WHO'S LEFT SUSPENDED ON THE LINE?: THE OMINOUS HANGING PARAGRAPH AND THE SEVENTH CIRCUIT'S INTERPRETATION IN *IN RE WRIGHT*

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INTRODUCTION

For decades, bankruptcy reform has been controversial. Believing that gaps in the then-existing bankruptcy laws provided the means by which the bankruptcy system was being exploited[1] and thus, the impetus for at least some of the dissention, Congress enacted the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA).[2] However, rather than improve matters, the legislation arguably resulted in even *more* controversy. And though the consequences of this legislation were not limited to any one form of bankruptcy filing,[3] an intense debate ensued with respect to a

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[1] *See* H.R. REP. No. 109-31, pt. 1 (2005).

[2] Pub. L. No. 109-8, 119 Stat. 23 (codified in part as 11 U.S.C. § 1325 (2005)).

[3] Brett Weiss, *"Not Dead Yet:" Bankruptcy After BAPCPA*, MD. B.J., May-June 2007, at 17, 18-20. For example, enactment of the BAPCPA resulted in, *inter alia,* mandatory credit counseling for Chapter 7 and Chapter 13 filers, required means testing to determine eligibility for Chapter 7, and refiling restrictions for Chapter 7 debtors. *Id*.

provision of the BAPCPA affecting Chapter 13 proceedings exclusively.[4] Specifically, the dispute centered around the "hanging paragraph"—the unnumbered paragraph following § 1325(a)(9).[5]

The Seventh Circuit, in *In re Wright*, became the first court of appeals to interpret the hanging paragraph.[6] The decision in this case limits the conditions under which a bankruptcy court shall confirm the Chapter 13 repayment plan of a 910 debtor.[7] It did so by holding the debtor accountable for its original contractual obligations, where the debtor proposed in its repayment plan, to surrender its 910 vehicle to the 910 creditor.[8]

In *In re Wright*, at the time that the 910 debtors proposed their Chapter 13 repayment plan, they owed more on the loan for their vehicle than the vehicle was worth.[9] Despite the difference between the loan's balance and the market value of the vehicle, the debtors proposed a Chapter 13 repayment plan whereby they would surrender their vehicle to the 910 creditor in full satisfaction of the debt.[10] The issue on appeal was whether the BAPCPA allowed the debtors to surrender their vehicle in complete satisfaction of their debt obligations or, alternatively, if the creditor was entitled to an unsecured

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[4] *See* In re Graupner, 356 B.R. 907, 911 (Bankr. D. Ga. 2006).

[5] 11 U.S.C. § 1325(a)(9). The "hanging paragraph" is so named, as it "has no alphanumeric designation and merely dangles at the end of § 1325(a)." Dianne C. Kems, *Cram-a-lot: The Quest Continues*, AM. BANKR. INST. J., Nov. 2005, at 10.

[6] 492 F.3d 829 (7th Cir. 2007).

[7] *See id.* at 833.

[8] *Id.* A "910 creditor" is a creditor who possesses a purchase money security interest (PMSI) in a vehicle acquired by a Chapter 13 debtor for the debtor's personal use during the 910 days prior to the debtor's filing of a Chapter 13 bankruptcy petition. *See* 11 U.S.C. § 1325(a). Similarly, the vehicle is referred to as a "910 vehicle;" the debtor, a "910 debtor." *See id.* Because the Bankruptcy Code does not provide a definition of the term "purchase money security interest," courts interpreting it have looked to state law. In re Stevens, 368 B.R. 5, 8 (Bankr. D. Neb. 2007) (citing In re Price, 363 B.R. 734 (Bankr. E.D.N.C. 2007)). Generally, a "purchase money security interest" is defined as a security interest created when a buyer uses the lender's money to make the purchase and immediately gives the lender security. BLACK'S LAW DICTIONARY 1127 (8th ed. 2005).

[9] *In re Wright*, 492 F.3d at 831.

[10] *Id.*

claim in the amount of the difference that remained on the loan after surrender.[11] In affirming the decision of the bankruptcy court and thereby adopting the minority view among bankruptcy courts, the Seventh Circuit held that while the BAPCPA prohibits the application of § 506[12] to the claim of a 910 creditor, in the absence of § 506 the debtor is left with its original, contractual responsibilities.[13] The Seventh Circuit looked to Article 9 of the Uniform Commercial Code ("U.C.C.") and to the parties' contract and concluded that upon the debtors' surrender of their vehicle, the creditor was "entitled to an (unsecured) deficiency judgment for the difference between the value of the collateral and the balance on the loan."[14]

Section I of this note outlines the relevant bankruptcy law, including the BAPCPA. Section II discusses the differing views between the bankruptcy courts. Section III analyzes the Seventh Circuit's recent opinion in *In re Wright*. Section IV discusses why the Seventh Circuit's holding in *In re Wright*, that in the absence of § 506 the parties are left with their original contractual agreements, was correct. Section V concludes that in adopting the minority view among bankruptcy courts, the Seventh Circuit chose the proper interpretation of the hanging paragraph.

I. THE BANKRUPTCY CODE

In a time when consumers are bombarded with unsolicited offers for credit, it is not surprising that they may sometimes find themselves overextended and unable to meet their resulting payment obligations.[15] Congress—by way of the Bankruptcy Code—attempted to provide

[11] *Id.* at 830-31.

[12] 11 U.S.C. § 506 (2006).

[13] *In re Wright*, 492 F.3d at 832-33.

[14] *Id.* at 833.

[15] *See* Julie L. Williams, Acting Comptroller of the Currency, Speech before the American Bankers Association on Credit Underwriting Standards (Sept. 27, 1998), *in* O.C.C. Q.J., Dec. 1998, at 108.

relief to strained debtors in the form of a Chapter 7, Chapter 11, or Chapter 13 bankruptcy filing.[16]

Chapter 13 is "a form of bankruptcy relief where the debtor commits to repay a portion or all of his debts in exchange for receiving a broad discharge of debt."[17] As such, a Chapter 13 filing is often used by debtors who are "on the way up" as a result of an improved financial situation.[18] In a Chapter 13 bankruptcy filing, a debtor is required to prepare a plan of repayment that must be confirmed by the bankruptcy court.[19] Pursuant to § 1325(a)(5),[20] the court "shall confirm" the plan if the debtor addresses its secured debt in one of three ways.[21] First, the creditor may agree to the debtor's proposed treatment of the creditor's claim.[22] Second, the debtor may keep the collateral by allowing the creditor to retain the lien on the collateral until the debtor has made payments totaling the amount of the creditor's claim.[23] Finally, the debtor may surrender the collateral to the creditor.[24] It is in the context of the last alternative that the

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[16] *See* FCC v. NextWave Pers. Comm'ns Inc., 537 U.S. 293, 305 (2003). While the elements of these proceedings differ, the scope of this article is limited to bankruptcy filings made pursuant to Chapter 13.

[17] H.R. REP. No. 109-31, pt. 1 (2005).

[18] Henry E. Hildebrand III, *Unintended Consequences: BAPCPA and the New Disposable Income Test*, AM. BANKR. INST. J., May 2006, at 14.

[19] 11 U.S.C. § 1325.

[20] 11 U.S.C. §1325(a)(5).

[21] *Id.* The pertinent part of the statute states the options for plan confirmation:

> (A) the holder of [the secured] claim has accepted the plan; (B) (i) the plan provides that—(I) the holder of [the secured] claim retain the lien securing such claim until . . . (aa) the payment of the underlying debt . . . and (ii) 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; or . . . (C) the debtor surrenders the property securing such claim to such holder.

Id.

[22] 11 U.S.C. § 1325(a)(5)(A).

[23] 11 U.S.C. § 1325(a)(5)(B). Courts have termed this process "cramdown." *In re* Wright, 492 F.3d 829, 830 (7th Cir. 2007).

[24] 11 U.S.C. § 1325 (a)(5)(C).

BAPCPA has created great discord among the bankruptcy courts.[25] Namely, courts have had to address the effect of the newly added hanging paragraph in this situation and answer the question of whether, upon the debtor's surrender of the vehicle, the 910 creditor possesses an unsecured claim equal to the amount of any deficiency or whether the surrender fully satisfies the 910 creditor's claim.[26]

A. Pre-BAPCPA

Prior to the enactment of the BAPCPA, a Chapter 13 debtor was given three options for the disposition of the collateral—convince the creditor to accept the plan, keep the collateral and make payments totaling the value of the collateral, or surrender the collateral to the creditor. Further, in the simple—or at least *simpler*—pre-BAPCPA times, the claims of all Chapter 13 secured creditors were treated equally.[27] The claims of a 910 creditor and any other Chapter 13 secured creditor were subject to § 506, which provides that:

> (1) [a]n allowed claim of a creditor secured by a lien on property in which the estate has an interest, or that is subject to setoff under section 553 of this title, is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property, or to the extent of the amount subject to setoff, as the case may be, and is an unsecured claim to the extent that the value of such creditor's interest or the amount so subject to set off is less than the amount of such allowed claim. Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in

[25] *See In re* Graupner, 356 B.R. 907, 911 (Bankr. D. Ga. 2006).

[26] *See In re* Pinti, 363 B.R. 369 (Bankr. S.D.N.Y. 2007); *In re* Ezell, 338 B.R. 330 (Bankr. E.D. Tenn. 2006); *In re* Particka, 355 B.R. 616 (Bankr. E.D. Mich. 2006); *In re* Zehrung, 351 B.R. 675 (W.D. Wis. 2006).

[27] *See id*. at 334-35.

> conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest.[28]

Thus, the claims of all Chapter 13 secured creditors were subject to bifurcation.[29] As such, a Chapter 13 secured creditor, including a 910 creditor, was entitled to a secured claim in the amount of the value of the collateral.[30] Where the creditor's claim exceeded this amount, the creditor was entitled to an unsecured claim for the deficiency.[31] Accordingly, the unsecured claim was treated identically to that of the remaining general unsecured claims asserted by the debtor's other creditors.[32]

B. Post-BAPCPA

Although bankruptcy law has seen its fair share of changes, no amendment since the Bankruptcy Reform Act of 1978[33] has been as comprehensive as the BAPCPA.[34] Referred to as the "new bankruptcy law"[35], the BAPCPA was enacted in response to several factors[36] that Congress believed necessitated extensive reform of the Bankruptcy

[28] 11 U.S.C. § 506 (2006); *see In re Ezell*, 338 B.R. at 338.
[29] *See In re Ezell*, 338 B.R. at 338-40.
[30] *Id.*
[31] *Id.* at 338-40.
[32] *See id.*
[33] Pub. L. No. 95-598, 92 Stat. 254 (1978).
[34] 151 CONG. REC. H1993-01, at H2047-48 (daily ed. Apr. 14, 2005) (statement of Rep. Sensenbrenner) ("This legislation represents the most comprehensive reforms of the bankruptcy system in more than 25 years.").
[35] *E.g.* The Law Offices of John T. Orcutt, Website Home Page, http://www.billsbills.com (last visited Nov. 28, 2007).
[36] These factors include: the determination that the increase in bankruptcy filings was not temporary but rather part of a consistent upward trend, the substantial losses that resulted from bankruptcy filings, loopholes that allowed abuse of the bankruptcy system, and findings that some bankruptcy debtors were able to repay much of their debt. H.R. REP. No. 109-31, pt. 1 (2005).

Code.[37] The most notable change effectuated by the BAPCPA was to Chapter 13 bankruptcy filings—namely, the BAPCPA's hanging paragraph and its resulting effect on the claims of a 910 creditor.[38]

While the BAPCPA changed certain provisions, others, such as §§ 1325(a)(5)(A)[39] and (C),[40] were left unchanged and § 1325(a)(5)(B)[41] was modified largely to include more detailed terms and specific requirements relating to the section.[42] Consequently, following the enactment of the BAPCPA, the debtor still had the same three options for the disposition of the collateral—acceptance by the creditor, retention of the collateral, or surrender of the collateral.[43] However, the enactment of the BAPCPA added the hanging paragraph to § 1325.[44] This provision provides that:

> [f]or purposes of paragraph (5),[45] section 506 shall not apply to a claim described in that paragraph if the creditor has a purchase money security interest securing the debt that is the subject of the claim, the debt was incurred within the 910-day preceding the date of the filing of the petition, and the collateral for that debt consists of a motor vehicle (as defined in section 30102 of title 49) acquired for the personal use of the debtor, or[46] if collateral for that debt

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[37] *See generally* Joseph Satorius, Note, *Strike or Dismiss: Interpretation of the BAPCPA 109(h) Credit Counseling Requirement*, 75 FORDHAM L. REV. 2231, 2237 (2007).

[38] *In re* Morales, 359 B.R. 211, 215 (Bankr. N.D. Ill. 2007).

[39] 11 U.S.C. § 1325(a)(5)(A) (2006).

[40] 11 U.S.C. § 1325(a)(5)(C).

[41] 11 U.S.C. § 1325(a)(5)(B).

[42] *In re* Particka, 355 B.R. 616, 618 (Bankr. E.D. Mich. 2006).

[43] *Id.*

[44] Pub. L. No. 109-8, 119 Stat. 23 (codified in part as 11 U.S.C. § 1325).

[45] This referenced paragraph is 11 U.S.C. § 1325(a)(5) which provides the debtor with three methods by which to have a Chapter 13 repayment plan confirmed. *See supra* Part IB.

[46] As this second situation to which the BAPCPA applies is beyond the scope of this article, it will not be discussed further.

consists of any other thing of value, if the debt was incurred during the 1-year period preceding that filing.[47]

As a result of the addition of the hanging paragraph, the claims of all Chapter 13 secured creditors are no longer treated the same.[48] Rather, the hanging paragraph distinguishes between the claims of 910 creditors and those of other Chapter 13 secured creditors.[49] In so doing, the BAPCPA prohibits the application of § 506 and, thus, bifurcation of the claims of 910 creditors.[50] Although the statute prohibits bifurcation of the claim regardless of the debtor's proposed disposition of the vehicle,[51] this prohibition leads to two very different results depending on whether the debtor retains or surrenders the vehicle.[52]

In the instance where the debtor proposes to retain the 910 vehicle, it is true that bifurcation is forbidden—but this is irrelevant, as the debtor must agree to pay the 910 creditor the full value of the creditor's claim.[53] In this scenario, the law is well-settled.[54] However, appropriate application of the law is less clear in the frequent scenario where the debtor intends to surrender the vehicle to the 910 creditor.[55]

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[47] 11 U.S.C. § 1325(a) (2006).

[48] *See In re* Ezell, 338 B.R. 330, 338 (Bankr. E.D. Tenn. 2006).

[49] 11 U.S.C. § 1325 (2006); *In re Ezell*, 338 B.R. at 340.

[50] 11 U.S.C. § 1325.

[51] *Id.*

[52] *See In re* Zehrung, 351 B.R. 675, 678 (W.D. Wis. 2006).

[53] 11 U.S.C. § 1325(a)(5)(B).

[54] *See generally In re* Shaw, 341 B.R. 543 (Bankr. M.D. N.C. 2006); *In re* Turner, 349 B.R. 431 (Bankr. D. S.C. 2006); *In re* White, 352 B.R. 633 (Bankr. E.D. La. 2006); *In re* Solis, 356 B.R. 398 (Bankr. S.D. Tex. 2006). In this scenario, the debtor must pay the full amount of the claim even if the vehicle is worth less than the claim.

[55] *Compare In re* Pinti, 363 B.R. 369, 369 (Bankr. S.D.N.Y. 2007) (holding that a 910 creditor is not entitled to an unsecured claim for the amount of the deficiency), *and In re* Ezell, 338 B.R. 330, 330 (Bankr. E.D. Tenn. 2006) (910 creditor's claim is fully satisfied upon surrender despite deficiency), *with In re* Particka, 355 B.R. 616, 616 (Bankr. E.D. Mich. 2006) (910 creditor entitled to an unsecured claim in the amount of the deficiency), *and In re Zehrung*, 351 B.R. at 675 (creditor allowed to assert an unsecured claim for the amount of the deficiency).

Suppose the debtor's 910 vehicle was valued at $12,000 and the creditor filed a claim in the amount of $15,000, representing the amount owing on the loan. If the debtor keeps the vehicle—though the claim is not bifurcated into a secured and unsecured portion—the debtor must pay the creditor the full $15,000. This outcome is the same in all courts. However, the result is not as clear in the scenario where the debtor surrenders the vehicle. In courts adopting the majority view, the creditor would only receive $12,000, satisfied by the vehicle's surrender. The debtor would not be responsible for the remaining $3,000 even if the parties' contract so provided. Conversely, in courts subscribing to the minority view, the creditor would be entitled to the full $15,000. The surrender of the vehicle would satisfy $12,000 and the creditor would be allowed an unsecured claim for the remaining $3,000.[56]

II. DISSENT THROUGHOUT THE BANKRUPTCY COURTS

Because of the difficulties encountered when interpreting the hanging paragraph, two diverse series of opinions have emerged from the bankruptcy courts.[57] "As of last count—by a margin of 3–1—the vast majority of reported cases favor the position . . . that the 910 creditor can, through the confirmation of a proposed plan, be compelled to accept the surrender of its collateral in full satisfaction of its claims."[58] Not only is there conflict among the various circuits but conflicting opinions within circuits have also begun to emerge.[59]

[56] A distinction must be made at this point. Although it is not likely that the holders of general unsecured claims would be paid the full amount of their claim, the holder of an unsecured claim is at least *theoretically* entitled to the full value of the claim. How much the creditor receives, however, depends on, *inter alia*, the bankruptcy estate's value, the number and nature of the creditors, the amount of the claims, and the number of claims.

[57] *In re* Roth, No. 06-11330, 2007 Bankr. LEXIS 1647, at *2 (N.D. Ind. May 4, 2007), *rev'd*, No. 1:07-CV-135-TS, 2007 U.S. Dist. LEXIS 80162 (N.D. Ind. Oct. 25, 2007).

[58] *Id.*

[59] *Compare In re* Kenney, Nos. 06-71975-A, 07-70359-A, 2007 Bankr. LEXIS 1646 (Bankr. E.D. Va. May 11, 2007) (applying the majority position), *with In re*

Consequently, this article does not endeavor to categorize circuits based upon whether the circuit subscribes to the majority or the minority view of the issue. Rather, the article sets forth each opposing view and provides representative cases from the bankruptcy courts that have adhered to the particular position. While the varying views will be presented, the focus of this article is the Seventh Circuit's decision in *In re Wright*, whereby the Seventh Circuit adopted the minority view that where there exists a deficiency after surrender, the creditor is entitled to an unsecured claim for that amount.[60]

The importance of a consistent application of the hanging paragraph among all bankruptcy courts is apparent in light of the fact that this issue arises in a substantial number of consumer Chapter 13 bankruptcy proceedings.[61] Considering the rising costs of litigation, potential Chapter 13 debtors and 910 creditors alike would be well-served by uniform treatment of the hanging paragraph.[62]

A. The Majority's Interpretation of the Hanging Paragraph

A large number of courts adopting the majority interpretation maintain the view that the language of the hanging paragraph is unambiguous.[63] These courts reason that the hanging paragraph

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Long, No. 06-10601, 2007 Bankr. LEXIS 2423 (Bankr. W.D. N.C. Feb. 1, 2007) (applying the minority approach).

[60] 492 F.3d 829, 833 (7th Cir. 2007).

[61] *Id.* at 831.

[62] *Id.*

[63] *See In re* Pinti, 363 B.R. 369, 376 (Bankr. S.D.N.Y. 2007); *In re* Wampler, 345 B.R. 730, 740 (Bankr. D. Kan. 2006); *In re* Curtis, 345 B.R. 756, 760 (Bankr. D. Utah 2006); *In re* Ezell, 338 B.R. 330, 341 (Bankr. E.D. Tenn. 2006); *In re* Osborn, 348 B.R. 500, 504 (Bankr. W.D. Mo. 2006); *In re* Quick, 360 B.R. 722, 728 (Bankr. N.D. Okla. 2007); *In re* Steakley, 769, 770 n.1 (Bankr. E.D. Tenn. 2007); *In re* Bivins, No. 06-51778 RFH, 2007 Bankr. LEXIS 519, at *8 (Bankr. D. Ga. Feb. 23, 2007); *In re* Feddersen, 355 B.R. 738, 741 (Bankr. S.D. Ill. 2006); *In re* Pool, 351 B.R. 747, 752 (Bankr. D. Or. 2006); *In re* Nicely, 349 B.R. 600, 604 (Bankr. W.D. Mo. 2006); *In re* Payne, 347 B.R. 278, 282 (Bankr. S.D. Ohio 2006); *In re* Long, No. 06-30651, 2006 Bankr. LEXIS 1605, at *30 (Bankr. E.D. Tenn. July 12, 2006). Similarly, a number of courts subscribing to the minority view have also found the statute to be unambiguous. *See In re* Morales, 359 B.R. 211, 215 (Bankr. N.D. Ill.

explicitly states its applicability to a 910 claim and expressly prohibits bifurcation of the claim.[64] Arguing that the invocation of § 506 is the sole means of bifurcating a creditor's claim, the courts assert that in the absence of § 506, a 910 creditor is not allowed to bifurcate its claim.[65]

The bankruptcy court in *In re Pinti* acknowledged that the hanging paragraph was "poorly drafted" but found the language of the statute to be unambiguous.[66] Though the *In re Pinti* court recognized that state law controls the creation and perfection of a lien, the court held this to be the extent of state law's authority with respect to the lien and any claim that may arise in relation to it once the debtor has entered into bankruptcy.[67] After the filing of the debtor's bankruptcy petition, the "Bankruptcy Code, and not state law, determines whether and to what extent such claim should be allowed in the bankruptcy estate."[68] The court asserted that § 506 was the "starting point" in making this determination.[69] Because the court maintained that the hanging paragraph prohibits application of this provision to claims by 910 creditors, the court held that the creditor was not entitled to an unsecured claim for the deficiency.[70] Additionally, the court noted that its holding would remain unchanged regardless of whether the debtor retained or surrendered the 910 vehicle.[71]

2007); *In re* Hoffman, 359 B.R. 163, 166 (Bankr. E.D. Mich. 2006); *In re* Particka, 355 B.R. 616, 625 (Bankr. E.D. Mich. 2006).

[64] *See In re Pinti*, 363 B.R. at 376; *In re Wampler*, 345 B.R. at 736; *In re Quick*, 360 B.R. at 722; *In re Payne*, 347 B.R. at 278.

[65] *See supra* note 64.

[66] 363 B.R. at 369.

[67] *Id.*

[68] *Id.*

[69] *Id.*

[70] *Id.*

[71] *Id.*

B. The Minority's Position of the Applicability of the Hanging Paragraph

A minority of bankruptcy courts hold that a 910 creditor may assert an unsecured claim for any amount remaining after the debtor's surrender of the 910 vehicle.[72] Although these courts reach the same end result, they utilize different arguments to arrive at the conclusion. Some courts, such as the Seventh Circuit in *In re Wright*, maintain that with § 506 gone, both the debtor and creditor are left with their contractual rights and obligations, as defined by state law.[73] According to the courts that adopt this reasoning, where the contract and/or the appropriate UCC provision of the state provides for a deficiency, the 910 creditor is entitled to assert an unsecured deficiency claim for that amount.[74] Because of this entitlement, the 910 creditor may not be forced to accept the vehicle in full satisfaction of the creditor's claim.[75] Other courts maintain that where the debtor surrenders the 910 vehicle, it passes out of the bankruptcy estate and is no longer confined by the strictures of § 506.[76] In these courts, because the bankruptcy law does not apply, the parties are left to their original contractual obligations. Still other courts assert that the language of the statute is ambiguous.[77] Finding that the legislative history demonstrates Congress's intent that the BAPCPA provide greater protection to 910 creditors, these courts hold that the creditor is entitled to assert an unsecured claim for any deficiency.

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[72] *See*, *e.g.*, *In re* Morales, 359 B.R. 211, 217 (Bankr. N.D. Ill. 2007); *In re* Particka, 355 B.R. 616, 629 (Bankr. E.D. Mich. 2006); *In re* Zehrung, 351 B.R. 675, 678 (Bankr. W.D. Wis. 2006); *In re* Duke, 345 B.R. 806, 809 (Bankr. W.D. Ky. 2006).

[73] 492 F.3d 829 (7th Cir. 2007).

[74] *Id.*

[75] *See* sources cited *supra* note 72.

[76] *See*, *e.g.*, I*n re Zehrung*, 351 B.R. at 678.

[77] *See*, *e.g.*, *id.* at 678.

1. Upon Its Surrender, the 910 Vehicle is No Longer Part of the Estate[78]

The bankruptcy court in *In re Zehrung* recognized that the BAPCPA prohibits the use of § 506 for the claims of 910 creditors but found that this was not the relevant provision of the bankruptcy code.[79] This provision applies only when the bankruptcy estate retains an interest in the 910 vehicle—an interest which "disappears with surrender."[80] The court found its interpretation of the hanging paragraph to be consistent not only with the statute's language but also with Congress's intent in enacting the legislation.[81] The *In re Zehrung* court noted that the title of the section of the BAPCPA which added the hanging paragraph is "Section 306—Giving Secured Creditors Fair Treatment in Chapter 13 . . . Restoring the Foundation for Secured Credit."[82] Given Congress's express objectives, the court found it improbable that the BAPCPA was intended to abrogate the rights of a 910 creditor to an unsecured deficiency claim—a right that the creditors were entitled to prior to the enactment of the statute.[83] The court further noted the result obtained under the majority's approach—the expansion of rights to the creditor where the debtor keeps the vehicle and the reduction of rights to the creditor where the collateral is surrendered.[84] Consequently, the court held that the creditor was entitled to liquidate the vehicle and assert an unsecured claim for the remaining balance.[85]

[78] *See supra* note 72.
[79] 351 B.R. at 677-78.
[80] *Id.*
[81] *Id.*
[82] *Id.*
[83] *Id.*
[84] *Id.*
[85] *Id.* at 678.

2. The Hanging Paragraph is Ambiguous[86]

Because the court in *In re Duke* found the language of the hanging paragraph to be ambiguous, it looked to the legislative history.[87] While the court acknowledged that the history is limited, it discerned indicators that Congress, in passing the BAPCPA, sought to discourage bankruptcy abuse.[88] Like the court in *In re Pinti*, the *In re Duke* court noted that the title of the section of the BAPCPA which added the hanging paragraph is, "Section 306—Giving Secured Creditors Fair Treatment in Chapter 13 . . . Restoring the Foundation for Secured Credit."[89] Therefore, the court reasoned that it was clear that Congress intended to provide secured creditors with greater protection.[90] Forcing a creditor to accept surrender of the collateral in full satisfaction of its claim would eliminate the creditor's deficiency claim and was therefore contrary to Congress's purpose behind enacting the statute. Absent a clear indication that Congress intended this "anti-deficiency" result, the court held that upon surrender of the vehicle, the creditor was entitled to pursue the remedies available to it under state law.[91] Namely, the creditor was entitled to an unsecured claim in the amount of the deficiency.[92]

III. *IN RE WRIGHT*: THE SEVENTH CIRCUIT BECOMES THE FIRST COURT OF APPEALS TO ADDRESS THE ISSUE

In *In re Wright,* the Seventh Circuit was asked to decide whether the hanging paragraph precluded a 910 creditor from asserting an unsecured claim for the amount of the balance that remained after the debtors' surrender of the automobile.[93] The debtors in *In re Wright*

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[86] *In re* Duke, 345 B.R. 806, 809 (Bankr. W.D. Ky. 2006).
[87] *Id.*
[88] *Id.*
[89] *Id.*
[90] *Id.*
[91] *Id.*
[92] *Id.*
[93] *In re* Wright, 492 F.3d 829, 829 (7th Cir. 2007).

purchased a vehicle and, in so doing, entered into a contract where they agreed to be responsible for any deficiency in the event that the vehicle was seized and liquidated due to non-payment.[94] Within 910 days of the purchase, the debtors filed their bankruptcy petition.[95] They subsequently proposed a Chapter 13 repayment plan whereby they would surrender the vehicle to the creditor in full satisfaction of the loan.[96] The debtors did not propose to pay any of the deficiency and as a result, the bankruptcy judge declined to confirm their Chapter 13 plan.[97] Pursuant to 28 U.S.C. § 158(d)(2)(A),[98] the bankruptcy judge certified that the case satisfied subparagraphs (i) and (ii) of the statute.[99] The Seventh Circuit accepted the bankruptcy court's certification, noting that this issue arises in a large number of consumer cases but appears to be "stuck" in the bankruptcy courts.[100] The court affirmed the decision of the bankruptcy court and in doing

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[94] *Id*. at 830.
[95] *Id*. at 832.
[96] *Id*. at 831.
[97] *Id*.
[98] *Id*. The statute provides:

> The appropriate court of appeals shall have jurisdiction of appeals described in the first sentence of subsection (a) if the bankruptcy court, the district court, or the bankruptcy appellate panel involved, acting on its own motion or on the request of a party to the judgment, order, or decree described in such fist sentence, or all the appellants and appellees (if any) acting jointly, certify that – (i) the judgment, order or decree involves a question of law as to which there is no controlling decision of the court of appeals for the circuit or of the Supreme Court of the United States, or involves a matter of public importance; (ii) the judgment, order, or decree involves a question of law requiring resolution of conflicting decisions; or (iii) an immediate appeal from the judgment, order, or decree may materially advance the progress of the case or proceeding in which the appeal is taken; and if the court of appeals authorizes the direct appeal of the judgment, order, or decree.

28 U.S.C. § 158(d)(2)(A) (2006).
[99] *In re Wright*, 492 F.3d at 831.
[100] *Id*. at 833.

so adopted the minority view among bankruptcy courts.[101] The court agreed that the hanging paragraph eliminates the application of § 506 to the claims at issue and thus the requirement that claims be bifurcated into secured and unsecured claims.[102] However, the Seventh Circuit argued that § 506 is not "the *only* source of authority for a deficiency judgment when the collateral is insufficient."[103]

Judge Easterbrook considered the United State Supreme Court's decision in *Butner v. United States*,[104] and the court's holding that when the Code does not provide a federal rule, state law determines rights and obligations.[105] Because the hanging paragraph prohibits the application of § 506 to 910 claims post-BAPCPA, the debtors were left with their original contractual obligations and the 910 creditor was left with its rights specified in the contract.[106] The contract that debtors entered into with the creditor provided that if the loan was not paid, the vehicle would be seized and sold.[107] Further, the contract explicitly provided that upon seizure and liquidation of the automobile, the creditor would refund any surplus to the debtors.[108] However, in the event that the vehicle was sold for less than the amount of the loan, the debtors "shall be liable for any deficiency."[109] This contract, Judge Easterbrook held, created a secured loan with recourse against the borrower.[110] The contract further provided that the parties were entitled to all of their rights as specified in the U.C.C.[111] The court then consulted 810 ILL. COMP. STAT. 5/9-615(d),[112] the applicable

[101] *Id.* at 832.
[102] *Id.*
[103] *Id.*
[104] 440 U.S. 48 (1979).
[105] *In re Wright*, 492 F.3d at 832.
[106] *Id.*
[107] *Id.*
[108] *Id.*
[109] *Id.*
[110] *Id.*
[111] *Id.*
[112] The pertinent part of 810 ILL. COMP. STAT. 5/9-615(d)(2) (2007) states that, "If the security interest under which a disposition is made secures payment or performance of an obligation, after making the payments and applications required

U.C.C. provision enacted by Illinois, and held that upon surrender of the automobile, the creditor was entitled to an unsecured claim for the difference between the car's value and the balance of the loan.[113] Judge Easterbrook went on to pose a hypothetical in which debtors surrendered the automobile just one day prior to the filing of their Chapter 13 petition.[114] The court reasoned, based upon the parties' contract and the appropriate Illinois statute,[115] that under those circumstances, the creditor would have been entitled to assert an unsecured claim for any amount by which the loan exceeded the value of the vehicle.[116] The Seventh Circuit noted this anomalous outcome[117]—the creditor would have been allowed a deficiency the day *before* filing a bankruptcy petition but denied a deficiency just one day *after* filing.[118] Not finding an operative provision in the Code to the contrary, Judge Easterbrook then looked to the title of the statute that enacted the hanging paragraph.[119] Discerning what he believed to be Congress's intent to provide protection for secured creditors, Judge Easterbrook reasoned that the hanging paragraph replaced a "contract-defeating provision such as § 506" (which allows judges rather than the market to value the collateral and set an interest rate, and may prevent creditors from repossessing [the vehicle]) with the agreement freely negotiated between debtor and creditor."[120]

Judge Easterbrook also refuted the assertions of the National Association of Consumer Bankruptcy Attorneys, appearing as amicus curiae, that the hanging paragraph completely eliminates the 910

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by subsection (a) and permitted by subsection (c) . . . the obligor is liable for any deficiency. 810 ILL. COMP. STAT 5/9-615(d)(2).

[113] *In re Wright*, 492 F.3d at 832.

[114] *Id.*

[115] 810 ILL. COMP. STAT. 5/9-615(d)(2).

[116] *In re Wright*, 492 F.3d at 832.

[117] *Id.* While other events are triggered the day *after* filing bankruptcy where they would not have been the day *before* bankruptcy, the court seemingly found this result inconsistent with Congress's purpose in enacting the BAPCPA. *See id.* at 832.

[118] *Id.*

[119] *Id.*

[120] *Id.*

creditor's secured status.[121] The reasoning of the amici was flawed, the court asserted, because it assumed that § 506 was the only source in bankruptcy of a secured creditor's rights.[122] These considerations led Judge Easterbrook to hold that while the debtors were not required to pay the unsecured debt in full any more than they were obligated to pay the full amount of their other unsecured debts, the creditor's unsecured claim could not "be written off *in toto* while other unsecured creditors are paid some fraction of their entitlements."[123] In other words, Judge Easterbrook decided that the creditor was allowed at least the *right* to receive a portion of its unsecured claim—the same percentage that other creditors with unsecured claims were entitled.

IV. The Seventh Circuit Made the Right Decision in *In re Wright*

In *In re Wright*, the Seventh Circuit made an important decision: in cases where the value of the 910 vehicle is insufficient, § 506 does not provide the sole source of authority for a deficiency judgment.[124] This determination is not only consistent with the statute and state law but it is also in line with Congress's purpose in enacting the BAPCPA.

A. The Hanging Paragraph and State Law

In *Butner v. United States*[125] the Supreme Court, desiring uniform treatment of property interests in state and federal courts, held that,

> Property interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a *bankruptcy proceeding*.[126]

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[121] *Id.*
[122] *Id.* at 833.
[123] *Id.*
[124] *Id.* at 832.
[125] 440 U.S. 48 (1979).
[126] *Id.* at 55 (emphasis added).

The Court went on to note that the justifications for applying state law were not limited to ownership interests.[127] Rather, the Court expanded the application to *security interests* as well.[128] The Seventh Circuit interpreted this language to mean that unless there is a provision in the Bankruptcy Code that says otherwise, state law governs the parties' rights under a contract.[129] Prior to the enactment of the BAPCPA, there was a provision in the Code—§ 506— that provided otherwise.[130] There is no dispute. There also is no disagreement that this provision still exists with respect to *non*-910 creditors. However, as the majority courts so steadfastly maintain, the BAPCPA expressly prohibits the application of § 506 to the claims of 910 creditors. Consequently, as the majority courts argue, there is no applicable bankruptcy provision that applies with respect to the bifurcation of a *910 creditor's claim*.[131] Applying the Supreme Court's holding in *Butner*, state law applies.[132] As the Seventh Circuit held, in the case where parties have contracted for particular rights, they are entitled to those rights.[133]

The Seventh Circuit's approach is also consistent with Article 9 of the U.C.C. The purpose of Article 9 of the U.C.C. is "to provide a simple and unified structure within which the immense variety of present-day secured financing transactions can go forward with less cost and with greater certainty."[134] It provides parties with recourse so that they will freely contract with others, which is crucial in our market-driven economy. The Seventh Circuit recognized the importance of the parties' contract; namely, that the debtors explicitly agreed to be responsible for any deficiency.[135] And the courts' holding resulted in the parties' actual contract having meaning—legal

[127] *Id.*
[128] *Id.*
[129] *In re Wright*, 492 F.3d at 832.
[130] *In re* Ezell, 338 B.R. 330, 338 (Bankr. E.D. Tenn. 2006).
[131] *In re* Duke, 345 B.R. 806, 809 (Bankr. W.D. Ky. 2006).
[132] 440 U.S. 48 at 48 (1979).
[133] *In re Wright*, 492 F.3d at 832.
[134] UCC 9-101 cmt.
[135] *In re Wright*, 492 F.3d at 832.

meaning—rather than simply being a means by which the debtors were able to get what they wanted, to the detriment of the creditor.[136] To adopt the majority's view would obviate the need to contract because parties would not be held to them. This would further have the adverse effect of striking a serious blow to the effectiveness of Article 9 and precluding parties from relying on the security interests.

B. The Reason for the BAPCPA

One of the factors that led to the enactment of the BAPCPA was abuse of the bankruptcy system.[137] As discussed earlier, the enactment of the BAPCPA resulted in a provision applicable only to those debtors acquiring a vehicle shortly before filing bankruptcy. By singling out these debtors, Congress was seemingly concerned about their potential for abuse. It hardly seems rational that Congress would enact a provision targeting a potentially abusive debtor which afforded the debtor more opportunity to abuse the system *after* the enactment of the statute than the debtor had *prior* to. The Seventh Circuit's interpretation is in harmony with this reasoning. Adoption of the majority courts' reasoning would have an outcome that Congress surely could not have intended.

Further, while the BAPCPA's legislative history is dearth, the title of the section that enacted the BAPCPA clearly indicates that it was enacted to protect secured creditors.[138] While one majority court was not convinced that its holding was "adverse to the position of a secured creditor,"[139] under the reasoning of the majority courts, secured creditors will be denied that to which they are entitled—that to which they lawfully contracted for. If the amount of litigation brought by secured creditors with respect to this issue is not conclusive proof of the secured creditors' belief that the majority courts' holdings are "adverse" to their interests, surely it at least must be extremely

[136] *Id.*

[137] *See* source cited *supra* note 36 and accompanying text.

[138] *In re* Zehrung, 351 B.R. 675, 678 (Bankr. W.D. Wis. 2006); *In re Wright*, 492 F.3d at 832.

[139] *In re Quick*, 360 B.R. 722, 728 (Bankr. N.D. Okla. 2007).

persuasive. In *In re Wright*, the Seventh Circuit did protect the secured creditor, consistent with the purpose of the BAPCPA, by affording them an unsecured deficiency claim.[140]

CONCLUSION

While the language of the BAPCPA is clear, the interpretation given to it by the majority courts is not only contrary to its plain meaning but also to Congress's motivations behind enacting the legislation. A major factor underlying the need for the statute was to protect secured creditors. However, under the majority court's interpretation, secured creditors are in a worse position *following* the enactment of the statute than they were *before* the legislation. It is hardly affording the secured creditor *greater* protection when you take away its entitlement to an unsecured claim—a right that it had previously enjoyed. Further, these contracted rights represent the very foundation upon which Article 9 of the U.C.C. is built. Depriving secured creditors of them while entitling *unsecured* creditors to these rights renders Article 9 a nullity and fails to pass "logical muster."[141] In *In re Wright*, the Seventh Circuit adopted the correct interpretation. And by holding the 910 debtors to their original contractual obligations, the court's holding is consistent with the plain meaning of the statute, Congress's purpose for enacting the statute, and Article 9.

Though the debate continues with little possibility of subsiding soon, it is clear that in courts adopting the majority view, 910 debtors will continue to have the opportunity to abuse the bankruptcy system to the detriment of 910 creditors—exactly what the BAPCPA was intended to prevent. As such, it is imperative that the majority courts adopt the view to which the Seventh Circuit subscribes. It is then that secured creditors will be given the protection that they expect, the protection that Congress desired them to have, and the protection that they have *contracted* for.

[140] 492 F.3d at 832.
[141] *In re* Quick, 360 B.R. 722, 728 (Bankr. N.D. Okla. 2007).