United States Bankruptcy Court
Western District of Wisconsin

Cite as: [Unpublished]

In re Jerry K. Erickson, Debtor
Bankruptcy Case No. 92-31013-12

United States Bankruptcy Court
W.D. Wisconsin

June 17, 1992

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William A. Chatterton, Ross & Chatterton, Madison, WI, Trustee.

Robert D. Martin, United States Bankruptcy Judge.

MEMORANDUM DECISION

On May 9, 1991 the United States of America (FmHA) obtained a judgment for foreclosure and sale of the debtor' residence and dairy farm in Iowa County, Wisconsin. The Judgment granted the defendants, Jerry K. Erickson, Patricia C. Erickson, Hinckley State Bank, and the First National Bank of Blanchardville, sixty days to redeem the property for $606,795.25. No one redeemed the property during the sixty days. The judgment "forever barred and foreclosed [defendants] of all right, title, interest and equity of redemption in said mortgaged premises, except the right to redeem the same before sale as provided herein."

On March 23, 1992 the debtor, Jerry K. Erickson, filed this chapter 12 bankruptcy case. The foreclosure sale of the Iowa County property, which was scheduled for March 24, 1992, did not take place.

On April 15, 1992, the United States filed a motion for relief from the automatic stay, alleging that the debtor has no equity in the property. The debtor acknowledges that the property is worth somewhere between $200,000.00 and $220,000.00. A preliminary hearing was held on May 11, 1992. The motion for relief from stay was denied.(1) However, the parties were invited to brief the merit of the United States' argument, expressed during the hearing, that the debtor is unable to deal with the property in his chapter 12 case because the sixty day redemption period specified in the district court judgment has expired.

The United States contends that "the debtor is unable to propose a confirmable Chapter 12 plan incorporating the subject real estate because he is not able to redeem said property at this time. Therefore, the United States is entitled to relief from stay." The United States failed to state whether it believes itself entitled to relief from the stay under 11 USC § 362(d)(1) or (d)(2), or to employ the language of either subsection in its argument.(2)

The United States contends that because the debtor failed to redeem the property as

provided in the United States District Court's judgment, he is "forever barred and foreclosed of all right, title, interest and equity of redemption." In support of its position, the United States relies on U.S.A. v Molitor, et al., 91-C-308-C (WD Wis, April 13, 1992).

In Molitor, a judgment of foreclosure was entered against the Molitors. Although the terms of the judgment gave the Molitors sixty days within which to redeem the property, the Molitors failed to do so, and the property was sold at public sale. Prior to the hearing on confirmation of the sale, the Molitors filed for protection under the Bankruptcy Code. At the hearing, the district court directed the parties to brief the effect of the bankruptcy proceeding on the government's motion to seek confirmation of the sale. The motion was referred to the magistrate, who recommended denial of the motion pending bankruptcy court determination that the government was entitled to relief from the automatic stay. The district court thereafter adopted the magistrate's conclusions of law and recommendation as the court's own, and denied the government's motion for confirmation of sale.(3)

In Molitor, the district court states that "[d]efendants have no right of redemption in this case," and implies (without engaging in any analysis of bankruptcy law), that for this reason the government's entitlement to relief from the stay in the bankruptcy case is a given. The United States now seizes upon Molitor as standing for the proposition that a district court judgment establishing a period of redemption renders inapplicable the right to "cure" a mortgage default in bankruptcy. See 11 USC §§ 1222(b)(2), (3), and (5). However, the district court's comments, whatever their import, are dicta, and the Molitor case must be limited to its holding that when foreclosure judgment defendants have filed for bankruptcy prior to confirmation of the foreclosure sale, the party seeking to confirm the sale must obtain relief from the automatic stay before the order of confirmation of sale may be entered.(4)

The Seventh Circuit Court of Appeals has issued two decisions which have direct bearing on the issues in the present case. In Matter of Clark, 738 F2d 869 (7th Cir 1984), the Court considered the issue of whether a debtor who has filed a petition under chapter 13 of the Bankruptcy Code, subsequent to a state court judgment of foreclosure, but prior to sale of the property, is entitled under 11 USC § 1322 to "cure" a default on a residential mortgage loan. The Court stated:

> Despite the judgment of foreclosure, the Clarks still had an interest in the property at the time they filed their petition in bankruptcy, such that the property was part of the estate under 11 U.S.C. §§ 541 and 1307. Under Wisconsin law, a mortgagee has only a lien on the mortgaged property even after a judgment of foreclosure is entered. Neither equitable nor legal title passes until the foreclosure sale is held. A judgment of foreclosure "does little more than determine that the mortgagor is in default, the amount of principal and interest unpaid, the amounts due to plaintiff mortgagee for taxes, etc. . . . The judgment does not destroy the lien of the mortgage but rather judicially determines the amount thereof."

Clark, 738 F2d at 871, citing Marshall and Ilsley Bank v Greene, 227 Wis 155, 164, 278 NW 425, 429 (1938); Bank of Commerce v Waukesha County, 89 Wis 2d 715, 723, 279 NW2d 237, 241 (1979); In re Lynch, 12 BR 533, 534-35 (Bankr WD Wis 1981).

After analyzing Section 1322(b), the Court stated:

> [W]e conclude that the power to "cure" a default provided by § 1322(b)(5) permits a debtor to de-accelerate the payments under a note secured by a residential property mortgage. . . . As we have noted, in Wisconsin a judgment of foreclosure does nothing but judicially confirm the acceleration. Though we do not reach the question whether

the same result obtains in a state in which the effect of a judgment of foreclosure is different, in Wisconsin such a judgment adds nothing of consequence as far as § 1322(b) is concerned.

Clark, 738 F2d at 874. The language of chapter 12 is taken from chapter 13, and Section 1222(b) tracks the language relied upon in Clark.(5)

In Matter of Madison Hotel Associates, 749 F2d 410 (7th Cir 1984), the Seventh Circuit revisited Wisconsin foreclosure law as it relates to bankruptcy. In Madison Hotel Associates, the mortgagee obtained an order of foreclosure from the federal district court, and was directed to submit a form of judgment for the judge's signature. Before the judgment was submitted, the mortgagor filed a petition under chapter 11 of the Bankruptcy Code, thereby precluding the mortgagee from obtaining a final judgment of foreclosure. The district court subsequently overruled the bankruptcy court's holding that the mortgagee was not "impaired" under the plan, as that term is defined in 11 USC § 1124(2).(6)

The Circuit Court considered the issue of "what effect the district court's order of foreclosure, entered pursuant to Wisconsin state law, has upon MHA's attempt to cure the default of its accelerated loan and thereby render Prudential's claim 'not impaired' under 11 U.S.C. § 1124(2)." Madison Hotel Associates, 749 F2d at 419. After analyzing the law relating to Section 1124(2), the Court concluded that:

a creditor, holding a final judgment of foreclosure, is not impaired under section 1124(2) if the debtor's plan of reorganization cures the default of the accelerated loan before the foreclosure sale actually occurs or before the judgment merges into the mortgage under state law, thereby transferring title to the mortgagee.

Madison Hotel Associates, 749 F2d at 422. The Court analyzed Wisconsin case law, including the Clark decision, to determine whether under it a foreclosure judgment merges into the mortgage. In so doing, it distinguished out-of-state case law. The Court concluded that:

Prudential's failure to obtain a judgment of foreclosure on its accelerated loan is of no consequence in this case. Under Wisconsin law, the judgment would simply represent a judicial determination of the amount due under the accelerated loan and Prudential would continue to hold only a lien upon MHA's property.

Madison Hotel Associates, 749 F2d at 422-23.

The Court determined that the "contention that the default is not cured under MHA's plan because Prudential has an order of foreclosure that will not be reduced to final judgment, directly contravenes the purpose of 11 U.S.C. § 1124(2) to allow a Chapter 11 debtor to reverse a contractual or legal acceleration." Madison Hotel Associates, 749 F2d at 424. The Court held that "in light of the fact that Prudential holds only a lien upon MHA's property, and that MHA's plan of reorganization satisfies the four-prong test of 11 U.S.C. § 1124(2)," Prudential's claim was "not impaired." Id., 749 F2d at 424. For this reason, Prudential was deemed to have accepted the plan for purposes of 11 USC § 1129(a)(8). Id.

The Seventh Circuit's holdings in Clark and Madison Hotel Associates eliminate any doubt concerning the conclusion which must be reached in this case. In Clark, the Court held that in a chapter 13 case in which a mortgagee had obtained a judgment of foreclosure on the debtor's farm, but the property had not been sold prior to filing of the petition, "'the power to "cure" a default provided by [11 U.S.C.] § 1322(b)(5) permits a debtor to de-accelerate the payments under a note secured by a residential property

mortgage.'" Madison Hotel Associates, 749 F2d at 422, citing Clark, 738 F2d at 874. Similarly, in Madison Hotel Associates, the Court determined that, where no foreclosure sale had yet taken place, the district court's order of foreclosure, entered pursuant to Wisconsin state law prior to the filing of the debtor's chapter 11 petition, had no effect upon the debtor's plan proposal to cure the default of the accelerated loan and thereby render the mortgagee's claim "not impaired" for purposes of Section 1124(2).

In the present case, the debtor filed a petition under chapter 12 of the Bankruptcy Code, after the district court judgment of foreclosure and sale, but prior the sale of the property. The judgment of foreclosure "'does not destroy the lien of the mortgage but rather judicially determines the amount thereof.'" Clark, 738 F2d at 871 (citations omitted). The Clark court held that in Wisconsin, a foreclosure judgment "adds nothing of consequence as far as § 1322(b) is concerned." Clark, 738 F2d at 874. Nor does a foreclosure judgment add anything of consequence as far as Section 1222(b), modeled as it is after Section 1322(b), is concerned. Furthermore, Madison Hotel Associates answers the question of whether, under Wisconsin law, a district court order of foreclosure precludes a debtor's right under the Bankruptcy Code to reverse a contractual or legal acceleration. Madison Hotel Associates makes clear that in Wisconsin, the debtor retains that right until the foreclosure sale is held, notwithstanding the district court's order. As the foreclosure sale has not been held in the case at bar, the debtor retains the right to "cure" the default under Section 1222(b).[(7)]

The United States' contention that the debtor is unable to propose a confirmable chapter 12 plan incorporating the Iowa County real estate cannot be sustained as a matter of law. Because the debtor does not lack the legal capacity to propose a confirmable chapter 12 plan, and there is no factual predicate advanced for any other type of inability to propose a confirmable plan, the United States' motion for relief from the stay was correctly denied. We do not have to guess as to which subsection of Section 362(d) the United States believed itself to be pursuing. Neither would be supported without its prevailing on the issue herein decided.

The United States additionally contends that "if the debtor is allowed by this Court to redeem the subject real estate, the debtor may only do so for the full amount of the foreclosure judgement plus interest, costs and taxes." This issue is not appropriate for decision in the context of a motion for relief from the stay, but should be considered in connection with confirmation of the debtor's proposed plan.

END NOTES:

1. 11 USC § 362(e) requires a prompt decision on requests for relief from the stay by providing that relief will be granted if not promptly denied. In this case, where there was no apparent chance of success, the relief was denied as a preliminary matter.

2. 11 USC §§ 362(d)(1) and (2) provide:

On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay--

(1) for cause, including the lack of adequate protection of an interest in property of such party in interest; or

(2) with respect to a stay of an act against property under subsection (a) of this section, if-

(A) the debtor does not have an equity in such property; and

(B) such property is not necessary to an effective organization.

3. At the subsequent bankruptcy court hearing, the court ordered the debtor to pay adequate protection payments and denied the government's motion for relief from the stay. The government's appeal of this order is currently pending in the district court.

4. The United States' additional reliance upon 11 USC § 108(b) and Matter of Tynan, 773 F2d 177 (7th Cir 1985), is misplaced. See Tynan, 773 F2d at 178 n 2 ("In the Matter of Clark, 738 F.2d 869 (7th Cir. 1984) is inapposite because it arose under Wisconsin [rather than Illinois] law, the mortgage lender opposed the Chapter 13 plan, and no foreclosure sale had occurred before the Chapter 13 petition was filed.").

5. "This new chapter [chapter 12] is closely modeled after existing Chapter 13." Conference Report 99-958, pp 49, 50; also appearing in 132 Cong Rec H 8998, H 8999 (Oct 2, 1986)). Section 1322(b)(5) is essentially identical to Section 1222(b)(5). Section 1322(b)(5) provides that:

Subject to subsections (a) and (c) of this section, the plan may--

notwithstanding paragraph (2) of this subsection, provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due[.]

Section 122(b)(5) provides that:

Subject to subsections (a) and (c) of this section, the plan may--

provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due[.]

6. The Circuit Court explained the district court's basis for reversal of the bankruptcy court's order:

The district court disagreed with the bankruptcy court's analysis of section 1124(2). According to the district court, "MHA's plan impairs Prudential's [the mortgagee's] claim because it does not restore Prudential's judicially-recognized right to proceed with foreclosure of the real and personal property of the Concourse Hotel." . . . [T]he district court reasoned that "[a] judicially-recognized right to foreclosure is something different from a right to accelerated payments that arises by operation of a contractual provision or of applicable law." Thus, the district court concluded that "because Prudential's right to foreclosure does not arise merely from a contractual provision or applicable law but is created by court order and is not simply a right to accelerated payments which can be cured, Prudential's claim does not fall within the exception created by § 1124(2)."

Madison Hotel Associates, 749 F2d at 419 (citations omitted).

7. Although Clark and Madison Hotel Associates speak only in terms of a debtor's power under the Bankruptcy Code to cure a default under circumstances in which a foreclosure sale has not yet occurred, it should be noted that under Wisconsin law, it is confirmation of the sale, and not the foreclosure sale itself, which extinguishes a mortgagor's equity of redemption and passes title to the property. In Gerhardt v Ellis et al., 134 Wis 191, 114 NW 495 (1908), the Wisconsin Supreme Court stated:

[A] foreclosure is not completed until the sale on foreclosure is confirmed. . . . There can be no doubt but that the right to redeem persists at least until confirmation of sale, unless that right is cut off by statute. . . . It is clear that the title does not pass until confirmation so as to vest the purchaser with the right of possession. And it is equally clear that the right of redemption is not barred until confirmation of the sale.

Gerhardt, 134 Wis at 195-96 (citations omitted). See also Bank of Commerce v Waukesha County, 89 Wis 2d 715, 723, 279 NW2d 237 (1979) ("[W]e hold pursuant to the case law and statutory authority reviewed [see Wis Stat § 846.17], the Bank did not acquire title in the property until June 3, 1974, the date of the judicial confirmation of the sheriff's sale. Prior to the confirmation of the sale, the Bank's interests in the property was [sic] limited to that of a lien holder[.]"); Shuput v Lauer, 109 Wis 2d 164, 174, 325 NW2d 321 (1982) ("[T]he sheriff's sale is not final until the sale is confirmed. In other words, title to the property does not pass prior to confirmation of the sale."); In re Lynch, 12 BR 533, 535 (Bankr WD Wis 1981) ("[U]nder Wisconsin law mortgagors retain an equitable interest, i.e., the right to redeem, until a foreclosure sale is confirmed pursuant to Wis.Stats. § 846.165.").