section 506(a), it could have done so expressly, as it did in 11 U.S.C. section 1111(b)(2).[104] "Section 1111(b)(2) provides that 'notwithstanding section 506(a) of this title,' an undersecured creditor may elect to have an allowed claim treated as a secured claim to the full extent the claim is allowed, rather than to the extent of the collateral."[105] The court noted that "this conclusion is underscored by the different treatment given throughout the Code to the secured and unsecured portions of an undersecured claim."[106] "For example, an undersecured claim survives a Chapter 7 discharge to the extent of the value of the collateral that secures it; the unsecured portion of the claim is treated separately and discharged . . . ."[107] "Likewise, it is self evident that a creditor with a lien on collateral worth a small percentage of its claim should be treated in a Chapter 13 plan as holding one relatively small secured claim and one relatively large unsecured claim, rather than a single fully secured claim."[108]

As previously noted, courts rejecting *Hougland* have found that the two statutes conflict and the specific provisions of section 1322 prevail over the

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Diamond Mortgage Corp., 119 Bankr. 156, 162 (N.D. Ill. 1990)).

98. *See supra* note 3 and accompanying text.

99. *In re* Frost, 123 Bankr. 254, 257 (Bankr. S.D. Ohio 1990).

100. 881 F.2d 801 (9th Cir. 1989).

101. *Id.* at 804.

102. *See supra* note 3 and accompanying text.

103. 122 Bankr. 856, 860 (Bankr. D. Conn. 1981).

104. *Id.*

105. 11 U.S.C. § 1111(b)(2) (1988).

106. *Bellamy*, 122 Bankr. at 860.

107. *Id.* (citing Lindsey v. Fed. Land Bank of St. Louis, 823 F.2d 189, 190-92 (7th Cir. 1987)).

108. *Id.* (citing Goins v. Diamond Mortgage, 199 Bankr. 156, 162 (N.D. Ill. 1990)).

general provisions of section 506.[109] The *Hynson* court stated that "regardless of the inclusiveness of the general language of [section 506(a)], it does not apply or prevail over matters specifically dealt with in another part of the same enactment."[110] This rule of construction, however, is only applicable when the statutes conflict.[111] The *Hougland* court's construction does not find the statutes in conflict, but rather "in harmony when read in the context of the whole statute."[112] In addition, section 103(a) is strong evidence that section 506 was intended to apply to section 1322.[113]

Courts interpreting the "specific over general" rule avoid its use unless absolutely necessary. In *Aeron Marine Shipping Co. v. United States*,[114] the court stated that this rule of statutory construction is applicable only when there is an inescapable conflict between the two provisions.[115] In *United States v. Stauffer Chemical Co.*,[116] the court stated that statutory provisions are to be construed, whenever possible, in a way that avoids conflicts and achieves consistency.[117] The *Hougland* result would achieve a construction of section 1322 and section 506 that is consistent with these guidelines.

The legislative history of section 1322 lends additional support to the *Hougland* court's reasoning. The original House version of section 1322(b)(2) provided for the modification of the rights of holders of secured claims or holders of unsecured claims.[118] The original Senate version of section 1322(b)(2) provided for modification of the rights of holders of secured claims (other than claims wholly secured by mortgages on real property) or of holders of unsecured claims.[119] "The final version of section 1322(b)(2) represented a 'compromise agreement' between the House version that allowed modification of all secured claims and the Senate version allowing modification of all secured claims except 'claims wholly secured by mortgages on real

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109. *See supra* note 58 and accompanying text.

110. *In re* Hynson, 66 Bankr. 246, 249 (Bankr. D.N.J. 1986) (citing Maitico v. United States, 302 F.2d 880, 886 (D.C. Cir. 1962)).

111. *In re* Demoff, 109 Bankr. 902, 920 (Bankr. N.D. Ind. 1989).

112. *Hougland II*, 886 F.2d at 1184.

113. Wilson v. Commonwealth Mortgage Corp., 895 F.2d 122, 128 (3d Cir. 1990) (citing *In re* Lewis, 875 F.2d 53, 55 (3d Cir. 1989)).

114. 695 F.2d 567 (D.C. Cir. 1982).

115. *Id.* at 576 (citing C. SANDS, STATUTES AND STATUTORY CONSTRUCTION § 46.05 (4th ed. 1972)).

116. 684 F.2d 1174 (6th Cir. 1982), *aff'd*, 464 U.S. 165 (1984).

117. *Id.* at 1186.

118. *In re* Bellamy, 122 Bankr. 856, 861 (Bankr. D. Conn. 1991) (*citing* H.R. 8200, 95th Cong., 1st Sess. (1977)).

119. *Id.* at 861 (*citing* S. 2266, 95th Cong., 2d Sess. (1978)).

property'."[120] Since the final version represented a compromise between the pro-debtor House version and the pro-creditor Senate version, which prohibited the modification of claims wholly secured by *any* real property, the final version of section 1322(b)(2) would not provide any more protection to creditors than the original Senate version.[121] It is doubtful, however, that the statute would even provide that much protection. In *Wilson v. Commonwealth Mortgage Corp.*,[122] the court noted that "although it [was] clear that the anti-modification provision was inserted on behalf of the home mortgage industry, the fact that the provision itself was a compromise suggests that the residential mortgage providers did not emerge with all the protection they may have sought."[123]

The *Hougland* result is as fair as it is logical. In *In re Demoff*,[124] the court noted that it is doubtful that such a construction would have "considerable impact on first mortgage lenders" if the mortgage was in fact based on "sound credit judgment."[125] The court noted that the value of the property might decrease below the claim in some circumstances, but "if the lender is at all diligent this should not be a frequent state of affairs so as to impair the long-term residential mortgage market."[126] In *Kehm v. Citicorp Homeowners Service Inc.*,[127] the court stated that "[t]here is good reason to believe that Congress was contemplating more substantial alterations of rights when it excepted home mortgagees' rights from section 1322(b)(2)'s general authorization to 'modify the rights of holders of secured claims'."[128] The court then noted that the Third Circuit had "already ruled that a post-acceleration cure, a step with a much more drastic and more immediate impact on a mortgagee's rights, is not prohibited by section 1322(b)(2)."[129] It would appear, therefore, that the *Hougland* court's construction of these statutes would not vitiate the protections of section 1322(b)(2), as many courts rejecting *Hougland* had feared, because this construction would not leave section 1322(b)(2) without a *raison d'etre*.[130] Furthermore, in addition to the sound statutory construction and fairness of the *Hougland* court's

120. *Id.* (citing 124 CONG. REC. H1106-07 (Sept. 28, 1978) (statement of Rep. Edwards); 124 CONG. REC. S17,423 (Oct. 6, 1978) (statement of Sen. DeConcini)).
121. *Id.*
122. 895 F.2d 123 (3d Cir. 1990).
123. *Id.* at 128.
124. 109 Bankr. 902 (Bankr. N.D. Ind. 1989).
125. *Id.* at 921.
126. *Id.*
127. 90 Bankr. 117 (Bankr. E.D. Pa. 1988).
128. *Id.* at 120.
129. *Id.* at 121.
130. *Wilson*, 895 F.2d at 128.

decision, the result will encourage debtors to file Chapter 13 proceedings rather than Chapter 7 proceedings[131] and is consistent with the purpose of the Bankruptcy Code to provide debtors with a "fresh start, . . . by not strapping the debtor with preexisting unsecured debt."[132] It is a result, therefore, that all courts should adopt.

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131. *In re* McNair, 115 Bankr. 520, 523 (Bankr. E.D. Va. 1990).

132. *In re* Harris, 94 Bankr. 832, 836 (D.N.J. 1989) (quoting *In re* Simmons, 78 Bankr. 300, 304 (D. Kan. 1987)). *See also In re* Frost, 123 Bankr. 254, 257-58 (Bankr. S.D. Ohio 1990); *McNair*, 115 Bankr. at 523.