In the United States Bankruptcy Court

for the Northern District of Iowa

RICKY WYNN DRAHOS
CRISTIE ELAINE DRAHOS
Debtor(s).

Bankruptcy No. 93-60924KW

Chapter 13

ORDER RE: MOTION TO LIFT STAY AND PLAN CONFIRMATION

On September 15, 1993, the above-captioned matter came on for hearing pursuant to assignment. The Debtors appeared in person with their attorney, Stephen Rapp. Also appearing was Chapter 13 Trustee Carol Dunbar as well as Attorney Larry Anfinson representing Creditor MidAmerica Savings Bank. Evidence was presented after which the Court took the matter under advisement.

There are two matters before Court for consideration: (a) final hearing on Creditor MidAmerica Savings Bank's Motion to Lift Stay; and (b) Confirmation of Debtors' Chapter 13 Plan and consideration of the objection filed thereto by MidAmerica Savings Bank. The Court will address each matter separately.

FINDINGS OF FACT

Debtors executed a note for $19,700 on May 12, 1991. This note was payable to MidAmerica Savings Bank (MidAmerica) and was secured by a mortgage on Debtors' home. Debtors began failing to make monthly payments to MidAmerica and other creditors near the end of 1992. Debtors filed for relief under Chapter 13 on May 25, 1993. Debtors submitted a Chapter 13 Plan on June 8, 1993. This proposed Plan would allow Debtors to make monthly installment payments of $110 over a 60 month period. The Chapter 13 Trustee has filed no formal objection to this Plan.

However, Creditor MidAmerica objects to Debtors' Plan in two respects. First, MidAmerica argues that the Court should lift the automatic stay to allow completion of foreclosure proceedings against Debtors' personal residence because Debtors have no equity in this property. Debtors owe MidAmerica approximately $21,455 as of the date of trial. The appraised value on this property has deteriorated and the appraised value as of June 7, 1993 was approximately $8,000. Second, MidAmerica argues that it is entitled to interest on the arrearage of approximately $4,100 in addition to contractual interest under the original note. Under the proposed Plan, the existing arrearage would be cured by Debtors over a period of five years without the imposition of additional interest.

AUTOMATIC STAY

The first issue for the Court's consideration is whether this Court should lift the automatic stay presently in place on foreclosure proceedings against Debtors' personal residence because the Debtors have no equity in this residence. Relief from the effects of the automatic stay under 11 U.S.C. § 362(a) is controlled in the present context by 11 U.S.C. § 362(d)(2). The provisions of § 362(d)(2) state:

> d. On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay--
> 2. with respect to a stay of an act against property under subsection (a) of this section, if--
> A. the debtor does not have an equity in such property; and
> B. such property is not necessary to an effective reorganization.

The record establishes that this property has decreased substantially in fair market value since its purchase. The property was purchased in 1991 and the outstanding balance on the mortgage has not decreased substantially. It is uncontested that, at the present time, Debtors have no equity in this property. As such, MidAmerica must receive relief from the automatic stay if the provisions of § 362(d)(2)(B) are met. In order to satisfy the requirements of this section, it is necessary that one or both of the following propositions are established: (1) that the property is not necessary to an effective reorganization; or (2) that an effective reorganization under the Plan is not feasible. The Debtors have the burden of proving both that the property is necessary and that the reorganization is feasible. 11 U.S.C. § 362(g).

a. Is the property necessary to an effective reorganization?

The term "necessary", in the context of 11 U.S.C. § 362(d)(2)(B), was recently defined by the United States Supreme Court as,

> "not merely a showing that if there is conceivably to be an effective reorganization, this property will be needed for it; but that the property is essential for an effective reorganization. . ."

United States Savs. Ass'n of Texas v. Timbers of Inwood Forest Assoc., Ltd., 484 U.S. 365, 375-76, 108 S. Ct. 626, 633 (1988).

Debtors have cited to the Court the case of Phoenix Piccadilly, Ltd. v. Life Ins. Co. of Virginia, 849 F.2d 1393 (11th Cir. 1988), for the proposition that a default may be cured over the course of the Plan even if the Debtors have no equity in the property. However, Phoenix Piccadilly focuses more on the issue of bad faith than curing of a default. A case similar on its facts has been decided in the Northern District of Iowa. Judge William Edmonds determined that under the facts presented in that case, a home can be property which is necessary to an effective reorganization. In re Thacker, No. X90-01494S, slip op. at 9 (Bankr. N.D. Iowa Aug, 24, 1993). In Thacker, the mortgagee sought relief from the automatic stay arguing that the home was not necessary for an effective reorganization. Thacker holds that, "the stability a home provides makes it necessary." Thacker at 9 (citing, In re Thomas, 121 B.R. 94, 108 (Bankr. N.D. Ala. 1990)).

The analysis in Thacker is identical to that of Timbers of Inwood Forest, in that "necessary" is equated to "essential for an effective reorganization". In his analysis, Judge Edmonds in Thacker determined that the home was essential to a reorganization in that the home provided necessary stability for the family and less expensive alternatives were scarce.

Debtors have lived in this home for several years and have made it their homestead. The payment plan envisions payments of $110 per month. It would be very difficult for Debtors to find alternative housing which is less expensive. It is apparent that the home is important to the stability of Debtors household.

In summary, the United States Supreme Court has determined that for property to be "necessary" to an effective reorganization, it must be "essential" to the plan and not merely convenient. While these terms have been given specific legal meaning, their application becomes much more subjective when applied to a specific factual situation. What is essential or necessary to a large corporation, has little, if any, relevance to what is "necessary" or "essential" to a family struggling to make house payments on a limited income. The Northern District of Iowa has determined that under appropriate facts, a home is "necessary" to an effective reorganization where it provides stability to the family unit. It is the ultimate conclusion of this Court that the Debtors have met their burden of proof under the present facts and their home is "necessary" to their rehabilitation under the proposed Plan. The Court will subsequently be discussing interest on arrearage in this opinion. The Court's analysis in this section will not change as a result of the Court's subsequent determinations as to interest on arrearage.

b. Is an effective reorganization feasible?

In Timbers of Inwood Forest, 484 U.S. at 376, 108 S. Ct. at 633, the Court held that the term "effective reorganization" means, "there must be a reasonable possibility of a successful reorganization within a reasonable time." The Debtors have the burden of proving the feasibility of the Plan. 11 U.S.C. § 352(g)(2).

In this case, the Trustee stated, "[t]he Plan appears to be feasible based on the figures provided in Schedules I and J of

the petition." Trustee's Report of No Objections to Plan, No. 93-60924KW, at 1 (Aug. 18, 1993). The Trustee further reported that the Debtors were current in proposed Plan payments through August 1993, Id. at 1. By staying current in making payments to the Trustee, the Debtors are proving their commitment to the Plan and the feasibility of an effective reorganization. Further, the nominal amount of the monthly payments, $110.00, are reasonably calculated to be feasible in light of the Debtors' monthly income stream.

In summary, the standard for the feasibility of an effective reorganization is a "reasonable" possibility of success. The Debtors' Plan, including modest monthly payments to the Trustee, is reasonable, especially in light of the Debtors' initial compliance with it and the Trustee's positive report. Again, the Court will be discussing the issue of interest on arrearage in the subsequent section. The Court's analysis in this section does not necessarily change based upon the Court's ruling in the following analysis.

INTEREST ON ARREARAGE

The Chapter 13 Trustee has filed no objection to the Plan as proposed. Creditor MidAmerica has filed one objection to the Plan in which it asserts that it is entitled to interest on the arrearage of approximately $4,162. It asserts that in addition to interest payable under the mortgage, it is entitled to additional interest under the legal framework established in Nobelman v. American Savs. Bank, ___ U.S. ___, 113 S. Ct. 2106 (1993).

The issue of a mortgagee's rights under a Chapter 13 Plan, where the claim is undersecured as in the present case, was recently addressed by the U.S. Supreme Court in Nobelman. Nobelman involved a Plan which proposed to bifurcate a claim on the debtor's principal residence into secured and unsecured claims, reducing the mortgage to the fair market value of the mortgaged residence. Id. at 2108. In affirming the lower court's denial of confirmation, the Court held that 11 U.S.C. § 1322(b)(2) protects a creditor's rights under a principal residence mortgage contract with respect to both the secured and unsecured claims. Id. at 2111. Section 1322(b)(2) reads as follows:

> (b) Subject to subsections (a) and (c) of this section, the plan may--
>
> (b) modify the rights of holders of unsecured 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;

The Court interpreted the term "rights" as follows:

> The bank's contractual rights are contained in a unitary note that applies at once to the bank's overall claim, including both the secured and unsecured components. Petitioners cannot modify the payment and interest terms for the unsecured component, as they propose to do, without also modifying the terms of the secured component.

Id. at 2111. The Court in Nobelman, overruled In re Bellamy, 962 F.2d 176 (2d Cir. 1992).

Since Nobelman, one Bankruptcy Court opinion has addressed a Chapter 13 Plan which did not provide for interest arrearage in the context of an undersecured principal residence mortgage claim. In re Callahan, No. 93-20452, 1993 WL 359853 slip op. at 1 (Bankr. W.D.N.Y. Sept. 13, 1993). The court determined that the undersecured creditor was entitled to interest on arrearage. Id. at 4. The court held that in order to meet the requirements of 11 U.S.C. § 1322(b)(5), which provides for the curing of a default (within the constraints of § 1322(b)(2)), the consequences of the default must be nullified through the granting of interest or a present value factor. Id. at 2-3. Nobelman and Callahan, in conjunction, establish that a creditor is entitled to the benefit of the original bargain, even though a debtor may cure a default over a reasonable period of time.

Having determined that an undersecured creditor is entitled to interest on arrearage, the Court in Callahan entered into a discussion of the appropriate methodology to use to provide an equitable cure which complies with the requirements of § 1322(b)(5) and Nobelman. The Court, in Callahan, ultimately determined that the New York judgment interest rate was an appropriate mechanism to provide for this equitable cure based on reasons of administrative convenience and

consistency. In the present case, the note entered into evidence at Exhibit "A" states that: "Borrower shall pay to the Note holder a late charge of 5 percent of any monthly installment not received by the Note holder within 15 days after the installment is due." This late charge may constitute a sufficient equitable cure to satisfy the requirements of Nobelman. Additionally, Iowa has a judgment interest rate which may provide an alternative equitable cure. Sec. 535.3 of the Iowa Code. Finally, various rates of interest are specified as alternative rates of interest when no default rate is specified. See sec. 535.2 of the Iowa Code. The Court does not intend to indicate that the foregoing is an exclusive list of possible equitable cures though they are three alternatives which provide some specificity and consistency in compliance with Nobelman.

In summary, it is the conclusion of this Court that the Plan, as proposed, provides for monthly repayments, without interest on the arrearage. The arrearage is a claim secured by a security interest in real property that is the Debtors' principal residence. Under Nobelman, the rights of MidAmerica bargained for in the loan agreement are modified. The modification of a creditor's right is prohibited by 11 U.S.C. § 1322(b)(2) as well as the language of Nobelman. Under Callahan, the equitable cure envisioned by this Plan is not a true cure because the Creditor is not reinstated into its predefault economic position through the granting of a present value factor. As such, the Plan, as proposed, cannot be confirmed. The only modification necessary to acquire confirmation is the addition of an acceptable mechanism for providing an equitable cure as previously discussed. In that regard, the Court has discussed certain options which may comply with the doctrine of equitable cure. However, the Court does not ultimately decide any particular preference. The Court will allow the parties an opportunity to negotiate a resolution consistent with this opinion. If the parties are unable to reach an agreement as to an equitable cure, the Court will allow the parties additional oral argument and briefing in order to achieve an appropriate mechanism which satisfies the equitable cure requirement.

WHEREFORE, for the reasons set out herein, Creditor MidAmerica Savings Bank's Motion to Lift Stay is DENIED.

FURTHER, for the reasons set forth herein, MidAmerica Savings Bank's Objection to Debtors' Chapter 13 Plan is SUSTAINED.

FURTHER, Debtors shall be granted 30 days from the date of this Order within which to submit an amended Chapter 13 Plan.

SO ORDERED this 5th day of October, 1993.

Paul J. Kilburg
U.S. Bankruptcy Judge