

---



---

**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF UTAH  
CENTRAL DIVISION**

---

In re:

DENNIS VARIO  
SHELLY VARIO

Debtors.

Bankruptcy Number 96B-22208

Chapter 13

---

LARRY RONALD BOSWELL  
KIMBERLY ANN BOSWELL

Debtors.

Bankruptcy Number 96B-21913

Chapter 13

---



---

**MEMORANDUM OPINION REGARDING CONFIRMATION OF THE DEBTORS'  
CHAPTER 13 PLANS AND ORDER**

---

The issue presented in each of these chapter 13 cases is whether a secured creditor is entitled to interest on mortgage arrearages to be cured in the debtors' proposed chapter 13 plans. The Court concludes that secured creditors with claims consisting of delinquent prepetition mortgage principle and interest payments arising from contracts entered into with debtors after October 22, 1994, are not entitled to payment of a discount factor or interest on their secured claims.

## FACTS

The facts of each of the cases are similar. Each chapter 13 plan as initially drafted provided that mortgage default creditors would be paid interest on their prepetition default claims.<sup>1</sup> The Standing Chapter 13 Trustee filed objections in each case asserting that 11 U.S.C. §1322(e) prevented the payment of interest unless the underlying agreement or applicable nonbankruptcy law so provided. Both cases were continued from their initially scheduled confirmation hearings to allow the debtors to respond to the Standing Chapter 13 Trustee's objections. In both cases modifications were made to the chapter 13 plans addressing the issue.<sup>2</sup> None of the parties dispute that the underlying contracts were entered into after October 22, 1994, and that the contracts do not provide for the payment of postpetition interest. No party has cited any applicable nonbankruptcy law that provides for the payment of postpetition interest. Because the issue is universal to all chapter 13

---

<sup>1</sup> The plan filed by Dennis and Shelly Vario listed The Money Store as a prepetition mortgage default creditor with a default of \$3,910.00 and interest to be paid of 10%. The Money Store filed claim number 7, seeking prepetition monthly default payments of \$3,911.45 and prepetition late charges of \$39.11 for a total claim of \$4107.00. The claim indicated the debt was incurred April 24, 1995.

The plan filed by Larry and Kimberly Boswell listed G.E. Capital Mortgage as a prepetition mortgage default creditor with a default of \$2,249.58 and interest to be paid of 9.5%. Commercial Credit was also listed as a prepetition mortgage default creditor with a default of \$232.00 and interest to be paid of 18%. G.E. Capital Mortgage filed claim number 9, seeking prepetition monthly default payments of \$4,221.68 representing \$3,350.24 in prepetition arrearages and costs amortized at 9.5% over 60 months. The claim indicated the debt was incurred March 23, 1995. Commercial Credit filed claim number 3, seeking prepetition monthly default payments of \$270.37, and did not request interest. The claim indicated the debt was incurred December 8, 1995.

<sup>2</sup> On October 23, 1996, the Vario plan was amended to modify the amount of the arrearage and to pay 11.75% interest on only the late charges. The plan was orally modified in court to eliminate all interest on the prepetition claim in accordance with an agreement reached with The Money Store.

On October 2, 1996, the Boswell plan was amended to eliminate interest to both of the prepetition mortgage creditors.

plans that include mortgage arrearages arising from contracts entered into after October 22, 1994, the Court issues this written ruling.

### DISCUSSION

A chapter 13 plan may not modify the rights of holders of secured claims "secured only by a security interest in real property that is the debtor's principal residence...." 11 U.S.C. §1322(b)(2). Such a plan may, however, cure any default on a long-term debt, such as a mortgage. 11 U.S.C. §1322(b)(5).

Prior to the Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, there was no provision in section 1322 or any other section of the Bankruptcy Code which governed how to effectuate a cure of a mortgage default. As a result, the allowance of interest on mortgage arrearages became the subject of some controversy. *See Rake v. Wade*, 508 U.S. 464, 466 & n.2 (1993) (collecting cases). In *Rake v. Wade*, the Supreme Court resolved this controversy concluding that sections 506(b),<sup>3</sup> 1322(b) and 1325(a)(5)<sup>4</sup> of the Bankruptcy Code mandate that oversecured creditors be paid reconfirmation and postconfirmation interest on mortgage arrearage claims cured pursuant to the terms of a chapter 13 plan. *Id.* at 464.

A little over one year after the Supreme Court decided *Rake*, Congress, as part of the Bankruptcy Reform Act of 1994, enacted section 1322(e) which states that "[n]otwithstanding

---

<sup>3</sup> See 11 U.S.C. §506(b); see also *United States v. Ron Pair Enterp., Inc.*, 489 U.S. 235 (1989) (right to postpetition interest on oversecured debt is unqualified under section 506(b) and exists regardless of whether the agreement giving rise to secured claim provides for interest).

<sup>4</sup> Under section 1325(a)(5), a chapter 13 plan will not be confirmed unless: (1) secured creditors accept the plan; (2) the debtor surrenders the property securing the secured creditors' claims; or (3) secured creditors retain their liens and "the value, as of the effective date of the plan, of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim...." 11 U.S.C. §1325(a)(5).

subsection (b)(2) of this section and sections 506(b) and 1325(a)(5) of this title, if it is proposed in a plan to cure a default, the amount necessary to cure the default, shall be determined in accordance with the underlying agreement and applicable nonbankruptcy law." 11 U.S.C. §1322(e). This subsection has "the effect of overruling" *Rake*. 140 Cong. Rec. H 10,770 (Oct. 4, 1994). The legislative history to section 1322(e) states:

Notwithstanding State law, [*Rake*] has had the effect of providing a windfall to secured creditors at the expense of unsecured creditors by forcing debtors to pay the bulk of their income to satisfy the secured creditors' claims. This had the effect of giving secured creditors interest on interest payments, and interest on the late charges and other fees, even where applicable law prohibits such interest and even when it was something that was not contemplated by either party in the original transaction... [Section 1322(e)] will limit the secured creditor to the benefit of the initial bargain with no court contrived windfall. It is the Committee's intent that a cure pursuant to a plan should operate to put the debtor in the same position as if the default had never occurred.

*Id.* It is now clear under section 1322(e) that a mortgagee is not permitted to collect interest on arrearages being cured in a chapter 13 plan, unless its contract so provides and such interest is not prohibited under applicable nonbankruptcy law.

Congress expressly provided that section 1322(e) should "apply only to agreements entered into after [October 22, 1994]." Pub. L. No. 103-394, §702(b)(2)(D) (1994); *see also* 140 Cong. Rec. H 10,770 (Oct. 4, 1994) ("This provision will be applicable prospectively only, i.e., it will be applicable to all future contracts, including transactions that refinance existing contracts...") In cases involving agreements entered into prior to or on October 22, 1994, *Rake* is controlling and secured creditors are entitled to interest on arrearages proposed to be cured in a chapter 13 plan.

## CONCLUSION

In both of the pending cases, section 1322(e) prohibits payment of interest on the secured creditors' prepetition mortgage default claims,<sup>5</sup> absent a contrary provision in the underlying agreement or applicable nonbankruptcy law. Since each of the debtors modified their chapter 13 plans in response to the objections filed by the Standing Chapter 13 Trustee to conform to the statute, it is hereby

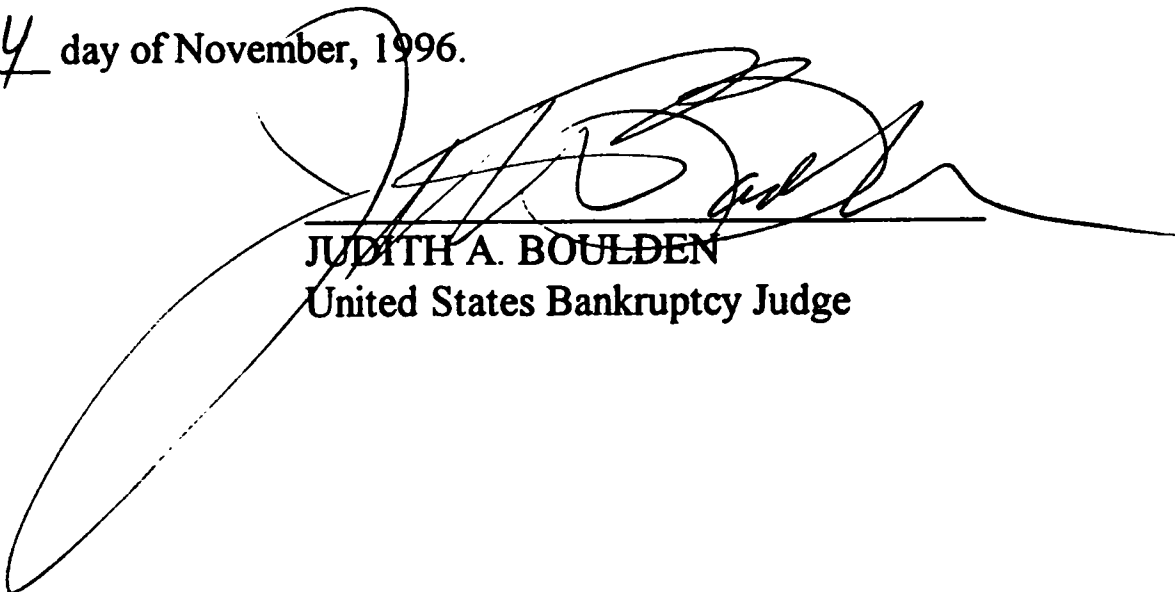
**ORDERED**, that the Standing Chapter 13 Trustee's objection to confirmation of Dennis and Shelly Vario's proposed chapter 13 plan is sustained, and it is further

**ORDERED**, that the plan as amended to delete the provision for payment of interest to the prepetition mortgage default creditor is confirmed, and it is further

**ORDERED**, that the Standing Chapter 13 Trustee's objection to confirmation of Larry and Kimberly Boswell's proposed chapter 13 plan is sustained, and it is further

**ORDERED**, that the plan as amended to delete the provision for payment of interest to prepetition mortgage default creditors is confirmed.

**DATED** this 14 day of November, 1996.



JUDITH A. BOULDEN  
United States Bankruptcy Judge

---

<sup>5</sup> The Money Store may assert that it is entitled to interest on the principle only of its prepetition default claim, but has declined to modify its proof of claim to break out that portion of its principle and interest claim applicable to principle only. Therefore the Court does not address this issue.