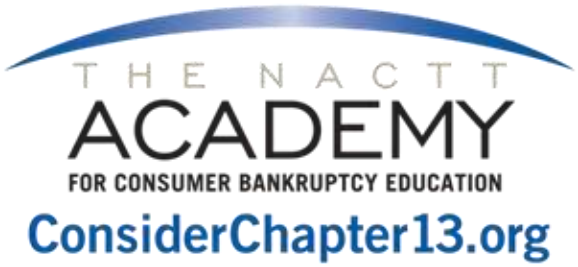
NACTT 57th Annual Seminar San Francisco, CA Educational Materials



Thursday 1:00 – 2:00 Breakout Session

Mortgage Issues

Moderator: John M. Hauber, Chapter 13 Standing Trustee for the District of Indiana (Indianapolis)

Alice Whitten, Managing Counsel - Senior Vice President, Consumer Lending Division, Wells Fargo (Irving, TX)

Michael T. Bates, Executive Director/Attorney, Chief Legal Office, USAA (San Antonio, TX)

Lisa Sitkin, Senior Staff Attorney, National Housing Law Project (San Francisco, CA)

MATERIALS INDEX

Why Homeowner Assistance Fund Programs Should be Accessible to Homeowners in Bankruptcy

July 2021

The American Rescue Plan Act of 2021 includes $9.9 billion for creation of a Homeowner Assistance Fund (HAF) to be administered by the Treasury Department. The HAF was established to mitigate financial hardships connected with the coronavirus pandemic and prevent foreclosures among homeowners who have experienced a hardship related to the pandemic. Treasury has released initial guidance regarding how states should utilize the HAF funds pursuant to an approved plan. States have until July 31, 2021 to submit their proposed HAF plans for approval or provide information regarding when they will submit their proposed HAF plans.

State plans should not exclude borrowers in active bankruptcy from eligibility for the HAF assistance. As explained below, homeowners might need to file bankruptcy for a number of reasons, including preventing a foreclosure sale from occurring while they wait for HAF programs to open for applications and then go through the application process. These borrowers will still need HAF assistance, and helping this population of borrowers to avoid foreclosure would fulfill both the letter and the spirit of the American Rescue Plan.

Many Homeowners Recovering from Economic Impacts of the Pandemic Will Need to File Bankruptcy.

Many homeowners who have experienced a financial hardship related to the COVID-19 pandemic may need to file bankruptcy. This could be necessitated by medical expenses not covered by insurance, credit card debt accumulated during a period of unemployment, car payments that fell into arrears, or other bills that have mounted during the past year. In addition, many homeowners will file bankruptcy in order to prevent a foreclosure sale from occurring while they are attempting to apply for HAF assistance. For example, one-third of the mortgage market is comprised of non-federally backed mortgages that have not been subject to any moratorium on foreclosure sales. These borrowers are among those most likely to need HAF assistance, because their servicers offer few other viable options to save their homes. There is likely to be a surge in foreclosure filings for these homes between now and August 31, 2021, as servicers rush to begin foreclosure before a CFPB rule providing additional foreclosure protections goes into effect. For many of these borrowers, the only way to save their homes will be to file bankruptcy while awaiting HAF assistance.

These homeowners should still be able to obtain HAF assistance despite their active bankruptcy case. Many of them will not be able to afford the necessary bankruptcy payments unless their mortgage arrears are covered by HAF funds. They will need to devote their available income to paying up car arrears or other required amounts in the bankruptcy plan.

States are required to spend at least 60% of the HAF funds on eligible purposes related to homeowners who are up to 100% of area median income or U.S. median income, whichever is greater. These below-median income homeowners are more likely to be financially struggling on multiple fronts, and may need bankruptcy protection for a variety of reasons. They should not be blocked from accessing the HAF program based on having an active bankruptcy case. As described below, bankruptcy law does not pose a barrier to receiving the assistance.

Clearing up Common Misconceptions About Bankruptcy:

- **Mortgage servicers can communicate with borrowers who are in an active bankruptcy case**. Mortgage servicers can, and are required to, send mortgage statements to borrowers in active bankruptcy. They can review such borrowers for loss mitigation, and they frequently offer loss mitigation options to borrowers in bankruptcy. Some bankruptcy courts even have programs to facilitate this process. Servicers can also communicate with HAF administrators regarding matters like mortgage account reinstatement as part of the process of facilitating the use of HAF assistance to cure mortgage delinquencies. These actions do not violate the bankruptcy "automatic stay."

- **Servicers cannot refuse to take a full mortgage reinstatement simply because a borrower is in bankruptcy**. If the borrower provides sufficient funds to bring the loan current, the servicer must apply it properly to the loan and must not send the money back. If servicers improperly send the money back, the borrower's bankruptcy attorney can and should intervene to correct the problem. Chapter 13 Trustees can also be helpful in making sure that mortgage servicers correctly apply HAF funds.

A Number of States Had Success Providing Hardest Hit Funds Relief to Borrowers in Bankruptcy.

A number of states successfully provided Hardest Hit Fund (HHF) assistance to homeowners in an active bankruptcy case. Given the similarities between the HHF and HAF programs, the experiences of program administrators in these states demonstrate that borrowers in bankruptcy can receive funds under this kind of program without legal barriers. The states that allowed homeowners to receive HHF funds while in an active bankruptcy case include at least the following: Arizona, Illinois, Indiana, Michigan, North Carolina, and Rhode Island.

Homeowners in a Chapter 7 Bankruptcy Should Not Be Excluded from HAF Assistance.

Chapter 7 bankruptcy is relatively short process. Typically, a chapter 7 case will last for about 6 months from the bankruptcy filing to the entry of the bankruptcy discharge. In chapter 7 bankruptcy, debtors must disclose to the court all of their assets, debts, income, and expenses. Any assets the debtor owns that exceed the allowed exemptions are sold for the benefit of the creditors. Chapter 7 bankruptcy is most helpful for dealing with unsecured debts like medical and credit card debt. If a borrower is in default on a secured loan like a mortgage or car loan, the creditor's lien will survive the bankruptcy, so the borrower must cure the default in order to avoid repossession of the car or foreclosure on the home.

The bankruptcy court and chapter 7 Trustee oversee the case to ensure that creditors are treated equitably (and that no creditor is being unfairly given preference) and that the debtor is not hiding assets that could be paid over to creditors. Since secured creditors must be paid if the debtor wishes to retain the property, there is no problem with the HAF program administrator making direct payment to the mortgage creditor to cure the mortgage arrears. If the HAF assistance is awarded after the bankruptcy filing date, this money should not be treated as an asset of the borrower, because it arose post-petition. Moreover, because funds will typically be paid directly to the mortgage servicer (and the

borrower will never exercise control over the funds), there is an additional argument that this is not an asset of the bankruptcy estate.

Questions have been raised about whether a borrower in a chapter 7 bankruptcy case can receive assistance to repay utility arrears, which is one allowed purpose for HAF funds. If a HAF program is paying utility arrears on behalf of a borrower in bankruptcy, there may need to be some consideration of whether this is a secured or unsecured debt. In some jurisdictions, municipal water service is secured by a lien by operation of law. If the utility debt is secured, there should be no problem with paying the debt in full despite the pending bankruptcy. If the utility debt is unsecured, a voluntary payment by the debtor after the bankruptcy filing still should be acceptable, but another option would be to simply use the HAF funds to pay the deposit for future utility service (usually equal to two times the average monthly bill), and allow the old account balance to be discharged in the bankruptcy.

Borrowers in Chapter 13 Bankruptcy Should Not Be Excluded from HAF Assistance.

Chapter 13 bankruptcy involves a payment plan in which the debtor pays a required amount over a three to five-year period and only then receives a discharge. Because the chapter 13 plan allows for curing the arrears on a secured debt over that three to five-year period, this is the most common kind of bankruptcy filing by homeowners attempting to save their home from foreclosure.

Similar to a chapter 7 bankruptcy, debtors in a chapter 13 case must disclose to the court all of their assets, debts, income, and expenses. However, in a chapter 13 filing, the creditors are typically paid through the chapter 13 plan payments (from the debtor's disposable income), rather than from the sale of assets.

When a chapter 13 case is filed, the debtor proposes the chapter 13 plan, including how much will be paid to various creditors. A confirmation hearing is scheduled for about 2 months after the case is filed, although confirmation is often postponed several times while the debtor works on addressing any objections from the chapter 13 trustee or creditors and possibly modifying the proposed plan. Regardless of whether a chapter 13 plan has been confirmed or has not yet been confirmed, the approval for HAF funds may be a reason for the debtor to modify the chapter 13 plan. If that is necessary, the debtor's bankruptcy attorney can be expected to handle it.

Program administrators should be able to send HAF funds directly to mortgage servicers. When debtors make their usual chapter 13 plan payments to the chapter 13 trustee, this includes an amount for the mortgage arrears, which are then sent by the chapter 13 trustee to the mortgage servicer. Sometimes the monthly plan payment also includes an amount to cover the prospective mortgage payments that come due during the plan – bankruptcy court districts that require this are known as "conduit" jurisdictions. In either case, chapter 13 trustees can agree to allow a direct payment to the mortgage servicer. Many chapter 13 trustees allowed Hardest Hit Funds (HHF) payments to be sent directly to the mortgage servicer rather than being passed through the trustee's account. This kind of direct payment is likely the best way to handle the HAF funds. The bankruptcy attorney can contact the chapter 13 trustee to inform them of the direct payment being sent. Depending upon the terms of the debtor's confirmed plan, if the HAF assistance paid to the servicer will cure the mortgage arrearage, the debtor may wish to modify the plan.

The only other potential issue in an active chapter 13 case is that court approval is required if the debtor will incur a debt while the bankruptcy case is pending. When HHF assistance was structured as a

forgivable loan, this required bankruptcy court approval. Such approval was easily granted with no opposition, because it was in the best interest of all creditors for the mortgage arrears to be cured in this manner. When HAF assistance is structured as a grant rather than a forgivable loan, the bankruptcy court would not need to approve the chapter 13 debtor's participation in HAF.

How to Ensure that State HAF Programs Work Well for Borrowers in Bankruptcy

States should allow borrowers in bankruptcy to receive HAF assistance, and should follow these steps to smooth the way:

1. **Include a question on the application form about whether the borrower is in an active bankruptcy,** and a statement that, if the answer is yes, the borrower is should inform their bankruptcy attorney that they are applying for program funds. The borrower's bankruptcy attorney is in the best position to take any necessary steps to ensure that funds are handled properly and to deal with any bankruptcy implications.

2. **Communicate with Chapter 13 Trustees**. If there are questions or common issues arising with respect to HAF funds for borrowers in bankruptcy, program administrators could communicate with the Chapter 13 Trustee(s) in the relevant bankruptcy court district (some states have one federal district court, and others have more than one) to find out if they would like to develop a template or common procedure that will be followed when debtors in Chapter 13 bankruptcy are receiving HAF funds.

3. **If servicers send back the funds, escalate the problem**. Servicers should not be sending back money received from HAF programs. If that does happen in a rare occasion early in the program, the servicer needs to be educated about the fact that they can accept this money and must apply it to the mortgage account. Usually the borrower's bankruptcy attorney is the best situated to communicate this, although a Chapter 13 trustee can also help. Unrepresented or "pro se" bankruptcy filers might be able to get free legal assistance with this discrete issue from a legal services program in the area. NCLC is willing to help put any HAF program administrator in touch with a knowledgeable legal services attorney or Chapter 13 Trustee in order to eliminate any friction in this process.

4. **Make sure funds are applied properly**. Servicers should be required to apply the funds to the account properly to bring it current. Both inside and outside of active bankruptcy cases, it is important for state administrators to oversee this process and follow up on any issues.

For more information about these recommendations, please contact Sarah Mancini at smancini@nclc.org, or Alys Cohen at acohen@nclc.org.

UNITED STATES BANKRUPTCY COURT
DISTRICT OF RHODE ISLAND

IN RE: [Debtor's/Debtors' Name(s)], BK No. [XX-XXXXX]

Debtor(s). Chapter

MOTION FOR CONSENT TO APPLY FOR THE HOMEOWNER ASSISTANCE FUND

Debtor(s) [Debtor's/Debtors' names(s)] hereby moves this Court to provide consent for the Debtor(s) to apply for the Homeowner Assistance Fund. In support of this motion the Debtor(s) state(s) the following:

1. The Homeowner Assistance Fund (HAF) was established under section 3206 of the American Rescue Plan Act of 2021. The U.S. Department of the Treasury has allocated fund to the State of Rhode Island to be used to prevent mortgage delinquencies and defaults, foreclosures, and loss of utilities or home energy services. In Rhode Island, the funds will be offered as a grant and can be used concurrently with a loan modification or other workout solutions to help reach an affordable payment.
2. In Rhode Island, The Homeowner Assistance Fund are administered by RIHousing.
3. The Homeowner Assistance Fund is offered as a grant.
4. The events of default, which would trigger repayment, are (i) discovery that grant funds were procured through falsification or fraudulent means; (ii) in the case of monthly payment assistance, the grant recipient ceases to own and occupy the property while receiving ongoing assistance.
5. Because HAF is a grant, obtaining HAF funds will not result in additional monthly expenses for the Debtor(s).
6. RIHousing has requested that applicants with active Bankruptcy cases obtain leave of this Court before applying for the HAF program.
7. Debtor(s) obtaining funds through the HAF program would not cause harm to creditors.

Wherefore, the Debtor(s) requests that this Court give consent for Debtor(s) to apply for the HAF program.

Respectfully submitted,
Debtor(s) [Debtor's/Debtors' name(s)],

_____

Dated: [Month Day, Year] [Signature(s)]

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF NEW YORK
----------x
In re:

Case No. 8-19-71413-reg

Anelia Tcherneva aka
Anelia Tchernev,

Chapter 13

Debtor.
----------x

MEMORANDUM OPINION

This matter is before the Court pursuant to an application ("Application") for compensation filed by the law firm of Lester Kornman Kamran & Masini, P.C. ("Counsel"), which represents Anelia Tcherneva aka Anelia Tchernev ("Debtor") in this confirmed Chapter 13 case. Counsel filed the Application seeking $9,165.00 in attorney's fees for services rendered pre-confirmation, incurred almost exclusively as the result of the Debtor's desire to restructure a residential mortgage with her lender. In furtherance of that goal, the Debtor sought, and the Court granted, an order directing the parties to participate in a process known as loss mitigation. Counsel acknowledges they routinely charge clients a flat fee of $5,500.00 for Chapter 13 cases and charge additional fees for certain services. In this case, Counsel seeks compensation in addition to the flat fee of $5,500.00. Counsel argues the Court should find that the work performed in connection with loss mitigation in this case is not work performed in the ordinary course of a Chapter 13 case and therefore should not be included in the flat fee.

This case presents the Court with several challenges. While the legal issues raised in the Application are not complex and the Bankruptcy Code sections under which fees are awarded to counsel for Chapter 13 debtors are relatively clear, the Application highlights significant issues that this Court has not previously been asked to decide. Why these issues have not been brought

to the Court's attention earlier is a question the Court has for Michael Macco, the Chapter 13 Trustee ("Trustee") and the United States Trustee, but that is for a later date. By way of background, the Court recognizes that much of the work involved in the administration of the Chapter 13 cases is done by the Trustee and other professionals. This Court has written extensively on the challenges of the statute. This Court has on numerous occasions acknowledged the fine work of the Trustee, and many debtors owe their success to his efforts. However, what has developed is a process that has gone astray and we must recognize this fact.

It appears that a de facto "no-look" fee agreement has been implemented between professionals and the Trustee. If the fees sought by counsel to a Chapter 13 debtor exceed an amount the Trustee believes is fair and reasonable, the Trustee directs the attorney to file a fee application. However, if the Trustee and counsel agree on a fee, it is incorporated in a plan and the Trustee then recommends confirmation. While it can be argued the Court, while not conducting a specific hearing, is nonetheless ruling on the requested fees, this was never the intent of the statute and is a process that will cease. The argument for allowing such a procedure is the desire to streamline the confirmation process and reduce costs which is beneficial to the debtor and the creditors. However, the awarding of fees is the sole responsibility of the Court, and because of this fact, the Court will be formally implementing a process to satisfy this requirement and at the same time to continue to meet the Trustee's objective to limit costs. This Court will draft new rules which give counsel to Chapter 13 debtors the option of either proceeding under what we designate a "presumptively reasonable fee" which will allow the Court to award fees without the need for a hearing or filing a fee application. If counsel seeks fees beyond the stated presumptive fee, the request will be reviewed at the time of confirmation. This is explained in more detail herein.

The Court intends to adopt procedures that establish a presumptive fee of $5,500.00. It appears that this is the basic fee currently charged in our District. If there is support for establishing a different presumptive fee the Court will remain open to those arguments. Attorneys that seek a fee of $5,500.00 and submit an affirmation that the work done in the case at the attorney's hourly rate is equal to or less than $5,500.00, the fee will be presumed to be reasonable. Unless directed by the Court, attorneys seeking the presumptive fee will not be required to have a hearing. Attorneys may choose to forego this arrangement and file a fee application for any amount they wish to request and will be required to have a hearing which the Court will conduct under 11 U.S.C. § 330 and 11 U.S.C. § 1325 at the time of confirmation. Only the Court awards fees; no modification of this process will be permitted.

The Court will no longer entertain motions for loss mitigation in Chapter 7 or 13 cases. After a careful review of the history, function, and practices of the loss mitigation program as it is currently practiced, the Court has concluded that the program should cease. Loss mitigation is an administrative process that was needed by debtors and lenders when the mortgage industry itself was in collapse and it was difficult for debtors to identify the party that held the mortgage. The process was born out of necessity and implemented by bankruptcy courts all over the country. Many families kept their homes because the courts recognized a problem and provided a solution. However, it was never intended to become a de facto right or a new form of bankruptcy protection. Today, loss mitigation has morphed into an institutionalized process not supported by the Bankruptcy Code. It now seemingly exists not for the purpose originally intended but rather for the benefit of professionals, trustees, and institutions, often to the economic detriment of the creditors. This is the antithesis of what Chapter 13 was designed to do. The Court will always encourage Chapter 13 debtors and their secured creditors to reach a consensual arrangement,

including mortgage modifications, but this should be, as it always has been, on a voluntary basis between the parties. To be clear, "non-traditional" Chapter 13 cases which are filed solely to participate in the loss mitigation process will be subject to swift motions to dismiss as required by statute. Chapter 13 cases are difficult and many fail. This Court is not intending to punish debtors or counsel who in good faith try and fail in this process. However, the essential point is each case must be filed in good faith.

The Application is granted for the full amount notwithstanding the newly implemented policies. The Court recognizes that this is a confirmed case and Counsel incurred these fees before the Court reexamined its policies. For these reasons, and as more fully set forth below, the Court finds that the fees requested by Counsel are reasonable under 11 U.S.C. § 330.

Procedural History

On February 27, 2019, Debtor filed her petition along with the signed retainer agreement ("Retainer") which provides that for $3,000.00, plus an administrative fee of $2,500.00, and the $310.00 chapter 13 filing fee (for a total of $5,810.00), Counsel would provide certain enumerated services.[1] For an additional charge, Counsel would provide additional services not covered by the $5,810.00 amount.[2]

[1] Those services are the preparation and filing of a Chapter 13 petition, related required filings and plan of reorganization for the Debtor, stopping wage garnishment, providing representation at the initial 341 meeting and any adjournment not caused by Debtor's failure to appear or provide documentation, preparation and filing of any amended plans, representation at the confirmation hearing and any adjournment not caused by Debtor's failure to appear, provide documentation, or be current with payments to the Trustee or any creditor. ECF No. 3.

[2] Additional services include: attending an adjourned 341 or confirmation hearing caused by Debtor, defense of a motion to dismiss or a lift-stay motion due to Debtor's failure to pay mortgage payments, amending schedules to include information the Debtor failed to tell the law firm or failed to accurately disclose, preparation of motions and affidavits in support of the plan, objections to claim, motions to expunge a claim, motions to avoid liens, cramdown motions, contempt motions, and motions to recover an asset. ECF No. 3.

On April 9, 2019, Debtor filed her first Chapter 13 plan which indicated she would be requesting loss mitigation pursuant to the Court's loss mitigation procedures and that unsecured creditors would receive a distribution of not less than two (2) percent. Debtor filed her first motion to enter loss mitigation with respect to the first mortgage on her residence on April 11, 2019, but it was withdrawn the following day.

On April 12, 2019, Debtor filed a second motion to enter loss mitigation seeking to modify the first mortgage on her residence. ECF No. 24. The Court granted the second motion on September 6, 2019. ECF No. 33. That same day Debtor submitted a completed loan modification package to the lender, Fifth Third Bank ("the Bank"). ECF No. 37.

On September 10, 2019, the Court entered an order granting Debtor's motion pursuant to 11 U.S.C. §§ 506 and 1325 to deem the junior mortgage on Debtor's residence unsecured. On February 7, 2020, the Bank reported that Debtor's loan modification application was denied for reasons related to the stripping of the junior mortgage. These issues required an exception review by Freddie Mac and an updated loss mitigation package. ECF No. 42. As a result, Debtor was back at square one six months into the loss mitigation process.

On April 9, 2020, the Bank reported to the Court that Debtor was granted a six (6) month forbearance due to the COVID-19 pandemic. ECF No. 46. In October 2020, the Bank informed Counsel that a new package was required, along with a completed Uniform Borrower Assistance Form. In November of 2020, Debtor submitted another loss mitigation package at the direction of the Bank while the Bank, unbeknownst to either Debtor's counsel or the Bank's counsel, issued a trial modification without the Freddie Mac exception review or extra form, and sent it directly to Debtor's residence. The trial modification scheduled payments for December 2020, January 2021, and February 2021, which the Debtor completed.

On April 29, 2021, Counsel informed the Court that Debtor was still waiting for the final modification documents from the Bank and had followed up on March 23, April 21, and April 26, 2021. Debtor received the final modification documents in June 2021, which Debtor promptly signed and returned. A month later, the Bank signed and returned the fully executed modification documents. The Court entered an order approving the loan modification on August 3, 2021. An order was entered confirming Debtor's plan on August 12, 2021, one month after the expiration of her car lease. As a result, Debtor's counsel was required to bring an emergency motion to obtain funding for a new vehicle rather than simply obtaining financing approval by letter from the Trustee. In this time, Debtor's counsel made eleven (11) loss mitigation appearances, four (4) in-person and seven (7) telephonic.

On August 17, 2021, Debtor's counsel filed the Application. ECF No. 88. The Trustee filed a partial opposition ("Opposition") arguing that Counsel had agreed to represent Debtor for a fee of $5,500.00 plus the filing fee pursuant to the Disclosure of Compensation. ECF No. 91. The Trustee did not find anything in Counsel's time records demonstrating that the work performed was extraordinary or not contemplated under the original fee agreement between Debtor's counsel and Debtor. *Id.* Counsel filed a reply arguing that the Retainer set forth the services covered by the $5,500.00 fee and separately identified each specific, non-standard service which was not covered by the Retainer. ECF No. 93. The Retainer clearly states that loss mitigation is not included in the $5,500.00 fee. At the hearing on the Application, Counsel stated that the plan provided for payment of the attorney's fees from funds left over after payment of a lump sum to the Bank. Those funds were collected and held by the Trustee as proposed mortgage payments pending a final loan modification.

Discussion

The Application itself raises a relatively straightforward issue: should counsel to Chapter 13 debtors be permitted to seek compensation for services related to loss mitigation or should these services be included in the base fee commonly charged in this District? In this case, the plan has been confirmed and the plan itself provides for the payment of these additional fees, if awarded by the Court, from the funds currently held by the Trustee. The Application, arguments, and submissions to the Court have caused the Court to reconsider certain of its practices in Chapter 13 cases. While this decision addresses the Application, the Court will first review the current practice for compensating counsel to Chapter 13 debtors and the Bankruptcy Code requirements for awarding fees to counsel to Chapter 13 debtors. After ruling on the Application, the Court will set forth procedures, which will be implemented shortly, for awarding such fees on a prospective basis. The Court will also explain its rationale for terminating the loss mitigation procedures set forth in its Chambers Rules.

I. Applications for Compensation

Attorneys in this District representing Chapter 13 debtors have adopted a practice of charging debtors $3,000.00 prior to commencement of the case and charging an additional $2,500.00 upon confirmation which is reflected in the confirmed plan. This $2,500.00 fee is paid out over the life of the plan. There is no substantive Court oversight over the award of the fees up to $5,500.00 as the order of confirmation merely includes this as a matter of course. If additional work is performed post-confirmation, counsel will request additional fees in any motion seeking the post-confirmation relief. The Court does not have a procedure for so-called presumptively reasonable or no-look fees. Rather, it is left up to the Trustee to police the attorneys and to determine whether a fee application is required. In most Chapter 13 cases, no fee application is

filed and the bar accepts whatever the Trustee recommends. In this case, Counsel seeks an award in excess of $5,500.00 based on the additional work undertaken in connection with loss mitigation. Because the plan has been confirmed and the Trustee is holding funds sufficient to pay the fees as requested, there is no need in this case to consider the effect this award has on the creditors.

In cases where the plan is not confirmed, the Bankruptcy Code requires the Court to utilize a two-part analysis. First, the Court must determine the reasonableness of the requested fee pursuant to 11. U.S.C. § 330. Second, the Court must analyze the debtor's proposed plan, taking into consideration the allowed amount of fees. The Court must ascertain whether an award of fees as requested would render the plan unfeasible or would deem the plan as not proposed in good faith.

This tension between ensuring that a confirmed plan can be effectuated and the need to pay all administrative claims before unsecured creditors are paid is quite common in Chapter 11 cases. Often, professionals are faced with reducing their fees to facilitate a confirmable Chapter 11 plan. Because professional fees in Chapter 13 cases have historically been relatively low in proportion to proposed distributions, this issue has largely been avoided. However, in recent years this tension has come to the forefront. In this case, Counsel points to the work necessitated to comply with the Court's loss mitigation procedures along with a certain degree of ineptitude on the part of the Bank and its professionals. While the plan has been confirmed in this case, the additional fees requested highlights what takes place in many other Chapter 13 cases in this District.

It is crucial to understanding the Court's reasoning herein to recognize a simple but fundamental aspect of Chapter 13: the debtor commits all disposable income to paying creditors

for generally a five (5) year term. Therefore, any funds going to administrative expenses are deducted from money that would otherwise go to creditors. Chapter 13 was created to require debtors to make some payment to their creditors in return for keeping ownership of property, generally the family residence. Congress recognized the critical role of professionals and provided for their priority payment. However, balancing those objectives is the responsibility of the Court, not the Trustee.

A. 11 U.S.C. § 330

The Court is responsible for determining whether the fees requested are reasonable under 11 U.S.C. § 330. A professional requesting approval of fees and expenses bears the burden to prove that the fees and expenses requested are reasonable. *Continental Ill. Nat'l Bank & Trust v. Charles N. Wooten, Ltd. (In re Evangeline Refin. Co.)*, 890 F.2d 1312, 1326 (5th Cir. 1989); *see also In re King*, 546 B.R. 682, 711 (Bankr. S.D. Tex. 2016) ("[F]or any fees requested under § 330(a), '[t]he applicant bears the burden of proof in a fee application case.'"). "This burden is not to be taken lightly, especially given that every dollar expended on legal fees results in a dollar less that is available for distribution to the creditors or use by [the] debtor." *In re Pettibone Corp.*, 74 B.R. 293, 299 (Bankr. N.D. Ill. 1987).

Section 330(a)(1)(A) of the Bankruptcy Code states that a court may award "reasonable compensation for actual, necessary services rendered by the trustee, examiner, ombudsman, professional person, or attorney and by any paraprofessional person employed by any such person . . . ." To determine the amount of reasonable compensation, § 330(a)(3) directs courts to consider the nature, extent, and value of the services and taking into account several factors, including: (1) the time spent on the services; (2) the rates charged; (3) the necessity of the services to the administration of the case; (4) the benefit of the services towards completion of

the case; (5) the reasonableness of the time spent compared to the complexity, importance, and nature of the problem, issue, or task; (6) board certification of the professional or other demonstrated skill and experience in bankruptcy; and (7) the reasonableness of the compensation based on the customary compensation charged by comparably skilled practitioners.

Section 330(a)(4)(B) permits courts to exercise discretion in awarding compensation for services rendered which benefitted and were necessary for the debtor in Chapter 12 and 13 cases. This is an exception to the rule that services are compensable only if the work benefits the estate. *In re Steen*, 631 B.R. 704, 709 (Bankr. N.D. Tex. 2021). In adding § 330(a)(4)(B) in 1994, Congress recognized that services beneficial to the debtor can facilitate successful *completion* of the plan because the debtor must fund a Chapter 13 plan and success on an issue in the case can determine whether a debtor can continue in Chapter 13. *See id.* at 708–09 (citing *In re Williams*, 378 B.R. 811, 823 (Bankr. E.D. Mich. 2007)); *see also* 5 *Collier on Bankruptcy* ¶ 330.04[1][b][v] (16th ed.); 3 *Collier on Bankruptcy* ¶ 330.03[1][b][v] (16th ed.). Importantly, a successful Chapter 13 case is one where a plan is completed. A Chapter 13 case is not successful where it ends at any earlier stage. *See In re Pappas & Rose, P.C.*, 229 B.R. 815, 819 (W.D. Okla. 1998) ("Failure of a Chapter 13 plan is not reasonably likely to benefit the estate."). In *Williams*, the court first determined whether the services were beneficial to the estate, and if not, then determined whether the serves were reasonably likely to benefit the debtor. *Williams*, 378 B.R. at 826. Counsel should determine the impact of the services and the cost of those services upon the debtor and the plan at the time the services are rendered. *Id.*

Courts typically apply the "lodestar" method in calculating the reasonableness of attorney's fees under § 330. *In re Korean Chosun Daily Times, Inc.*, 337 B.R. 758, 766 (Bankr. E.D.N.Y. 2005) (Stong, J.) (holding that the lodestar method is to be used to determine

reasonable attorney's fees in all federal courts, including bankruptcy courts); *In re Hanover*, No. 8-20-70676-ast, 2020 WL 2554229, at *3 (Bankr. E.D.N.Y. May 19, 2020); *Jackson v. Reed Smith LLP (In re Jackson)*, 630 B.R. 700, 728 (Bankr. D. Conn. 2021). The lodestar method requires multiplying the number of hours reasonably expended by an hourly rate based on the prevailing market rate for attorneys of comparable skill and standing in the relevant legal community. *Hensley v. Eckerhart*, 461 U.S. 424, 433 (1983); *Kerin v. U.S. Postal Serv.*, 218 F.3d 185, 190 (2d Cir. 2000). As discussed later, many bankruptcy courts employ "presumptively reasonable fees" in Chapter 13 cases which presume that a set amount of attorney's fees are reasonable for the work performed. Courts which employ presumptive fees do not regularly review fee applications which fall below the set amount. To date, the Court has not adopted a "presumptively reasonable" fee amount for Chapter 13 cases.

If the Court determines that the fees are reasonable under § 330, it must then determine whether the fees are reasonable in the scheme of the proposed Chapter 13 plan.

B. Confirmability

An award of fees to debtor's counsel cannot be divorced from the Chapter 13 plan process. The amount of allowed administrative claims in a Chapter 13 proceeding is a critical component in analyzing whether a debtor's proposed plan is fair and reasonable and confirmable. Professional fees usually represent the bulk of these administrative claims. Courts cannot forget that the work undertaken by professionals is done in the context of a Chapter 13 case and an unconfirmed case is a failed case. Awarding excessive attorney's fees outside the context of plan confirmation leads to results estranged from the Bankruptcy Code. For example, courts have awarded tens of thousands of dollars attorney's fees based on the reasoning that the attorney performed the work and achieved a desired result for the benefit of the Chapter 13 debtor. While

that may be true, courts must be mindful that the purpose of Chapter 13 is to confirm a plan and then abide by its terms. Excessive attorney's fees should not be awarded where such award contravenes the purposes of Chapter 13.

At confirmation, the Court must independently evaluate the plan utilizing the standards set forth in 11 U.S.C. § 1325(a) and may deny confirmation if a plan does not comply with those requirements.[3] After confirmation, at the end of the plan term, if the debtor has successfully complied with the terms of the plan, the debtor is discharged of his or her personal liability on the remaining debts. Of the requirements of § 1325(a), feasibility and good faith are particularly important.

i. Good Faith

Under § 1325(a)(3), a Chapter 13 plan must be proposed in good faith. While the Bankruptcy Code does not define "good faith," the Second Circuit has found that to ascertain whether a plan was proposed in good faith, a bankruptcy court must determine "whether the debtor has misrepresented facts in his plan, unfairly manipulated the Bankruptcy Code, or otherwise proposed his Chapter 13 plan in an inequitable manner." *Johnson v. Vanguard Holding Corp. (In re Johnson)*, 708 F.2d 865, 868 (2d Cir. 1983) (quoting *Goeb v. Heid (In re Goeb)*, 675 F.2d 1386, 1389–91 (9th Cir. 1982)). Bankruptcy courts also consider whether, "under the 'totality of the circumstances,' the debtor has abused the provisions, purposes, and/or spirit of Chapter 13." *Plagakis v. Gelberg (In re Plagakis)*, No. 03 CV 0728(SJ), 2004 WL 203090, at *4 (E.D.N.Y. Jan. 27, 2004). It is not enough for a debtor to technically comply with

[3] By contrast, in a Chapter 11 case, debtors propose a plan of reorganization (which has similar aims to a Chapter 13 plan) or a plan of liquidation (similar to the purposes of Chapter 7). Creditors may vote to reject a plan wherever they believe the plan is not feasible. Although both Chapter 11 and Chapter 13 provide mechanisms for creditors to voice dissent to proposed plans, Chapter 11 specifically requires the assent of creditors whereas Chapter 13 does not. As a result, the Court plays a larger role when determining whether to confirm a Chapter 13 plan.

the Bankruptcy Code. *In re Renz*, 476 B.R. 382, 390 (Bankr. E.D.N.Y. 2012) (Craig, J.). The debtor must also show that he or she has chosen Chapter 13 "with the purpose of accomplishing the aims and objections of bankruptcy . . . ." *Id.* (quoting *In re Klevorn*, 181 B.R. 8, 10 (Bankr. N.D.N.Y. 1995)).

Several courts have denied confirmation of Chapter 13 plans as not proposed in good faith where attorney's fees paid through a Chapter 13 plan exceeded the amount paid to unsecured creditors. *See, e.g.*, *In re Paley,* 390 B.R. 53, 58–60 (Bankr. N.D.N.Y. 2008); *Ingram v. Burchard*, 482 B.R. 319 (N.D. Cal. 2012); *In re Arlen*, 461 B.R. 550 (Bankr. W.D. Mo. 2011). These kinds of plans, according to those courts, are an abuse of the provisions, purpose, and spirit of the Bankruptcy Code. *See Paley*, 390 B.R. at 58–60. They leave the vast majority of debts unpaid and may be vulnerable to abuse by attorneys seeking to advance their own interests ahead of debtors. *Berliner v. Pappalardo (In re Puffer)*, 674 F.3d 78, 83 (1st Cir. 2012). They are essentially Chapter 7 cases disguised as Chapter 13 cases. *See Paley*, 390 B.R. at 58–60; *In re Brown*, 742 F.3d 1309, 1317–18 (11th Cir. 2014).

However, such plans are not necessarily *per se* in bad faith. There may be the rare case where, considering the totality of the circumstances, it is appropriate to confirm a plan that pays attorneys more than unsecured creditors, but the burden to demonstrate that this kind of plan is justified is heavy. *In re Puffer*, 674 F.3d at 83. Conversely, there may be cases where unsecured creditors are paid more than the attorney's fees but the structure of the plan and the circumstances surrounding the plan weigh against finding good faith.

ii. Feasibility

Under § 1325(a)(6), a Chapter 13 plan must be feasible. That is, the debtor must "be able to make all payments under the plan and comply with the plan." This includes payments for both

administrative expenses and unsecured claims. Debtor's attorney's fees are administrative expenses under § 503(b) which may be paid before or contemporaneously with other creditors under § 1326(b)(1). Where payments of attorney's fees pursuant to § 1326 interfere with the feasibility of the plan, such plans should not be confirmed. *See Shorb v. Bishop (In re Shorb)*, 101 B.R. 185, 187 (B.A.P. 9th Cir. 1989). Courts have noted circumstances where attorney's fees are paid ahead of creditors while collateral decreases in value and, in some instances, the case is dismissed before payments are ever made to creditors. *See In re Tenney*, 63 B.R. 110, 11 (Bankr. W.D. Okla. 1986); *In re Lanigan*, 101 B.R. 530, 533 (Bankr. N.D. Ill. 1986). In those cases, "[w]here plan payments are small and payment of fees out front will delay payments to creditors for many months," there's "no reason . . . why the attorneys who present thinly funded plans should not share in the risk of possible failure thereof and thereby be encouraged to scrutinize all plans even more closely." *Lanigan*, 101 B.R. at 533.

Even where debtor's counsel files a fee application, courts must still evaluate the fee application against the Chapter 13 plan. A fee application may still be denied where the fees requested are in excess of the amounts to be paid to unsecured creditors or are otherwise inequitable compared to the plan provisions for creditors.

II. The Application

This case has already been confirmed and no analysis of the fee application against the confirmability of the Chapter 13 plan is required. Accordingly, the Application will be analyzed against the factors set out in 11 U.S.C. § 330.

Debtor's confirmed plan states that "[t]he balance of the fees owed to the attorney for the debtor(s) is $12,000." Counsel's fee application requests payment of $9,165.00 in fees.[4] Counsel submits that the bulk of the $9,165 in fees were incurred due to the Bank's conduct during the loan modification process. Debtor filed a motion for loss mitigation on April 12, 2019, ECF No. 24. On September 6, 2019, the Court granted the motion. Over the course of over two years, Debtor's counsel attended eleven (11) loss mitigation hearings, in person and telephonically, and submitted two (2) loss mitigation applications.

Debtor's first loan modification application was erroneously denied when the Bank believed the second mortgagee was required to subordinate its lien despite the entry of an order avoiding the second mortgagee's lien. After Debtor's trial loan modification was completed in February 2021, it took an additional four months for Debtor to receive the final loan modification documents and another month for the Bank to sign and return the fully executed documents. Debtor's plan was unable to be confirmed until August 2021 as a result of delays caused by the Bank. The delay also required Debtor's counsel to bring an emergency motion to obtain funding for a new vehicle for Debtor as Debtor's vehicle lease expired the month prior.

Based on the Court's own loss mitigation procedures which apply to this case and the terms of the confirmed plan, Debtor's counsel's fee request is reasonable under § 330 and reflects adherence to those procedures. The Court sees no reason to reduce the fee request and it shall be granted in full.

[4] The Court has already approved the disbursement of $2,500 in attorney's fees from the Trustee which constituted the balance of Counsel's base legal fee pursuant to the retainer agreement between Debtor and Counsel. ECF No. 99.

III. Presumptive Fees

Having ruled on the Application, the Court turns now to the fee award process in Chapter 13 cases on a prospective basis. The issue before the Court with respect to presumptive fees is whether that fee can be absorbed in a plan so that it is confirmable provided there are no other impediments to confirmation. In this Court's view, adopting a presumptive fee does not eliminate the Court's obligations set forth by statute. Rather, it permits the parties to have comfort that the Court will generally not reject a plan otherwise confirmable if the allowed fees are not greater than the presumptive fee.

Presumptively reasonable fees are amounts set by bankruptcy courts which the court expects is sufficient to fairly compensate a skilled attorney in providing routine services in a typical Chapter 13 case. *In re Wesseldine*, 434 B.R. 31, 37 (Bankr. N.D.N.Y. 2010). Presumptively reasonable fees assume that most Chapter 13 cases share common elements, for example, involving secured debt on homes and vehicles, debtors facing home foreclosure, or owing taxes to state, federal, and local governments. *See id.* at 38.

Courts that use presumptively reasonable fees believe they are a method for streamlining Chapter 13 cases for the court and for counsel. According to those courts, presumptively reasonable fees do not do away with the requirements of 11 U.S.C. § 330 nor do they eliminate the court's responsibility to review the reasonableness of attorney's fees. *In re Beale*, 553 B.R. 69, 80 (Bankr. E.D Va. 2016); *In re Debtor's Attorney Fees in Chapter 13 Cases*, 374 B.R. 903, 908–09 (Bankr. M.D. Fla. 2007); *Sikes v. Crager (In re Crager)*, 691 F.3d 671 (5th Cir. 2012). The specific circumstances of a case may cause a court to order an itemized fee application and to perhaps reduce the amount of attorney's fees to be awarded. *Beale*, 554 B.R. at 81. For example, attorneys who routinely charge the maximum flat fee allowed regardless of the

complexities of each case and provide the bare minimum of services required by Chapter 13 cases run afoul of their ethical obligations and may find their fees disgorged. *See Wesseldine*, 434 B.R. at 39. A court may also suspend presumptively reasonable fees as to a particular attorney if circumstances warrant as part of its duty to review compensation for reasonableness under 11 U.S.C. § 330. *Beale*, 554 B.R. at 81.

The utility of presumptively reasonable fees is persuasive and this Court will formally implement a procedure to allow presumptively reasonable fees. The Court will not require a hearing for fees at or below $5,500.00 in Chapter 13 cases if an attorney opts into this arrangement and affirms that the services performed and the time spent performing those services are commensurate with the fee requested. That is, the Court will presume that upon the attorney's affirmation of the work done, fees that are less than or equal to $5,500.00 as of the hearing on confirmation of the Chapter 13 plan are reasonable. Attorneys may choose to forego this arrangement and file a fee application for any amount of fees which the Court will review under 11 U.S.C. § 330 and 11 U.S.C. § 1325 at the time of confirmation. This procedure properly vests the duty to review attorney's fees with the Court. The Court may request a full fee application, including detailed time records, and conduct a full analysis of the fee application even where an attorney has chosen to accept a presumptively reasonable fee.

IV. Loss Mitigation

What makes Chapter 13 particularly enticing to even those who could qualify for the more straight-forward Chapter 7 bankruptcy is the prospect of saving the family home. Where in a Chapter 7 case the trustee is vested with the power to sell the debtor's residence and use the proceeds to pay creditors, in a Chapter 13, the debtor has the power to delay full repayment of mortgage arrears for up to 60 months and reinstate the mortgage by continuing to make post-

petition mortgage payments, resulting in the debtor being allowed to remain in the home. Over the past decade, due to the fallout from the mortgage crisis and problems uncovered in the mortgage lending process, debtors sought home mortgage restructurings. Upon a successful restructuring, the debtor would file a motion to approve a loan modification with the Bankruptcy Court which the Court may approve by order. This was a formal process undertaken on a case-by-case basis between borrower and lender. The Court's only role into the process was approval of the loan modification. Because of the collapse of many institutions in the early part of this century it was difficult for debtors to communicate with anyone of authority to negotiate a modification. To facilitate this many bankruptcy courts instituted procedures to assist debtors. This was always a temporary administrative solution. There is nothing in the Code which permits a bankruptcy court to forcibly restructure a residential mortgage.

In 2009, certain judges in this District adopted loss mitigation procedures in response to the 2008 housing crisis.[5] Gen. Order No. 676 (amending general orders nos. 543 and 582). The purpose was to "facilitate[ing] consensual resolutions for individual debtors whose real property is at risk of loss to foreclosure." *Id.* While the aim of the loss mitigation program is noble, the circumstances that led to its implementation are now absent. Last year, total bankruptcy filings fell twenty-four (24) percent from the previous year with a twenty-four (24) percent decrease in

[5] Several other bankruptcy courts similarly adopted loss mitigation procedures in the wake of the 2008 housing crisis. *See In re Sosa*, 443 B.R. 263, 265 (Bankr. D.R.I. 2011) for a discussion of the impetus for establishing loss mitigation procedures in the Rhode Island bankruptcy court and other courts. Under this Court's loss mitigation procedures, debtors must file and serve a motion requesting the Court to direct the debtor and creditor into loss mitigation. During loss mitigation, a creditor may contact the debtor directly and may not file a lift-stay motion except where necessary to prevent irreparable injury. The time to object to confirmation is extended to a date fourteen (14) days following the loss mitigation period. The loss mitigation period is set by the bankruptcy court in the loss mitigation order. The period can be extended by agreement of the parties or by filing a request with the court. Loss mitigation can be terminated before the period ends on request of a party to loss mitigation. A case cannot be dismissed during the loss mitigation period except upon motion of the Chapter 13 trustee or U.S. Trustee or the voluntary request of the debtor. A resolution or settlement reached during loss mitigation is subject to court approval.

consumer filings, due to government relief programs, moratoriums, lender deferments, and low interest rates. *Total Bankruptcy Filings Drop 24 Percent in Calendar Year 2021, Commercial Chapter 11s Down 48 Percent*, Am. Bankr. Inst. (Jan. 7, 2022), https://www.abi.org/newsroom/press-releases/total-bankruptcy-filings-drop-24-percent-in-calendar-year-2021-commercial. In grappling with the effects of an unprecedented pandemic, Congress passed legislation which addressed mortgage defaults and evictions by providing relief for those falling behind on mortgages and rent as the result of COVID-19. Congress could have added court-ordered loss mitigation to the Bankruptcy Code, but it did not.

The onslaught of foreclosures and bankruptcy filings that necessitated a broad program directing mortgage lenders to the table to negotiate modifications with debtors has abated. Slowly, Chapter 13 has morphed into the pursuit of loss mitigation as its sole purpose in which debtors file cases they never intend to bring to confirmation. These cases are dismissed prior to confirmation, and if they do reach confirmation, the debtors make initial plan payments which repay attorney's fees and then payments stop, leading to unopposed dismissals. Meanwhile, attorneys exclude loss mitigation services from their retainer agreements and rack up additional fees beyond the initial retainer amount and expect these fees get paid out of the plan or other funds held by the Chapter 13 trustee. Attorneys for the mortgagees benefit regardless of whether loss mitigation is successful because they are also getting paid their attorney's fees for simply being a part of the process. The result is that unsecured creditors essentially pay for debtors to retain counsel for loss mitigation without getting paid themselves. This violates the purposes of Chapter 13.

Additionally, the Court has no legal authority under the Bankruptcy Code to enforce the loss mitigation program. Courts have justified these programs by finding they have an inherent

power to manage their dockets under 11 U.S.C. § 105(a) which authorizes courts to implement orders or rules. *See, e.g.*, Hon. Cecelia G. Morris and Mary K Guccion, *The Loss Mitigation Program Procedures for the United States Bankruptcy Court for the Southern District of New York*, 19 Am. Bankr. Inst. L. Rev. 1 (2011). However, the Court finds no authority in § 105(a) or elsewhere to establish a loss mitigation program as it is currently used by debtors. The Court will not read into § 105(a) rights or powers which do not exist in the bankruptcy code. *See U.S. v. Farrell (In re Farrell)*, 241 B.R. 348, 349 (Bankr. M.D. Pa. 1999); *Martelloni v. Martelloni (In re Martelloni)*, No. 12-75072-ast, Adv No. 12-8437-ast, 2013 WL 5873264, at *6 (Bankr. E.D.N.Y. Oct. 31, 2013) (Trust, J.); *In re Barney's, Inc.*, 197 B.R. 431, 438 (Bankr. S.D.N.Y. 1996) "Section 105(a) is not a license to judicially legislate perceived shortcomings in existing law," *Farrell*, 241 B.R. at 349, nor does it "constitute a roving commission to do equity," *New England Dairies, Inc. v. Dairy Mart Convenience Stores, Inc. (In re Dairy Mart Convenience Stores, Inc.)*, 351 F.3d 86, 92 (2d Cir. 2003) (quoting *United States v. Sutton*, 786 F.2d 1305, 1308 (5th Cir. 1986)).

The Court views the loss mitigation program to be akin to court-ordered mediation, which the Court grants sparingly and only on consent of the parties. Parties may continue to submit motions for approval of loan modifications negotiated outside any formal court-sanctioned process. Likewise, parties may continue to request court-ordered mediation on any issue with consent the parties, but this Court will no longer entertain loss mitigation motions in Chapter 13 cases.[6]

The present application for compensation by Debtor's counsel is an example of the issues the loss mitigation program has created in this Court. It will be the last application for

[6] This Court will also no longer entertain loss mitigation motions in Chapter 7 cases. This decision does not modify, amend, or limit loss mitigation procedures for any other judge in this Court or the Court generally.

compensation this Court approves which seeks additional fees for loss mitigation absent extraordinary circumstances.

Conclusion

The Court finds Counsel's attorney's fees reasonable under § 330. The Application is granted for the full amount requested. The Court also finds it appropriate to allow attorneys to opt into a presumptively reasonable fee in Chapter 13 cases. With respect to cases before this Court, the Court will no longer entertain motions for loss mitigation in Chapter 7 or 13. Formal procedures regarding the compensation of counsel for debtors in Chapter 13 cases will be released in the coming weeks.

Dated: Central Islip, New York
February 28, 2022

Robert E. Grossman
United States Bankruptcy Judge

This document has been electronically entered in the records of the United States Bankruptcy Court for the Southern District of Ohio.

IT IS SO ORDERED.

Dated: April 1, 2022

Beth A. Buchanan
Beth A. Buchanan
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF OHIO
WESTERN DIVISION

In Re	)	
	)	
MONICA M. MORNINGSTAR	)	**Case No. 19-13676**
	)	**Chapter 13**
Debtor(s)	)	**Judge Buchanan**
	)	
	)	

ORDER APPLYING RULE 7023 PROCEDURES TO DEBTOR'S MOTION TO DETERMINE MORTGAGE PAYMENT PURSUANT TO FRBP 3002.1(b), FOR ESCROW ACCOUNT RECONCILIATION, FOR WAIVER OF UNNOTICED ESCROW CHARGES OR REFUND OF ESCROW SURPLUS, AND FOR DISGORGEMENT OF UNNOTICED FEES, COSTS, OR CHARGES PURSUANT TO FRBP 3002.1(c) WITH CLASS ACTION ALLEGATIONS [Docket Number 33]

This matter is before this Court on Debtor Monica Morningstar ("Debtor")'s request to apply Federal Rule of Bankruptcy Procedure ("Rule") 7023 to the issues raised in *Debtor's Motion to Determine Mortgage Payment Pursuant to FRBP 3002.1(b), for Escrow Account Reconciliation, for Waiver of Unnoticed Escrow Charges or Refund of Escrow Surplus, and for Disgorgement of Unnoticed Fees, Costs, or Charges Pursuant to FRBP 3002.1(c) with Class Action Allegations* [Docket Number 33] (the "Motion"). This Court has further considered the

briefs filed by Debtor and Creditor NewRez LLC d/b/a Shellpoint Mortgage Servicing ("Shellpoint") in support of their positions on the application of Rule 7023 to this matter [Docket Numbers 82, 89 and 93]. Upon review of the Motion and briefs, this Court concludes that the factual background and legal analysis necessary for determination is adequately set forth by the parties and the matter is ripe for determination

I. FACTUAL AND PROCEDURAL BACKGROUND

In the Motion, the Debtor asserts that Shellpoint, her mortgage servicer, failed to file and serve notices in her bankruptcy case required by Rule 3002.1(b) and (c) for disclosure of mortgage-related fees or expenses and mortgage-related payment changes. Specifically, Shellpoint's alleged violations include: 1) failing to file and serve notices when the Debtor's mortgage payment changed due to changes in escrow expenses [Docket Number 33, pp. 2-3]; and 2) failing to file and serve notices for the collection of a late payment fee and property inspection fees during the Debtor's bankruptcy case [*Id*., p. 5]. The Debtor requests damages or sanctions for these violations but also asserts that Shellpoint's lack of compliance with Rule 3002.1 may be widespread. Accordingly, and in addition to other relief, the Debtor requests that this Court exercise its discretion to apply Rule 7023's class action provisions to this contested matter.

On September 30, 2021, the Debtor's Motion was partially granted on a default basis by this Court's order determining that Shellpoint failed to file notices in the Debtor's case required by Rule 3002.1(b) and/or (c) [Docket Number 52]. In the order, this Court noted the need to set a damages hearing to determine the appropriate relief to be awarded the Debtor pursuant to Rule 3002.1(i) but also the need to address the Debtor's request to apply Rule 7023's class action provisions [*Id*.].

Following a preliminary hearing and status conference held on October 21, 2021, this Court set a briefing schedule for the parties to address the following issue:

> . . . whether this Court should exercise its discretion to apply Rule 7023 in this contested matter. In particular, the parties should address in their briefs whether class procedures are superior to non-class procedures with respect to the contested matter at issue, whether class certification would be legally impossible such that it would be futile to apply Rule 7023, and any other relevant considerations. *See e.g.*, *In re Biery*, 2014 Bankr. LEXIS 1603, 2014 WL 1431947 (Bankr. E.D. Ky. April 14, 2014).

[Docket Number 74]. The Debtor and Shellpoint subsequently filed briefs [Docket Numbers 82, 89 and 93].

In her brief, Debtor asserted that systemic violations of Rule 3002.1 have occurred among national mortgage servicers such that, in December of 2020, the United States Department of Justice's Trustee Program ("USTP") announced agreements reached with three large national mortgage servicers for servicing deficiencies impacting homeowners in bankruptcy [Docket number 82, Ex. 8]. According to the press release, the deficiencies, impacting more than 60,000 debtor accounts, included the failure to file timely and accurate notices of changes in debtors' mortgage payments, the failure to file timely and accurate notices of mortgage-related fees assessed during bankruptcy cases, and the failure to provide accurate final accountings. The agreements with the USTP resulted in more than $74 million in refunds, waivers, and credits recovered and the three mortgage servicers were required to implement improvements to their internal bankruptcy operations to prevent recurrence.

Although Shellpoint was not one of the mortgage servicers subject to these agreements, Debtor's counsel cites four other local cases in which he was debtor counsel involving allegations that Shellpoint violated Rule 3002.1 [*Id.*, p. 4].[1] Debtor counsel asserts that Shellpoint was

[1] The four cases in this district cited by the Debtor include *In re James*, Case Number 18-11778, Docket Number 74; *In re Christmon*, Case No. 14-15073, Docket Numbers 132 and 138; *In re Dunn*, Case Number 15-11789, Docket

prompted to fix its errors only after actions taken by the debtors in each case. Because Rule 3002.1 errors are difficult to catch without a review and understanding of a mortgage servicer's escrow accounting and because the amount of damages in each case is low, the Debtor asserts that a class action is the superior method to address these errors and ensure that corrective measures are taken to prevent them in the future. Accordingly, the Debtor requests that this Court apply Rule 7023 to allow "similarly situated debtors from across the Southern District of Ohio to vindicate their rights in a uniform way while recovering damages they may otherwise have foregone" [*Id*., p. 10].

II. LEGAL ANALYSIS

The Debtor requests application of Rule 7023's class action provisions to the issues raised in the Motion and, more specifically, to allegations that Shellpoint has violated Rule 3002.1 by failing to file and serve required notices of mortgage payment changes and mortgaged-related fees and expenses. Both Shellpoint and Debtor agree that the language of Rule 9014 gives this Court broad discretion to apply adversary proceeding rules, including Rule 7023, to contested matters at any point in the proceedings. Fed. R. Bankr. P. 9014(c); s*ee also In re Biery*, 2014 Bankr. LEXIS 1603, at *11-13, 2014 WL 1431947, at *4-5 (Bankr. E.D. Ky. April 14, 2014). Thus, the only issue is whether this Court *should* exercise that discretion in this particular case.

In determining whether to apply Rule 7023's class action procedures to a contested matter, the proper inquiry focuses on "whether class procedures are superior to non-class procedures with respect to the contested matter at issue." *Biery*, 2014 Bankr. LEXIS 1603, at *17, 2014 WL 1431947, at *6. Upon review of the parties' filings, this Court determines that the Debtor has set forth a sufficient basis to apply Rule 7023 to this contested matter and allow pre-certification discovery to proceed.

Number 83; and *In re Fleetwood*, Case No. 18-13959, Docket Numbers 70 and 85. This Court makes no findings or determinations with respect to the allegations of violations in these cases.

First, the Debtor has demonstrated that allowing discovery to proceed has the potential to uncover widespread violations of Rule 3002.1. This rule was adopted in 2011 to address the problem caused by mortgage creditors failing to provide notice to debtors of mortgage-related payment changes and other fees and expenses during their chapter 13 cases and then seeking to foreclose after the cases end. *Trevino v. HSBC Mortg. Servs., Inc. (In re Trevino)*, 615 B.R. 108, 128 (Bankr. S.D. Tex. 2020); *In re Tollstrup*, 2018 Bankr. LEXIS 767, at *9, 2018 WL 1384378, at *3 (Bankr. D. Or. March 16, 2018). Rule 3002.1 was adopted in an attempt to solve this problem "by providing a procedure for notice to be provided by a creditor for mortgage payment changes during a chapter 13 case, and an opportunity for the debtor to contest them[.]" *Trevino*, 615 B.R. at 128.

While Rule 3002.1's notice requirements were intended to ensure an end to surprise fees and changes in mortgage payments during a debtor's chapter 13 case, compliance with these requirements has been an ongoing issue for some mortgage servicers. As noted in the Debtor's brief, systemic violations of Rule 3002.1 by three large mortgage servicers resulted in a settlement with the USTP involving millions in recovered refunds, waivers, and credits. Although Shellpoint was not one of the nationwide mortgage servicers subject to the settlement, Debtor counsel cites four cases in this district, in addition to the Debtor's own case, with allegations of Rule 3002.1 violations by Shellpoint. Shellpoint argues that no determinations were made in the four other cases cited by the Debtor and, moreover, five cases is not evidence of routine or systemic violations by this mortgage servicer. But Shellpoint's argument begs the question: how would widespread violations be uncovered without allowing pre-class certification discovery to proceed? Based on the five cases cited by the Debtor, it is reasonable to believe that pre-certification discovery could uncover additional cases in this district involving the types of accounting irregularities and missed

notices that may make a class action appropriate. This factor supports applying Rule 7023 procedures to this contested matter.

Second, the Debtor has demonstrated that applying class procedures may enhance the chance that violations of Rule 3002.1 that are discovered will be adjudicated. *See Biery*, 2014 Bankr. LEXIS 1603, at *17-19, 2014 WL 1431947, at *6. In *Biery*, the bankruptcy court noted that class action procedures are superior in matters where damages in each individual case are limited or nominal reducing the incentive for individual debtors to expend the costs and time to litigate. *Id*. (determining class action procedures to be superior in an action for contempt for violation of the discharge injunction when the relatively small amount of compensatory damages in each case would not justify individual suits). Although this matter involves Rule 3002.1 violations rather than violations of the discharge injunction, the Debtor has noted that relief may be similarly limited. As an example of these limits, the Debtor notes that Shellpoint has calculated the damages in the Debtor's case to be $408.32 [*See* Docket Number 82, p. 8 *citing* Docket Number 41, Ex. A]. *See also Blanco v. Bayview Loan Servicing, LLC (In re Blanco)*, 633 B.R. 714, 755 (Bankr. S.D. Tex. 2021) (suggesting that the Rule 3002.1 noticing violations for small fees and charges may either go unnoticed by debtors or debtors may find it easier to pay the small fees rather than litigate them). Based on the limited incentive to pursue such small amounts individually, this factor weighs in favor of applying Rule 7023 in this matter.

Even with these factors weighing in its favor, application of the rule should be denied if class certification is legally impossible so that application of Rule 7023 would be futile. *Biery*, 2014 Bankr. LEXIS 1603, at *21, 2014 WL 1431947, at *7. Shellpoint argues that class certification is impossible with respect to its alleged Rule 3002.1 violations for several reasons: 1) that Rule 3002.1 is procedural in nature and does not provide a substantive cause of action; 2) that

this Court lacks jurisdiction over a class of debtors whose proceedings would not affect this Debtor or her bankruptcy estate; and 3) that the Debtor's proposed class will be uncertifiable because it will amount to a "fail-safe class" or will otherwise fail to meet a Rule 7023 requirement for certification. This Court will address each argument in turn.

First, Shellpoint argues that Rule 3002.1 is procedural in nature and does not provide substantive relief to a debtor in the form of compensatory and/or punitive damages. Shellpoint argues that violations of a procedural rule cannot form the basis of a class action.

Rule 3002.1(i) describes the relief afforded for a creditor's failure to file and serve proper Rule 3002.1 notices. Specifically, this provision provides that the bankruptcy court, after notice and hearing, may preclude the creditor from presenting the omitted information as evidence or may "award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure." Fed. R. Bankr. P. 3002.1(i). Whether the "appropriate relief" available under Rule 3002.1(i) includes compensatory damages or punitive sanctions is the subject of considerable recent dispute. *See PHH Mortg. Corp. v. Sensenich (In re Gravel)*, 6 F.4th 503 (2nd Cir. 2021) (the majority opinion and dissent set forth the conflicting views regarding whether Rule 3002.1(i)'s language "other appropriate relief" authorizes punitive sanctions); *Blanco*, 633 B.R. at 754-55 (agreeing with the dissent in *Gravel* that the plain language of Rule 3002.1(i) provides courts with significant latitude in awarding compensatory relief or punitive sanctions); *Beiter v. Chase Home Fin., LLC (In re Beiter)*, 590 B.R. 446, 456 (Bankr. S.D. Ohio 2018) (reserving for a later determination whether punitive sanctions may be imposed for violations of Rule 3002.1); *Tollstrup*, 2018 Bankr. LEXIS 767, at *11-13, 2018 WL 1384378, at *5-6 (concluding that Rule 3002.1(i) is a procedural rule that does not permit a monetary award as either compensatory damages or punitive sanctions).

At this preliminary stage, however, it is unnecessary to determine the outer limits of the relief that may be afforded under Rule 3002.1(i). It suffices to note that class actions have been utilized to address creditor violations of similar bankruptcy rules and have been permitted for purposes other than monetary damages. *See generally, Rodriguez v. Countrywide Home Loans, Inc. (In re Rodriguez),*695 F.3d 360 (5th Cir. 2012) (affirming bankruptcy court's certification of class action for injunctive relief against mortgage servicer for alleged violations of Federal Rule of Bankruptcy Procedure 2016(a) by charging fees without court approval and misapplying chapter 13 plan payments to satisfy some of the unauthorized fees); *In re Sheffield v. HomeSide Lending, Inc. (In re Sheffield),* 281 B.R. 24 (Bankr. S.D. Ala. 2000) (certifying class action for creditor's alleged failure to satisfactorily disclose post-petition, pre-confirmation attorney fees included in its proofs of claim). Accordingly, certification is not impossible in this respect.

This Court further rejects Shellpoint's argument that certification is rendered impossible because this Court lacks jurisdiction over multi-debtor class actions. Various courts, including a bankruptcy court within this district, have concluded that they have jurisdiction over multi-debtor class actions, at least with respect to debtors whose cases are filed in the same district. *Wilborn v. Wells Fargo Bank (In re Wilborn),* 609 F.3d 748, 754 (5th Cir. 2010); *Rodriguez v. Countrywide Home Loans, Inc.*, 421 B.R. 341, 354-55 (S.D. Tex. 2009); *Kilbourne v. CitiMortgage, Inc. (In re Kilbourne),* 555 B.R. 628, 633 (Bankr. S.D. Ohio 2015) (concluding that the bankruptcy court had jurisdiction over a class of debtors filing for chapter 13 bankruptcy in the Southern District of Ohio); *In re Biery*, 543 B.R. 267, 302 (Bankr. E.D. Ky. 2015) (certifying a class of district-wide debtors with respect to a contempt proceeding). Indeed, "class action proceedings are expressly allowed in the Federal Bankruptcy Rules" and "if bankruptcy court jurisdiction is not permitted over a class action of debtors, Rule 7023 is virtually read out of the rules." *Wilborn*, 609 F.3d at

754 (noting that the creditor's argument would restrict a bankruptcy court's class certification authority to a proposed class of creditors rather than debtors and that neither the Bankruptcy Code or Rules provided such an express limitation). Because the Debtor has expressly stated that the potential class will be limited to debtors who filed their cases in the Southern District of Ohio [Docket Number 82, p. 10], certification is of a multi-debtor class is possible.

Lastly, Shellpoint argues that class certification will be impossible because the putative class is a "fail-safe class" meaning that the class is defined in terms of the ultimate question of liability or entitlement to relief so that "[e]ither the class members win or, by virtue of losing, they are not in the class and, therefore, not bound by the judgment." *See Randleman v. Fidelity Nat'l Title Ins. Co.*, 646 F.3d 347, 352 (6th Cir. 2011) (noting that an improper fail-safe class is an independent ground for denying class certification). Alternatively, Shellpoint argues that certification of a class will be impossible because the Debtor will be unable to meet the commonality requirement under Rule 7023(a) or, if certifying under Rule 7023(b)(3), the predominance requirement. *See, e.g., Wilborn*, 609 F.3d at 755-57; *Gawry v. Countrywide Home Loans, Inc*. 640 F. Supp.2d 942, 951-52 (N.D. Ohio 2009), *aff'd*, 395 F. App'x 152 (6th Cir. 2010) (concluding that where extensive factual inquiries are required to determine whether an individual is a member of a class, certification under Rule 23(b)(3) is improper). Certainly, Shellpoint's arguments highlight hurdles that the Debtor may face when attempting to certify a class. However, difficulty is not the same as impossibility which is the limited issue to be addressed at this preliminary stage when the precise scope of the Debtor's putative class remains to be determined. It is neither appropriate to define the class at this time nor determine whether the Debtor will ultimately meet the requirements to certify a class both of which will largely depend on what is

uncovered once the parties have an opportunity for pre-certification discovery.[2] Because Shellpoint's arguments do not support that certification is impossible, and recognizing that pre-class discovery is liberally granted, *see Biery v. Beneficial Kentucky, Inc. (In re Biery)*, 2013 Bankr. LEXIS 3622, at *4, 2013 WL 4602698, at *1 (Bankr. E.D. Ky. Aug. 29, 2013), this Court concludes that the Debtor has set forth a sufficient basis to apply Rule 7023 to this contested matter and allow pre-certification discovery to proceed.

For these reasons, this Court will grant the Debtor's request to apply Rule 7023 to the issues raised in Debtor's *Motion to Determine Mortgage Payment Pursuant to FRBP 3002.1(b), for Escrow Account Reconciliation, for Waiver of Unnoticed Escrow Charges or Refund of Escrow Surplus, and for Disgorgement of Unnoticed Fees, Costs, or Charges Pursuant to FRBP 3002.1(c) with Class Action Allegations* [Docket Number 33].

SO ORDERED.

Distribution List:

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[2] Shellpoint further argues that permitting a class action to proceed will only complicate and delay what are otherwise simple procedures under Rule 3002.1 for dealing with post-petition mortgage payment changes, fees and expenses. The Debtor counters that providing a uniform remedy for similarly situated debtors will not delay these cases and missed notifications of payment changes, fees and expenses may never be uncovered without permitting pre-certification discovery to proceed. At this preliminary stage, Shellpoint's arguments remain speculative and are best raised if and when the Debtor seeks to certify a class.

Positive

As of: April 12, 2022 6:43 PM Z

Bivens v. NewRez LLC (In re Bivens)

United States Bankruptcy Court for the Middle District of North Carolina, Durham Division

March 25, 2021, Decided

Bankruptcy Case No. 14-80841, Chapter 13, AP No. 20-09018

Reporter

625 B.R. 843 *; 2021 Bankr. LEXIS 746 **; 2021 WL 1159878

IN RE: Wendy Bivens, Debtor.Wendy Bivens, Plaintiff, v. NewRez LLC f/k/a New Penn Financial, LLC and d/b/a Shellpoint Mortgage Servicing and CitiMortgage, Inc., Defendants.

Prior History: *Bivens v. NewRez LLC (In re Bivens), 2021 Bankr. LEXIS 532, 2021 WL 863343 (Bankr. M.D.N.C., Mar. 2, 2021)*

Core Terms

automatic stay, alleges, Notice, Mortgage, confirmed, misapplied, motion to dismiss, receive payment, charges, ongoing, expenses, arrearage, holder, prepetition, asserts, cause of action, monthly payment, transferred, injunction, contends, inflated, damages, monthly

Case Summary

Overview

HOLDINGS: [1]-A creditor's *Fed. R. Civ. P. 12(b)(6)* motion to dismiss a debtor's complaint was denied because the debtor sufficiently alleged a violation of the *11 U.S.C.S. § 524(i)* discharge injunction by failing to correctly credit payments received under the confirmed plan since the debtor sufficiently alleged that the creditor's action was willful and that he was injured due to the demand of post-discharge payments of amounts that had already been paid during the Chapter 13 plan; [2]-The debtor also sufficiently alleged a claim for sanctions for violation of the automatic stay under *11 U.S.C.S. § 362(k)* because the alleged misapplication of Chapter 13 plan payments stated violation of the automatic stay claim; [3]-In addition, the debtor's complaint sufficiently alleged violation of *Fed. R. Bankr. P. 3002.1(c)*, warranting imposition of Rule 3002.0(i) sanctions.

Outcome

Motion denied.

LexisNexis® Headnotes

Bankruptcy Law > Procedural Matters > Adversary Proceedings > Defenses & Objections

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Pleadings > Complaints > Requirements for Complaint

HN1[] Adversary Proceedings, Defenses & Objections

Fed. R. Civ. P. 12(b)(6), made applicable in a bankruptcy proceeding via Fed. R. Bankr. P. 7012, provides that a complaint should be dismissed if it fails to state a claim upon which relief can be granted. Fed. R. Civ. P. 12(b)(6). To satisfy this pleading standard, the complaint must allege facts sufficient to state a plausible claim for relief. A claim is plausible if the plaintiff pleads facts that allow the Court to reasonably infer that the plaintiff is entitled to his sought-after relief. To determine plausibility, all well-pled facts set forth in the complaint are taken as true and viewed in a light most favorable to the plaintiff. Legal conclusions, elements of a cause of action, and bare assertions devoid of further factual enhancement will not constitute well-pled facts necessary to withstand a motion to dismiss. In addition, if the complaint lacks an allegation regarding an element necessary to obtain relief, dismissal is proper under Rule 12(b)(6). A plaintiff must allege facts sufficient to state each element of his claim in order to survive a Rule 12(b)(6) motion to dismiss.

Bankruptcy Law > ... > Bankruptcy > Discharge & Dischargeability > Effect of Discharge

Evidence > Burdens of Proof > Allocation

HN2[] Discharge & Dischargeability, Effect of Discharge

There are two requirements that must be met to establish a violation of 11 U.S.C.S. § 524(i): (1) a willful failure to credit payments received under a confirmed plan and (2) material injury to the debtor.

Bankruptcy Law > ... > Bankruptcy > Discharge & Dischargeability > Effect of Discharge

Bankruptcy Law > Individuals With Regular Income > Plans > Plan Contents

HN3[] Discharge & Dischargeability, Effect of Discharge

As to the first requirement to establish a violation of 11 U.S.C.S. § 524(i), in the context of § 524(i), willfulness only requires that the creditor intended to apply the payments received in the manner it applied them. Willfulness does not require bad faith nor a specific intent to violate the Code or plan provisions.

Bankruptcy Law > ... > Bankruptcy > Discharge & Dischargeability > Effect of Discharge

Bankruptcy Law > ... > Types of Claims > Secured Claims & Liens > Rights of Secured Creditors

HN4[] Discharge & Dischargeability, Effect of Discharge

As to the second requirement to establish a violation of *11 U.S.C.S. § 524(i)*, a material injury to the debtor, this will be met in virtually every case involving a secured creditor, because the failure to properly credit payments will almost always result in a higher payoff balance for the debtor and therefore a larger lien on the debtor's property than if the payments were credited properly.

Bankruptcy Law > Individuals With Regular Income > Plans > Plan Contents

HN5[] **Plans, Plan Contents**

Where a creditor misapplies payments under a confirmed plan and then transfers the account with records showing an incorrect payment history and inflated loan balance, causing injury to the plaintiff, that those actions could constitute a violation of *11 U.S.C.S. § 524(i)*.

Bankruptcy Law > ... > Automatic Stay > Violations of Stay > Damages

Evidence > Burdens of Proof > Allocation

HN6[] **Violations of Stay, Damages**

To support an *11 U.S.C.S. § 362(k)* claim for violation of the automatic stay, a movant must show 1) that there was a violation of the automatic stay, 2) that the violation was willful, and 3) that actual damages resulted from the violation.

Bankruptcy Law > Individuals With Regular Income > Plans > Payments Under Plan

HN7[] **Plans, Payments Under Plan**

Misapplication of chapter 13 plan payments is a cause of action for violation of the automatic stay. There is no violation of the automatic stay if the erroneous bookkeeping entries are "in no manner communicated to the debtor, the debtor's other creditors, the bankruptcy court, or any third party.

Bankruptcy Law > ... > Automatic Stay > Violations of Stay > Contempt Actions

HN8[] **Violations of Stay, Contempt Actions**

To constitute a willful violation of the automatic stay, a creditor need only commit an intentional act with knowledge of the automatic stay.

Bankruptcy Law > Individuals With Regular Income > Plans > Plan Contents

HN9[] **Plans, Plan Contents**

Fed. R. Bankr. P. 3002.1(a) states that the noticing requirements of *Rule 3002.1(c)* apply in a chapter 13 case to claims (1) that are secured by a security interest in the debtor's principal residence and (2) for which the plan provides that either the trustee or the debtor will make contractual installment payments *Bankruptcy Rule 3002.1(a)*.

Bankruptcy Law > Procedural Matters > Adversary Proceedings > Causes of

Action

Bankruptcy Law > Procedural Matters > Contested Matters

Bankruptcy Law > ... > Retention of Professionals > Compensation > Interim Compensation

HN10[] **Adversary Proceedings, Causes of Action**

Under *Fed. R. Bankr. P. 3002.1(i)*, if a holder of a claim fails to provide the notice required under *Rule 3002.1(c)*, the court may take either or both of the following actions: (1) preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case, unless the court determines that the failure was substantially justified or is harmless; or (2) award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure. *Fed. R. Bankr. P. 3002.1(i)*.

Bankruptcy Law > ... > Commencement of Case > Joint Cases > Commencement

HN11[] **Joint Cases, Commencement**

Pursuant to *Fed. R. Bankr. P. 3002.1(i)*, the only defense a creditor has to this action by the court is to prove that the failure to provide the information was substantially justified or harmless.

Counsel: **[**1]** For Wendy Michelle Bivens (1:14bk80841), Debtor: John T. Orcutt, Raleigh, NC; Craig Matthew Shapiro, Law Offices of John T. Orcutt, Durham, NC.

For Wendy Michelle Bivens (1:20ap9018), Plaintiff: Koury Lee Hicks, LEAD ATTORNEY, Craig Matthew Shapiro, Law Offices of John T. Orcutt, Durham, NC.

For CitiMortgage Inc. (1:20ap9018), Defendant: Jason Kenneth Purser, Andrew Lawrence Vining, LOGS Legal Group, LLP, Charlotte, NC.

For NewRez LLC (1:20ap9018), Defendant: George Benjamin Milam, Bradley Arant Boult Cummings, Charlotte, NC.

Judges: Catharine R. Aron, UNITED STATES BANKRUPTCY JUDGE.

Opinion by: Catharine R. Aron

Opinion

[*845] SO ORDERED.

SIGNED this 25th day of March, 2021.

/s/ Catharine R. Aron

UNITED STATES BANKRUPTCY JUDGE

MEMORANDUM OPINION AND ORDER DENYING MOTION TO DISMISS COMPLAINT

This adversary proceeding came before the Court on February 25, 2021, to consider **[*846]** the Motion to Dismiss Adversary Proceeding [Doc. #10] (the "Motion to Dismiss") filed by Defendant CitiMortgage, Inc. ("Defendant") on October 12,

2020. At the hearing, Jason Purser and Andrew Vining appeared on behalf of Defendant, Koury Hicks and Craig Shapiro appeared on behalf of Wendy Bivens ("Plaintiff"), and William Miller appeared as the United States **[**2]** Bankruptcy Administrator. After considering the Motion to Dismiss, the Brief in Support of the Motion to Dismiss [Doc. #15], the Brief in Opposition to the Motion to Dismiss [Doc. # 30], the arguments of counsel, and the record in this proceeding, the Court finds that the Motion to Dismiss should be denied for the reasons that follow.

BACKGROUND

On July 31, 2014, Plaintiff filed a voluntary petition for relief under Chapter 13 of the United States Bankruptcy Code. Plaintiff owns real property located at 1618 South Alston Avenue, Durham, North Carolina (the "Property"), which is Plaintiff's principal residence. The Property secured a mortgage claim held by Defendant. Plaintiff's plan was confirmed on October 20, 2014. Pursuant to the confirmed plan, Plaintiff proposed to pay the mortgage as a long term debt with the Chapter 13 Trustee to make ongoing monthly mortgage payments to Defendant in addition to monthly payments on the prepetition arrearage in an amount "To be determined" (Case No. 14-80841, Doc. # 21). Defendant filed a proof of claim on November 14, 2014, indicating that the ongoing monthly mortgage payment was $1,128.08 and the total arrearage claim was $7,011.61 (Claim #3). **[**3]** The ongoing monthly mortgage payment was later reduced to $1,069.54 effective August 2015 due to an escrow change (Case No. 14-80841, Doc. # 29).

On December 9, 2016 a Notice of Transfer was filed indicating that Defendant assigned the deed of trust and secured claim to Ditech Financial, LLC, with notices and payments to be sent to Ditech Financial, LLC (Case No. 14-80841, Doc. # 44). On July 19, 2017 a Notice of Transfer was filed indicating that Ditech Financial, LLC assigned the deed of trust and secured claim to New Penn Financial, LLC d/b/a/ Shellpoint Mortgage Servicing with notices and payments to be sent to Shellpoint Mortgage Servicing (Case No. 14-80841, Doc. # 46). On January 29, 2020, the Trustee filed a Notice of Final Cure Mortgage Payment (Case No. 14-80841, Docket # 60). NewRez, LLC d/b/a Shellpoint Mortgage Servicing responded to the Notice of Final Cure Payment agreeing that the prepetition arrearage was cured and that the Plaintiff was current on all postpetition payments, with the next payment due on February 1, 2020 (Case No. 14-80841, Docket # 61). On February 19, 2020, a Notice of Transfer was filed indicating that New Penn Financial, LLC d/b/a/ Shellpoint Mortgage **[**4]** Servicing assigned the deed of trust and secured claim to NewRez, LLC d/b/a/ Shellpoint Mortgage Servicing with notices and payments to be sent to NewRez, LLC d/b/a/ Shellpoint Mortgage Servicing (Case No. 14-80841, Doc. # 62). Plaintiff made all payments required under the confirmation order and received her Order of Discharge on June 1, 2020 (Case No. 14-80841, Doc. # 69). Plaintiff received a Notice of Default and Intent to Accelerate from Shellpoint on June 2, 2020 (Doc. #1, ¶ 84). Her bankruptcy case

was closed on July 8, 2020.

On August 19, 2020, Plaintiff filed a motion to reopen her bankruptcy case for the purpose of filing an adversary proceeding against her past and present mortgage holders which was granted by Order dated September 11, 2020 (Case **[*847]** No. 14-80841, Doc. # 77 & 81). The same day the case was reopened, Plaintiff filed a complaint against NewRez LLC f/k/a New Penn Financial, LLC and d/b/a/ Shellpoint Mortgage Servicing and Defendant. The complaint contains three claims for relief: (1) violation of the discharge injunction, (2) violation of the automatic stay, and (3) violation of *Bankruptcy Rule 3002.1(c)*[1] . Plaintiff asserts that Defendant willfully failed to correctly credit payments received **[**5]** under the confirmed plan, in violation of the discharge injunction and automatic stay (Doc. #1, ¶¶ 144, 208). Specifically, Plaintiff alleges that Defendant misapplied ongoing monthly payments received from the Trustee to the prepetition arrearage claim, misapplied ongoing monthly payments to the wrong month, and misapplied prepetition arrearage payments to the ongoing monthly installment payments (Doc. #1, ¶¶ 96-98). Plaintiff further asserts that Defendant assessed fees, expenses, and charges to Plaintiff's account without filing the requisite notice pursuant to *Bankruptcy Rule 3002.1(c)* including late charges, foreclosure attorney fees, bankruptcy costs, property inspections, technology fees, appraisal fees, and electronic invoice fees (Doc. #1, ¶ 191).

On October 12, 2020, Defendant filed their answer and this Motion to Dismiss which is presently before the Court requesting that the Court dismiss the complaint for failure to state a claim upon which relief may be granted under *Rule 12(b)(6) of the Federal Rules of Civil Procedure*.

STANDARD OF REVIEW

HN1[] *Federal Rule of Civil Procedure 12(b)(6)*, made applicable in this proceeding via *Rule 7012 of the Federal Rules of Bankruptcy Procedure*, provides that a complaint should be dismissed if "it fails to state a claim upon which relief can be granted." *Fed. R. Civ. P. 12(b)(6)*. To satisfy this pleading standard, the complaint must allege **[**6]** facts sufficient to state a plausible claim for relief. *Bell Atlantic Corp. v. Twombly, 550 U.S. 544, 570, 127 S. Ct. 1955, 167 L. Ed. 2d 929 (2007)*. A claim is plausible if the plaintiff pleads facts that allow the Court to reasonably infer that the plaintiff is entitled to his sought-after relief. *Ashcroft v. Iqbal, 556 U.S. 662, 678, 129 S. Ct. 1937, 173 L. Ed. 2d 868 (2009)*. To determine plausibility, all well-pled facts set forth in the complaint are taken as true and viewed in a light most favorable to the plaintiff. *Id.* "[L]egal conclusions, elements of a cause of action, and bare assertions devoid of further factual enhancement" will not constitute well-pled facts necessary to withstand a motion to dismiss. *Nemet Chevrolet, Ltd. v. Consumeraffairs.com, Inc., 591 F.3d 250, 255 (4th Cir. 2009)*. In addition, "if the

[1] In addition, Plaintiff alleged violation of ***Bankruptcy Rule 3002.1(g)*** only as to NewRez LLC f/k/a New Penn Financial, LLC and d/b/a/ Shellpoint Mortgage Servicing. This Motion to Dismiss only pertains to the claims alleged against CitiMortgage, Inc.

complaint lacks an allegation regarding an element necessary to obtain relief," dismissal is proper under *Rule 12(b)(6)*. 2 *MOORE'S FEDERAL PRACTICE § 12.34(4)(a)* (2019); *see also EEOC v. Pbm Graphics, 877 F. Supp. 2d 334, 343 (M.D.N.C. 2012)* (finding that a plaintiff must allege facts sufficient to state each element of his claim in order to survive a 12(b)(6) motion to dismiss) (citing *Bass v. E.I. DuPont de Nemours & Co., 324 F.3d 761, 764-65 (4th Cir. 2003))*.

DISCUSSION

I) First Cause of Action: Violation of the Section 524(i) Discharge Injunction

Plaintiff contends that Defendant violated *11 U.S.C. § 524(i)* by willfully failing **[*848]** to correctly credit payments received under the confirmed plan and as such asks the Court to sanction Defendant pursuant to its authority under *11 U.S.C. § 105*.[2] *11 U.S.C. §524(i)* provides that:

> The willful failure of a creditor to credit payments **[**7]** received under a plan confirmed under this title, unless the order confirming a plan is revoked, the plan is in default, or the creditor has not received payments required to be made under the plan in the manner required by the plan (including crediting the amounts required under the plan), shall constitute a violation of an injunction under *subsection (a)(2)* if the act of the creditor to collect and failure to credit payments in the manner required by the plan caused material injury to the debtor.

11 U.S.C. § 524(i). *HN2*[] Thus, there are two requirements that must be met to establish a violation of *§524(i)*: (1) a willful failure to credit payments received under a confirmed plan and (2) material injury to the debtor. *Williams v. Citifinancial Servicing LLC (In re Williams), 612 B.R. 682, 691 (Bankr. M.D.N.C. 2020)* (citing *Ridley v. M&T Bank (In re Ridley), 572 B.R. 352, 361 (Bankr. E.D. Okla. 2017))*.

HN3[] As to the first requirement, in the context of *§524(i)*, "willfullness" only requires that the creditor intended to apply the payments received in the manner it applied them. *See In re Williams, 612 B.R. at 691*. "Willfullness" does not require bad faith nor a specific intent to violate the Code or plan provisions. *Id.* In the Complaint, Plaintiff alleges that Defendant "willfully failed to correctly credit payments received under the confirmed plan" (Doc. #1, ¶ 144). Specifically, the Plaintiff alleges that Defendant misapplied ongoing monthly **[**8]** payments received from the Trustee to the prepetition arrearage claim, misapplied ongoing monthly payments to the wrong month, and misapplied prepetition arrearage payments to the ongoing monthly installment payments (Doc. #1, ¶¶ 96-98). Plaintiff alleges that Defendant communicated inaccurate account information to

[2] *11 U.S.C. § 105* "allows a bankruptcy court to hold a creditor in civil contempt, and impose contempt sanctions, for violating the discharge injunction." *Williams v. Citifinancial Servicing LLC (In re Williams), 612 B.R. 682, 690 (Bankr. M.D.N.C. 2020)* (citing *Taggart v. Lorenzen, 139 S. Ct. 1795, 1801, 204 L. Ed. 2d 129 (2019))*.

Shellpoint, due to the misapplied payments, which led to Shellpoint demanding post-discharge payments of amounts that had already been paid during the Chapter 13 Plan and caused Shellpoint to send Plaintiff a Notice of Default and Intent to Accelerate, initiating a foreclosure action on Plaintiff's home of over fifty years (Doc. #1, ¶¶ 84, 171). The Court finds that the allegation that Defendant willfully misapplied payments, which is supported by the subsequent inaccurate account balance and threat of foreclosure, sufficiently plausible taken in the light most favorable to the Plaintiff to survive a motion to dismiss.

HN4[] As to the second requirement, a material injury to the debtor, this will "be met in virtually every case involving a secured creditor, because the failure to properly credit payments will almost always result in a higher payoff balance for the debtor and therefore **[**9]** a larger lien on the debtor's property than if the payments were credited properly." *Id. at 692* (quoting 4 Collier on Bankruptcy ¶ 524.08 (16th ed. 2019)). The Complaint alleges this precise injury, that due to the misapplication of payments, there was "an allegedly past due balance upon discharge" which led to "Shellpoint demanding post-discharge payments of amounts that had already been paid during the Chapter 13 Plan" (Doc. **[*849]** #1, ¶¶ 5, 171). Plaintiff also alleges emotional injury (Doc. #1, ¶ 173).

HN5[] Further, this Court has previously held in *Williams* that where a creditor misapplies payments under a confirmed plan and then transfers the account with records showing an incorrect payment history and inflated loan balance, causing injury to the plaintiff, that those actions could constitute a violation of *§ 524(i)*. *In re Williams, 612 B.R. at 693-94* (finding that *§524(i)* applies to both current and previous claim holders. Also finding that transferring a "mortgage account with an inflated balance due to misapplied payments sufficient to constitute an act to collect for the purposes of withstanding a motion to dismiss under *Rule 12(b)(6)*"). As such, the facts pled in the Complaint are sufficient to state a plausible claim for violation of the *§ 524(i)* discharge injunction. **[**10]**

II) Second Cause of Action: Violation of the Automatic Stay

Plaintiff also seeks sanctions against Defendant for violation of the automatic stay pursuant to *11 U.S.C. § 362(k)*. *HN6*[] *Section 362(k)* provides that "an individual injured by any willful violation of a stay ... shall recover actual damages including costs and attorneys' fees, and in appropriate circumstances, may recover punitive damages." *11 U.S.C. § 362(k)*. Therefore, to support a claim for violation of the automatic stay, a movant must show 1) that there was a violation of the automatic stay, 2) that the violation was willful, and 3) that actual damages resulted from the violation. *In re Williams, 612 B.R. at 694* (citing *Ridley v. M&T Bank (In re Ridley), 572 B.R. 352, 361 (Bankr. E.D. Okla. 2017)*.

Plaintiff alleges that the misapplication of payments received under the confirmed plan constitutes a violation of the automatic stay (Doc. #1, ¶¶ 204-

06). *HN7*[] This Court has followed the majority of courts and has held that "misapplication of chapter 13 plan payments is a cause of action for violation of the automatic stay." *In re Williams, 612 B.R. at 694*. However, Defendant contends that there was no violation of the automatic stay as Defendant never communicated the erroneously credited payments to the Debtor and that their bookkeeping entries do not violate the automatic stay, citing the First Circuit's decision in **[**11]** *Mann v. Chase Manhattan Mortg. Corp., 316 F.3d 1 (1st Cir. 2003)*. While it is true that there is no violation of the automatic stay if the erroneous bookkeeping entries are "in no manner communicated to the debtor, the debtor's other creditors, the bankruptcy court, nor any third party," that is distinguishable from what the Plaintiff alleges in the case at hand. *Mann, 316 F.3d at 3*. Here, the Plaintiff alleges that the Defendant misapplied payments and then transferred the account with an inflated loan balance which led the subsequent claim holder to attempt to collect the inflated balance. These allegations are sufficient for this Court to make the reasonable inference that the alleged misapplied payments were not simply internal bookkeeping records as discussed in *Mann*.

Plaintiff also alleges that the violation of the automatic stay was willful. *HN8*[] To constitute a willful violation of the automatic stay, a creditor need only "commit an intentional act with knowledge of the automatic stay." *Citizens Bank v. Strumpf (In re Strumpf), 37 F.3d 155, 159 (4th Cir. 1994)*. Plaintiff alleged that Defendant was aware of both the automatic stay and the confirmed plan and despite this knowledge misapplied the payments received under the confirmed plan (Doc. #1, ¶¶ 30, 56, 59, 160). Thus, Plaintiff has plausibly pled a willful violation of the automatic **[**12]** stay.

[*850] Finally, Plaintiff contends that she did in fact suffer actual damages as a result of the violation of the automatic stay. Plaintiff has alleged that due to the misapplication of payments under the confirmed plan there was "an allegedly past due balance upon discharge" which led to "Shellpoint demanding post-discharge payments of amounts that had already been paid during the Chapter 13 Plan and threatening to foreclose" (Doc. #1, ¶¶ 5, 171). Plaintiff also alleges emotional injury (Doc. #1, ¶ 173). The Court finds the allegations in the Complaint regarding damages sufficient for the purposes of *Rule 12(b)(6)* and that Plaintiff has plausibly pled all elements required under *§ 362(k)*.

III) Third Cause of Action: Violation of the Bankruptcy Rule 3002.1(c)

Plaintiff's final cause of action alleges that Defendant failed to give notice of assessed fees, expenses, and charges as required by *Bankruptcy Rule 3002.1(c)* and seeks sanctions under *Bankruptcy Rule 3002.1(i)*. *HN9*[] *Bankruptcy Rule 3002.1(a)* states that the noticing requirements of *Rule 3002.1(c)* apply "in a chapter 13 case to claims (1) that are secured by a security interest in the debtor's principal residence and (2) for which the plan provides that either the trustee or the debtor will make contractual installment payments..." *Bankruptcy Rule 3002.1(a)*. Thus,

Rule 3002.1(c) is applicable to the claim **[**13]** at hand.

Pursuant to *Bankruptcy Rule 3002.1(c)*:

> The holder of the claim shall file and serve on the debtor, debtor's counsel, and the trustee a notice itemizing all fees, expenses, or charges (1) that were incurred in connection with the claim after the bankruptcy case was filed, and (2) that the holder asserts are recoverable against the debtor or against the debtor's principal residence. The notice shall be served within 180 days after the date on which the fees, expenses, or charges are incurred.

Bankruptcy Rule 3002.1(c).

Plaintiff alleges that Defendant "assessed fees, expenses, and charges to the Account without filing the requisite notice and notifying [Plaintiff], [Plaintiff]'s counsel, and Trustee Hutson pursuant to *Rule 3002.1(c)*, including late charges, foreclosure attorney fees, 'bankruptcy costs,' property inspections, 'technology fees,' appraisal fees, and 'elec invoice fees.'" (Doc. #1, ¶¶ 185, 191). Plaintiff contends that Defendant transferred the account with the assessed fees, expenses, and charges, thus asserting the recoverability of such fees (Doc. #1, ¶¶ 61, 62).

HN10[] Under *Bankruptcy Rule 3002.1(i)*, if a holder of a claim fails to provide the notice required under *Rule 3002.1(c)*, the court may take either or both of the following actions:

> (1) preclude the holder from presenting **[**14]** the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case, unless the court determines that the failure was substantially justified or is harmless; or
>
> (2) award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure.

Bankruptcy Rule 3002.1(i).

HN11[] Pursuant to *Rule 3002.1(i)*, "[t]he only defense a creditor has to this action by the court is to prove that the failure to provide the information was substantially justified or harmless." 9 Collier on Bankruptcy ¶ 3002.1.03 (16th ed. 2020). Plaintiff alleges that Defendant's failure to provide the information required by *Rule 3002.1(c)* "was not substantially justified" and "was not harmless" (Doc. #1, ¶¶ 185, 186). Plaintiff contends that Defendant transferred the account with the assessed fees, expenses, and charges, thus asserting the recoverability **[*851]** of such fees, which inflated the balance of the amount owed as the "failure to comply with *Rule 3002.1(c)* prevented [Plaintiff], her counsel, and Trustee Hutson from utilizing *Rule 3002.1(e)* by moving this Court to 'determine whether payment of any claimed fee, expense, or charge is required by the underlying agreement and applicable nonbankruptcy law to cure a default or maintain payments **[**15]** in accordance with *§ 1322(b)(5)* of the Code'" (Doc. #1, ¶ 80). Taking Plaintiff's allegations as true, for the purposes of *Rule 12(b)(6)*, this Court finds that Plaintiff has plausibly pled her cause of action for violation of *Bankruptcy Rule 3002.1(c)* and sanctions pursuant to *Bankruptcy Rule 3002.1(i)*.

CONCLUSION

For the reasons as stated above, IT IS HEREBY ORDERED, ADJUDGED, AND DECREED that Defendant's Motion to Dismiss the Complaint is DENIED.

End of Document

§ 4.05 Loan Modifications in Chapter 13. This is section 4.05 of the Final Report of the ABI Commission on Consumer Bankruptcy, which was issued in April, 2019. Permission to reprint this part of the Commission's Report for this seminar was given by the American Bankruptcy Institute. The full Report is available at www.abi.org.

(a) The Commission supports the use of loan modification in bankruptcy proceedings. Loan modification programs vary widely from district to district. There should be more uniformity, and that uniformity could be encouraged through the bankruptcy rulemaking process.

(b) Courts should not delay confirmation of a chapter 13 plan because there is a pending loan modification. Instead, the terms of a successful mortgage modification should be incorporated into an amended plan that is approved through the plan modification process under section 1329 and Federal Rule of Bankruptcy Procedure 3015, with appropriate notice. This process also should include amended Official Bankruptcy Forms B106I and B106J if the loan modification changes the monthly mortgage payment by 10% or more.

(c) Attorneys should be encouraged to participate in loan modifications and should be appropriately compensated for their time in the loan modification process. An amended plan incorporating a loan modification should state the amount of fees to which debtor's counsel is entitled because of additional services rendered and how those fees will be paid. The plan also should specify any additional fees, costs, or expenses to which the debtor agrees that the mortgage holder or servicer is entitled.

(d) Because the plan modification process will provide appropriate notice to all parties, a loan modification incorporated into an amended plan does not require a payment change notice that would otherwise be required by Federal Rule of Bankruptcy Procedure 3002.1 because of a change in the mortgage payment or because of the fees, costs, or expenses due the mortgage holder or servicer.

(e) Transparency in the production of documents required for loan modification is vital to the success of loan modification. Too often, loan modifications fail due to a lack of communication between debtors and mortgage servicers, resulting in the other participants in the bankruptcy (debtor's and creditor's attorneys, trustees and the bankruptcy court itself) being unable to determine what problems have arisen and how to resolve them. Loan modification rules should encourage transparency through online portals, the case management and electronic case filing (CM/ECF) system, or through other processes.

Loan Modifications Generally. Consensual mortgage loan modification, sometimes called "loss mitigation," negotiates an adjustment to the terms of a mortgage secured by a debtor's principal residence or other real property. Mortgage loan modifications occur outside of bankruptcy, but they also can occur while the debtor is in a bankruptcy case.

Several chapter 13 trustees and their courts have instituted loan-modification programs, which typically involve some form of mediation between the mortgage lender or servicer and debtors.[73] This recommendation addresses mortgage loan modifications during a chapter 13 case.

The Commission supports the use of loan modification in bankruptcy. Loan modification, when done well, helps chapter 13 debtors retain their homes, provides better alternatives for home mortgage lenders, and benefits all creditors in chapter 13 cases. Lower mortgage payments obviously improve the debtors' chances of successfully rehabilitating a failing mortgage, which allows families to keep their homes. Lenders avoid foreclosure and other dispositions that are less economically advantageous than a performing loan. Loan modification can stabilize or reduce monthly mortgage payments, provide for payment of arrearages, and address payment of other components such as taxes and insurance. Loan modification also enhances the financial stability of the chapter 13 case, increasing the likelihood that the debtor will complete plan payments while also making possible increased payments to other creditors.

The loan-modification programs in effect are diverse. Some loan-modification programs are prescribed by local bankruptcy rules; others are less formal. Some are modeled as "mediations" using third-party neutrals; others are court-based and supervised by judges or trustees. Some programs are triggered automatically at the beginning of every chapter 13 case containing a home mortgage; others require initial action by a debtor or trustee. Some loan modifications are "motion and order" systems in which courts order temporary or permanent modifications of loans based on

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[73] The Commission believes several dozen judicial districts have loan-modification programs but is not aware of any comprehensive list of such programs. Examples include Bankr. S.D. Fla. Admin. Order 14-03; Bankr. S.D.N.Y. R. 9019-2; Bankr. D.R.I. R. App. VII; and Bankr. W.D. Wash. 4001-2. The topic also has been the subject of extensive commentary, much of which discusses the content of loan-modification programs in bankruptcy court. See, e.g., Kevin R. Anderson & Rebecca B. Connolly, Helping Chapter 13 Homeowners Keep Homes, Am. Bankr. Inst. J., Mar. 2011, at 40; Linda Elizabeth Coco, "Foaming the Runway" for Homeowners: U.S. Bankruptcy Courts "Preserving Homeownership" in the Wake of Home Affordable Modification Program, 23 Am. Bankr. Inst. L. Rev. 421 (2015); Heather D. McGivern, Loan Modifications: Short-Term Gain, Long-Term Pain, Am. Bankr. Inst. J., June 2015, at 36; Cathleen Cooper Moran, Reconsidering the Virtue of Loan Modifications in Chapter 13 Cases, Am. Bankr. Inst. J., June 2015, at 37; Cecilia G. Morris & Mary K. Guccion, The Loss Mitigation Program Procedures for the United States Bankruptcy Court for the Southern District of New York, 19 Am. Bankr. Inst. L. Rev. 1 (2011); John Rao, Bankruptcy Courts Respond to Foreclosure Crisis with LossMitigation Programs, Mar. 2011, at 14.

stipulations; others use the chapter 13 plan confirmation and modification as the platforms for loan modification. Debtors' attorneys drive the process in some districts, while lenders/servicers carry a greater burden in others — sometimes with little or no involvement by debtors' counsel.

Lenders and servicers have expressed frustration with the complexity, uncertainty and expense of the many different loan-modification programs. Lenders willing to offer loan modifications must consult professionals district by district — and sometimes judge by judge — to navigate the varying local cultures for loan modifications. Nonuniformity increases the costs of mortgage modification, and those costs are routinely passed on to debtors as postpetition fees, costs and expenses.

Consistent with its general recommendation in favor of more uniformity in the consumer bankruptcy system,[74] the Commission believes that it would be desirable to standardize important aspects of consensual mortgage loan modification in chapter 13 cases. This standardization should occur through the national rules process as well as new official forms, providing general authorization and structure for loan-modification programs. In doing so, the national rules also would encourage the development of programs in districts that do not already have them.

Loan Modifications and the Chapter 13 Plan. In most chapter 13 cases that contain a successfully negotiated mortgage loan modification, the terms are not known, and the process is not completed until after a plan has been confirmed. The meeting of creditors in a chapter 13 case commences within fifty days of the petition being filed,[75] and plan confirmation must be addressed within forty-five days after the meeting of creditors.[76] Loan-modification programs rarely adhere to that schedule in chapter 13 cases.

Many loan-modification protocols include trial periods that run three months or more before the terms of a final agreement are known. Other creditors in chapter 13 cases — particularly creditors with depreciating collateral such as car lenders — rightfully demand commencement of payments before the uncertain terminus of loan-modification discussions between a lender and a chapter 13 debtor. Loan modification

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[74] See § 4.02 Nonuniform Court Practices.
[75] See Fed. R. Bankr. P. 2003(a).
[76] See 11 U.S.C. § 1324(b).

can occur in chapter 13 cases months after confirmation or even years later if necessary to address the debtor's inability to comply with the terms of an unmodified mortgage loan.

Bankruptcy courts have adopted various procedural mechanisms to temporarily confirm plans that allow distributions to other creditors to begin without having complete information about a pending loan modification. Some courts order an "interim" confirmation. Others confirm plans that reference the pending loan modification without details. Some courts delay confirmation altogether, but enter orders allowing payment of adequate protection to some creditors while accumulating funds to be paid to other creditors after the loan modification completes.

Chapter 13 plans should be confirmed expeditiously to begin distributions to creditors. Except in the rare case in which the loan modification becomes final before plan confirmation, a successfully negotiated loan modification should be incorporated into the chapter 13 plan through the plan-modification process of section 1329.

Consensual mortgage modification necessarily changes the terms of payment of the mortgage claim — typically, the largest debt in a chapter 13 case. The mathematics of the chapter 13 case are changed in ways that will often require other adjustments to the plan. If loan modification reduces the monthly mortgage payment, for example, the freed-up income may be available to increase plan payments to other creditors. If the loan modification changes the treatment of an arrearage or changes the amount or method of paying taxes and insurance, those changes will also affect the availability of funds to pay other claims. The plan-modification process is the readily available, best understood and most appropriate vehicle for managing the mortgage loan-modification process in most chapter 13 cases.

Mortgage modification through modification of the chapter 13 plan should always include a motion to modify the plan consistent with Federal Rule of Bankruptcy Procedure 3015(h) and should always lead to an order under section 1329. In conduit districts, the plan-modification process thus will produce a court order on which debtors, trustees, and lenders can rely in altering any payment schedule.[77] This motion-and-order procedure is also important in nonconduit districts where, too often, only the debtor and lender are aware of the terms of the modified loan with a comparison to the terms of the original loan; a comparison of the monthly amounts due for principal, interest, taxes and insurance in the original and modified loan; the amount of arrears capitalized into the modified mortgage; any additional fees or deposit the debtor must pay to the lender; the date the first payment is due on the modified loan; and a certification from the lender that no pre- or postpetition amount is due or a statement of exceptions to the certification. This information could be required as part of a new official bankruptcy form, to be attached to any motion for approval of a modified plan that included mortgage modification.

Amended budget information — in the form of amended Official Forms 106I for

[77] In a conduit plan, payments to the mortgage holder are made through the chapter 13 trustee, and in a nonconduit plan, the debtor continues to make payments directly to the mortgage holder during the pendency of the chapter 13 case. A fuller discussion about the differences between conduit and nonconduit plans can be found in the Commission's recommendation about conduit plans. See § 4.06 Conduit Mortgage Payments.

income and 106J — should be filed and served together with the motion to modify the confirmed plan whenever loan modification changes the original monthly mortgage payment by a substantial amount. The trustee and creditors cannot meaningfully evaluate a consensual mortgage modification to determine whether to object to the plan as modified without amended budget information. When the payment changes are small and the financial impact of the proposed mortgage modification is insubstantial, debtors should not be put to the expense and delay of producing amended schedules unless requested by a creditor or the trustee. When payment changes are substantial, amended budgets should be required and should be served with the motion to approve the modified mortgage and plan. The Commission believes a 10% change in mortgage expenses should be considered "substantial."

Chapter 13 trustees must be fully engaged in the loan-modification process. In some districts, the chapter 13 trustee is a full participant in any loan modification undertaken by a debtor and a mortgage holder. In other districts, loan modification routinely proceeds without the involvement of the trustee, often becoming binding on debtors and lenders before the trustee knows the terms. The Commission was told that some chapter 13 trustees only became aware of consensually modified mortgage loans months or years after the modification was entered into, when payment-change notices or claims disputes revealed payment terms different from those disclosed at the beginning of the chapter 13 case. This lack of transparency and uncertain involvement by the trustee is inconsistent with the interests of creditors in individual cases. The plan-modification process will ensure the trustee is fully aware of any loan modification.

Encouraging Attorneys to Participate in Loan Modifications. Chapter 13 debtors' attorneys should be encouraged to vigorously represent their clients in the loan-modification process. Courts should allow fees for those services as a component of the plan-modification process. Loan modification is complicated, technical and tedious. Gathering the necessary documents and information, navigating the online portals for loan modification, responding promptly to questions from lenders and servicers, digesting and understanding loan-modification terms and documents — aspects common to all loan-modification programs — are usually not within the competence of unrepresented debtors. Once the information is gathered, determining whether the terms of a proposed loan modification are in the debtor's best interest is also commonly beyond the ability of unrepresented debtors. Consistent with its recommendation on presumptively reasonable fees in chapter 13 cases,[78] reasonable fees for representation in connection with loan modification should be allowed in addition to the fees normally allowed for representing debtors in chapter 13 cases.

Loan Modifications and Payment Change Notices (PCNs). The plan-modification process will provide detailed information about any mortgage payment change produced by the loan-modification process. As recommended above, a new official bankruptcy form should include specific information about how the loan modification changed the original mortgage payment. If the Commission's recommendation is adopted, approval of the mortgage modification in the judicial order should substitute for any PCN that Federal Rule of Bankruptcy Procedure 3002.1 otherwise would require.

Transparency in the Loan-Modification Process. Throughout the Commission's recommendations on loan modifications is the theme of transparency to all parties in the

[78] See § 3.03 Presumptively Reasonable Attorney's Fees in Chapter 13s.

bankruptcy process. Indeed, the Commission's recommendation to use the plan-modification process rests largely on providing notice and the ability to be heard to all parties. Participation not only allows all parties in the bankruptcy to protect their own interests but also to help resolve problems that have arisen in the loan-modification process. The rules process that the Commission recommends should consider how to promote transparency in loan modifications through existing online portals and who can access them. The rules process also should consider changes to which documents should be made available through the case management/electronic case filing (CM/ECF) system or through other processes.

Mortgage servicing coverage chart[1]

Consumer Financial Protection Bureau

Regulation X (12 CFR 1024)	Closed-end, principal residence	Closed-end, non-principal residence	Open-end	Servicers and loan types exempt from coverage
Escrow Accounts (§§ 1024.17 and .34)	Y	Y	Y (only for § 1024.17)	No annual statement required for certain default, foreclosure, or bankruptcy situations, per § 1024.17(i)(2). Subject to 1024.37, small servicers[2] may purchase force-placed insurance if less expensive than escrow payment for borrower's hazard insurance, per § 1024.17(k)(5)(iii).
Servicing Transfers (§ 1024.33(b)-(d))	Y	Y	N	Certain transfers specified in § 1024.33(b)(2) if there is no change in the payee, address for payments, account number, or amount of payment due.
Error Resolution & Information Requests (§§ 1024.35 and .36)	Y	Y	N	
Force-Placed Insurance (§ 1024.37)	Y	Y	N	Subject to § 1024.37, small servicers may purchase force-placed insurance if less expensive than escrow payment for borrower's hazard insurance, per § 1024.17(k)(5)(iii).
Policies & Procedures (§ 1024.38)	Y	Y	N	Small servicers; reverse mortgages[3]; qualified lenders.[4]
Early Intervention (§ 1024.39)	Y	N	N	Small servicers; reverse mortgages; qualified lenders. Partial exemptions for certain loans with a borrower in bankruptcy and certain debt collection-related situations, per § 1024.39(c)(1) and (d).
Continuity of Contact (§ 1024.40)	Y	N	N	Small servicers; reverse mortgages; qualified lenders.
Loss Mitigation Procedures (§ 1024.41)	Y	N	N	Small servicers (except must comply with certain prohibitions on foreclosure referral, moving for judgment or order of sale, or conducting a sale, per § 1024.41(j)); reverse mortgages; qualified lenders.

Regulation Z (12 CFR 1026)	Closed-end, principal residence	Closed-end, non-principal residence	Open-end	Servicers and loan types exempt from coverage
ARM Disclosures (§ 1026.20(c) & (d))	Y	N	N	Adjustable-rate mortgage (ARM) with term of 1 year or less. Exemption from § 1026.20(c) for certain first rate adjustments and certain debt collection-related situations.
Escrow Cancellation Notices (§ 1026.20(e))	Y	Y	N	Reverse mortgages; subordinate-lien mortgages.
Prompt Crediting & No Pyramiding (§ 1026.36(c)(1)-(2))	Y	N	N[5]	
Payoff Statements (§ 1026.36(c)(3))	Y	Y	Y	
Mortgage Loan Transfer Disclosures (§ 1026.39)	Y	Y	Y (only principal dwellings)	Servicers that are not covered persons per § 1026.39(a)(1) or that are subject to an exception in § 1026.39(c).
Periodic Statements (§ 1026.41)	Y	Y	N[6]	Small servicers; reverse mortgages; timeshare plans; certain charged-off loans; certain loans with a consumer in bankruptcy. Certain fixed-rate loans with coupon books are exempt from some requirements, per § 1026.41(e)(3).

[1] This chart summarizes rules in effect as of April 19, 2018 and is not a substitute for the rules. Only the rules and the Official Interpretations can provide complete and definitive information regarding their requirements. The complete rules, including the Official Interpretations and small entity compliance guide, are available at www.consumerfinance.gov/policy-compliance/guidance/implementation-guidance/mortserv. This chart does not include a discussion of the definitions or overall coverage exemptions in Regulations X and Z (for example, there are overall exemptions for credit primarily for a business purpose). For more information, *see, e.g.*, 12 CFR 1024.2; 12 CFR 1024.5; 12 CFR 1026.1; 12 CFR 1026.2; 12 CFR 1026.3; 12 CFR 1026.5. This chart discusses only the requirements listed in the chart and does not describe all of the requirements that may apply to a particular transaction.

[2] Small servicer is defined in 12 CFR 1026.41(e)(4)(ii).

[3] Reverse mortgage transaction is defined in 12 CFR 1026.33(a).

[4] Qualified lender is defined in 12 CFR 617.7000.

[5] For payment processing requirements for open-end loans, see 12 CFR 1026.10.

[6] For periodic statement requirements for open-end loans, see 12 CFR 1026.7.

Speaker Biographies

John M. Hauber was appointed as the Chapter 13 Standing Trustee for the Southern District of Indiana, Indianapolis Division on April 1, 2015. Prior to this appointment, Mr. Hauber was a partner in the Indianapolis, Indiana office of Tom Scott & Associates, P.C. His practice included business and consumer bankruptcy, debtor and creditor's rights including financial restructuring and workouts, and all aspects of bankruptcy litigation. Mr. Hauber received his A.B. from Wabash College in 1990 and his J.D. from Indiana University Robert H. McKinney School of Law in 1993. He worked for the Indiana Attorney General's Consumer Protection Division from 1993 through 1997 as a Deputy Attorney General and was a member of the National Association of Consumer Advocates and the Indiana Home Defense Task Force. He worked in private practice from 1997 through 2002 emphasizing the representation of consumer bankruptcy debtors. Mr. Hauber was a staff attorney for Chapter 13 Trustee Robert A. Brothers in December 2002 before returning to consumer bankruptcy practice in August 2008. Mr. Hauber is currently an adjunct professor at the I.U. McKinney School of Law. He has lectured on all aspects of consumer bankruptcy for the Indiana Continuing Legal Education Forum (ICLEF), the Indianapolis Bar Association, the American Bankruptcy Institute, and the Office of the United States Trustee for Region 10 since 2002. Mr. Hauber also offers free continuing legal education quarterly for members of the local bankruptcy bar. He is admitted to all Indiana state courts, federal courts for the Northern and Southern Districts of Indiana and the 7th Circuit Court of Appeals.

Alice Whitten is Managing Counsel - Senior Vice President in the Wells Fargo Legal Department in their Irving, TX office. She leads a team that provides guidance and support for consumer bankruptcy operations across the Wells Fargo enterprise, including mortgage, automobile, credit cards and student lending and supports FCRA, SCRA & MLA across the consumer lending enterprise. She has been with Wells Fargo since 2014. Prior to joining Wells Fargo, she previously served as a Standing Chapter 13 Trustee in the Northern District of Texas for four years and was Senior Vice President – Associate General Counsel with AmeriCredit Financial Services, Inc. (now known as GM Financial) providing legal support for bankruptcy and default services operations. Alice is a graduate of St. Mary's University School of Law (cum laude) in San Antonio, Texas and the University of Minnesota – Carlson School of Management. Alice is admitted to practice in Texas. She is currently the Co-Chair of the NACTT Automobile Committee and a Board Member for the NACTT Academy. She was a Council Member of the Bankruptcy Law Section Counsel of the State Bar of Texas from 2013-2015, and a Committee Member of the Committee on Case Administration and the Estate for the ABI Commission on Consumer Bankruptcy (2018-2019). She is currently the Co-Chair of the NACTT Automobile Committee and a Board Member for the NACTT Academy.

Michael T. Bates is an Executive Director and Managing Attorney at USAA, Federal Savings Bank where he provides support to the Bank's Member Debt Solutions Team on issues pertaining to consumer bankruptcy, collections, repossessions, foreclosures and other default-related servicing issues. Prior to joining USAA, Mike was a Vice President and Assistant General Counsel at JPMorgan Chase & Co. where he provided legal advice to Chase's mortgage banking bankruptcy group. Mike also served for over 21 years as a Senior Vice President and Senior Company Counsel for Wells Fargo & Company where he provided legal advice to all of Wells Fargo's consumer bankruptcy groups. Mike is a graduate of Hamline University School of Law (with honors) and Iowa State University and he is admitted to practice in Texas, Minnesota and Iowa. Mike served as a Commissioner on the ABI Consumer Bankruptcy Commission and has been active in the NACTT for more than fifteen years.

Lisa Sitkin is a Senior Staff Attorney at National Housing Law Project (NHLP) in San Francisco, CA, where she engages in policy advocacy and provides technical assistance, training and practice resources to attorneys representing low-income homeowners and tenants. She has been practicing law since 1997. Prior to joining NHLP, Ms. Sitkin was a Managing Attorney at Housing and Economic Rights Advocates in Oakland, CA. Ms. Sitkin has counseled and represented individual clients in foreclosure matters, participated in policy advocacy regarding mortgage servicing and foreclosure at the state and federal levels, and assisted with mortgage servicing, predatory and unfair lending litigation. She has conducted numerous workshops and trainings regarding mortgages, foreclosures, loan modification and foreclosure rescue scams, including programs produced by the Practicing Law Institute, the National Consumer Law Center and the National Association of Consumer Attorneys, and has testified before the California State Legislature and other governmental bodies regarding mortgage servicing and foreclosure issues. She has been active in legislative and regulatory advocacy related to homeowner and tenant relief during the COVID-19 pandemic. She is one of the original drafters of the bill that ultimately became the California Homeowner Bill of Rights.