Forthcoming in *The Yale Law Journal*

THE DEBTOR'S DILEMMA: ECONOMIC ANALYSIS OF ASSET RETENTION IN CONSUMER BANKRUPTCY

Amber J. Moren

Since 2005, the Bankruptcy Code has limited Chapter 7 debtors to two asset retention options, reaffirmation and redemption. This Note explores the impact of the modified asset retention options both on the incentives of debtors and creditors during bankruptcy proceedings and on the deals they reach in practice.

While the 2005 revisions succeeded in eliminating an irksome circuit split, this Note illustrates the way in which they fostered deeper problems with asset retention. It argues that allowing ride-through – the option laid to rest in 2005 – would better achieve the bankruptcy goals of protecting debtors and creditors while promoting doctrinal uniformity.

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INTRODUCTION

On August 11, 2011, Carolyn Denise Bowden filed a Chapter 7 bankruptcy petition in North Carolina.[1] Prior to filing, Bowden had been making regular payments on a 2006 Chevrolet Trailblazer.[2] When she filed her bankruptcy petition, Bowden owed $4,534.31 on the Trailblazer to her creditor, Ally Financial.[3] By filing Chapter 7 bankruptcy, Bowden successfully discharged unsecured obligations, including credit card debt. But Ally Financial still had a set of ownership rights with respect to the Trailblazer, which secured Bowden's outstanding $4,534.31 loan. For Bowden and Ally Financial, the treatment of the outstanding $4,534.31 debt on the Trailblazer presented a key procedural inquiry in the bankruptcy process, determining who would retain the vehicle and how retention costs would be allocated.

Bowden's vehicle retention dilemma is a recurrent procedural step for which consumer bankruptcy law should have a ready reply. But the treatment of secured debt in Chapter 7 bankruptcy is both uncertain and opaque. Three options have been uniformly available to Chapter 7 debtors for decades. Under section 521(a)(6) of the Bankruptcy Code ("the Code"), Bowden could surrender the Trailblazer to Ally Financial to satisfy her outstanding debt. Alternatively, Bowden could redeem the Trailblazer by paying Ally Financial the full value of the Trailblazer within thirty days following the petition. Finally, Bowden could reaffirm the debt, agreeing to a new post-bankruptcy repayment schedule and renewing personal liability for the vehicle. All of these options, unfortunately, present significant drawbacks for Chapter 7 debtors.

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1 *In re* Bowden, No. 11-06168-8-SWH, 2012 WL 589657, at *1 (Bankr. E.D.N.C. Feb. 22, 2012).
2 *Id.*
3 *Id.*

Beyond the three statutory options lies a potential fourth, which is the primary focus of this Note. In addition to surrender, redemption, and reaffirmation, a debtor may in certain circumstances retain the asset simply by continuing to make regular payments according to the pre-bankruptcy loan schedule, or ride-through the asset. This Note distinguishes between three types of ride-through. Beginning in the 1990s, courts divided on whether a Chapter 7 debtor could retain an asset by *common-law ride-through*, based on judicial interpretation of the relevant Code provisions. By the time Congress reacted in 2005, common-law ride-through was expressly accepted in five circuits and rejected in five others.[4]

In 2005, acting under a congressional mandate to create uniform bankruptcy laws,[5] Congress passed the Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA").[6] Courts initially struggled to interpret the amendments, but eventually reached a consensus that BAPCPA eliminated common-law ride-through. Yet it soon became clear that ride-through was not entirely defunct. Increasingly, courts construed the BAPCPA amendments to continue the automatic stay, and so prevent a creditor from repossessing, as long as the debtor attempted to either redeem, reaffirm, or surrender. In this way, if a reaffirmation agreement were rejected, a debtor could nonetheless retain the asset, achieving a second form of *backdoor ride-through*.

This Note shows how BAPCPA, while resolving the circuit split on common-law ride-through, aggravated other problems with Chapter 7 asset retention; and argues that replacing reaffirmation with *statutory ride-through* would cure the doctrinal defects. Part I first explores

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[4] The Second, Third, Fourth, Ninth, and Tenth Circuits allowed debtors to elect ride-through. *See infra* notes 23-25, 30. The First, Fifth, Sixth, Seventh, and Eleventh Circuits did not. *See infra* notes 27-29, 32.

[5] U.S. CONST. art. I, § 8, cl. 4 (empowering Congress to establish "uniform Laws on the subject of Bankruptcies throughout the United States").

[6] Pub. L. No. 109-8, 119 Stat. 23 (2005) (codified as amended in scattered sections of 11 U.S.C.).

the history and effect of the BAPCPA amendments by comparing the treatment of motor vehicle debt for Delaware debtors filing before and after 2005. Part II uses a simple game-theory framework to show why so many debtors and creditors avoid all three post-BAPCPA statutory options, instead reaching agreements entirely outside the scope of section 521(a)(6). In addition to backdoor ride-through, creditors and debtors enter informal forbearance agreements or Chapter 7 debtors may convert to Chapter 13.

To this descriptive analysis, Part III adds a normative overlay, arguing that the current system fails to protect both debtors and creditors while fostering uncertainty in the application of law. Many pre-BAPCPA commentators noted that reaffirmation agreements violate the fresh start policy of Chapter 7. Following BAPCPA, backdoor ride-through exposes secured creditors to unanticipated risk. Part IV, finally, argues that statutory ride-through, supplemented by a reinstate-and-cure provision, would create uniformity in consumer bankruptcy law while better serving the interests of debtors and their secured creditors. From a practical perspective, the emerging acceptance of backdoor ride-through could encourage pro-creditor Congress to formally adopt its statutory sibling.

On an aggregate scale, the significance of the procedural uncertainty facing debtors and secured creditors like Bowden and Ally Financial is enormous. In 2010, 1,129,955 individuals filed Chapter 7 bankruptcy petitions, bringing $273 billion of debt into bankruptcy proceedings.[7]

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[7] U.S. BANKRUPTCY COURTS, ASSETS AND LIABILITIES REPORTED BY INDIVIDUAL DEBTORS IN CHAPTER 7 CASES WITH PREDOMINANTLY NONBUSINESS DEBTS, http://www.uscourts.gov/Statistics/BankruptcyStatistics.aspx (follow "Calendar Year 2010" hyperlink under "Bankruptcy Abuse Prevention and Consumer Protection Act Statistics"; then follow "Table 1A" hyperlink) [hereinafter "CHAPTER 7 DEBTOR STATISTICS 2010"].

Collective assets of $235 billion offset the $273 billion debt. *Id.* The total assets include a debtor who reported nearly $100 billion in assets. When the outlier is removed from the sample, the total assets shrink to $136 billion, less than the total amount of secured debt. ADMIN. OFF. OF THE U.S. CTS., STAT. DIVISION, 2010 REPORT OF STATISTICS REQUIRED BY THE BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT OF 2005 10, Of the total debt, more than half – $148 billion – was secured, requiring treatment under section 521(a)(6).[8] This Note shows how, as asset retention options have splintered and Chapter 7 petitions continue to expand,[9] the need for reform of this Code section is more pressing than ever. Adopting statutory ride-through would alleviate many of the current problems with the Code's treatment of secured debt in consumer bankruptcy.

I. A TALE OF TWO DEBTORS

For Michael and Christine Price and Kimberly Miller, "it was the worst of times."[10] Like Carolyn Bowden, both debtors – Michael and Christine Price filing jointly[11] and Kimberly Miller individually – sought to cure their insolvency by filing Chapter 7 bankruptcy petitions. Both debtors filed in Delaware. Both hoped to retain their motor vehicles, encumbered by creditor liens, after emerging from bankruptcy. But the Prices filed their petition in 2001, and Miller filed hers in 2010. During the intervening decade, BAPCPA had taken effect.

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available at http://www.uscourts.gov/Statistics/BankruptcyStatistics.aspx (follow "Calendar Year 2010" hyperlink under "Bankruptcy Abuse Prevention and Consumer Protection Act Statistics"; then follow "Full Report" hyperlink) [hereinafter BANKRUPTCY REPORT 2010].

8 CHAPTER 7 DEBTOR STATISTICS 2010, *supra* note 7. To put the figure in perspective, the $148 billion of secured debt equaled over one-half the value of all new car sales and one percent of national gross domestic product during the same year. BUR. OF TRANSPORTATION STAT., TABLE 1-17 NEW & USED PASSENGER CAR SALES & LEASES, *available at* http://www.bts.gov/publications/national_transportation_statistics/html/table_01_17.html (listing total new vehicle sales in 2010 as $311 billion); U.S. DEP'T. OF COMM., BUR. ECON. ANAL., TABLE 1.1.5 GROSS DOMESTIC PRODUCT, *available at* http://bea.gov/iTable/iTable.cfm?ReqID=9&step=1 (follow "Table 1.1.5. Gross Domestic Product (A) (Q)" hyperlink under "Section 1 – Domestic Product and Income") (listing U.S. GDP as $14.8 trillion over the year ended December 2010).

9 In the year ended September 2011, the number of Chapter 7 petitions increased to 1,467,221. U.S. BANKRUPTCY COURTS, BUSINESS AND NONBUSINESS CASES COMMENCED, BY CHAPTER OF THE BANKRUPTCY CODE, DURING THE 12-MONTH PERIOD ENDING SEPTEMBER 30, 2011, http://www.uscourts.gov/Statistics/BankruptcyStatistics.aspx (follow "12-month period ending September" under "Filings"; then follow "2011 September xls" hyperlink).

10 CHARLES DICKENS, A TALE OF TWO CITIES 1 (A.C. McClurg & Co., 1888) (1859).

11 Because the couple filed jointly, they are treated as an individual debtor under the Bankruptcy Code. *See* 11 U.S.C. § 302. The Code provisions that refer to "Debtor" refer to both Michael and Christine Price.

Based on the BAPCPA amendments to the Bankruptcy Code, the *Price* and *Miller* courts reached opposite conclusions on whether a debtor could elect to ride-through an asset in bankruptcy. This section illustrates the way in which BAPCPA modified debtors' post-bankruptcy collateral retention options and the textual basis for the Delaware court's reversal on the issue of common-law ride-through. It then situates Delaware in a national context, describing how the pre-BAPCPA circuit split gave way to a universal extinction of common-law ride-through following BAPCPA.

A. *In re Price*: Ride-Through before BAPCPA

On December 11, 2001, Michael and Christine Price filed a joint Chapter 7 bankruptcy petition.[12] The Chapter 7 fresh start policy[13] allowed the Prices discharged their unsecured debts in exchange for forfeiting non-exempt assets.[14] For debt secured by personal property, however, Code section 521(2) required that the Prices

> (A) within thirty days after the date of the filing of a petition under chapter 7 . . . file with the clerk a statement of his intention with respect to the retention or surrender of such property and, *if applicable*, specifying that such property is claimed as exempt, that the debtor intends to redeem such property, or that the debtor intends to reaffirm debts secured by such property; and
> (B) within 30 days after the first date set for the meeting of creditors . . . perform his intention . . .;

[12] *In re* Price, 281 B.R. 240, 240 (Bankr. D. Del. 2002), *subsequently rev'd*, 370 F.3d 362 (3d Cir. 2004). The factual summary is based on the Bankruptcy Court opinion, while the legal analysis comes from the Third Circuit reversal.

[13] For further discussion of the fresh start and its policy rationale, *see infra* note 119 and accompanying text.

[14] A Chapter 7 debtor may take advantage of both state and federal exemptions to retain assets post-discharge. The federal exemptions, set in 2010 and subject to periodic adjustments, allow debtors to retain $21,625 in real property, $3,450 in one motor vehicle, and $1,450 in jewelry. 11 U.S.C. § 522(d) (adjustments under 11 U.S.C. § 104). For a list of personal and homestead exemptions under state law in 2000, *see* Lars Lefgren & Frank McIntyre *Explaining the Puzzle of Cross-State Differences in Bankruptcy Rates*, 52 J.L. & ECON. 367, 376-77 (2009).

> except that nothing in subparagraphs (A) and (B) of this paragraph shall alter the debtor's or the trustee's rights with regard to such property under this title.[15]

Earlier in 2001, the Prices had secured a loan for $21,985.29 from the Delaware State Police Federal Credit Union with their Toyota Corolla and Sienna.[16] Because the debt was secured by personal property, section 521(2)(A) required the Prices to file a statement of intention indicating whether they would redeem, surrender, or reaffirm the debt in bankruptcy. Section 521(2)(B) required them to promptly follow through with their intended action.

For the Prices, the three options looked dismal. They could not afford to redeem their vehicles under section 722, which required them to pay the Credit Union a lump sum equal to the liquidation value of the Corolla and Sienna.[17] The Prices could alternatively satisfy their debt by surrendering the vehicles to the Credit Union, but would then emerge from bankruptcy without a vehicle.[18] The third and final option was to reaffirm the debt under section 524. To reaffirm, the Prices had to enter a formal agreement with the Credit Union, promising to repay the outstanding loan according to a revised post-bankruptcy schedule.[19] If they reaffirmed, the Prices could retain

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15 11 U.S.C.A. § 521(2)(A) (2000) (emphasis added).

16 *In re* Price, 281 B.R. at 240.

17 11 U.S.C. § 722 (2000). In 1997, the U.S. Supreme Court in *Assocs. Commercial Corp. v. Rash* ruled that the appropriate valuation standard for a Chapter 13 cramdown was "replacement value" of the asset. 520 U.S. 953, 956. Although some courts applied the replacement value standard for Chapter 7 debtors as well, the Delaware Bankruptcy Court never adopted the standard. Other Third Circuit bankruptcy courts continued to use liquidation value in Chapter 7 cases. *In re* Basher, 291 B.R. 357, 364 n.6 (Bankr. E.D. Pa. 2003) (noting that "a Chapter 7 case . . . would not implicate application of the *Rash* replacement value test in a cramdown context"). When the Prices filed, liquidation value was required to redeem.

For further discussion of the infeasibility of redemption, *see infra* Part II(B)(ii).

18 The majority of debtors are reluctant to surrender their vehicles. *See* Marianne B. Culhane & Michaela M. White, *Debt After Discharge: An Empirical Study of Reaffirmation*, 73 AM. BANKR. L.J. 709, 739 (1999) [hereinafter Culhane & White, *Debt After Discharge*] (finding that in 1995, seventy-nine percent of Chapter 7 car-owners intended to retain their encumbered vehicles following bankruptcy). For further discussion of the disutility of surrender, *see infra* Part II(B)(i).

19 11 U.S.C. § 524 (2000).

the vehicles, but if they failed to make a scheduled payment, the Credit Union could repossess.[20] In that case, if the Credit Union sold the vehicles for less than the debt they secured, the Prices would be personally liable for the deficiency. Because motor vehicles are typically worth less than the debt they secure,[21] if the Prices defaulted after reaffirming, they would likely find themselves without a car and nonetheless mired in debt.

The options available under section 521(2)(A) left the Prices between a rock and a hard place. So when they filed their statement of intention, the Prices neglected to select redemption, surrender, or reaffirmation. Instead, the Prices indicated that they would simply "retain [the] collateral and continue to make regular payments,"[22] or ride-through the vehicles in bankruptcy. The Prices rested this election in bedrock of judicial authority from other circuits. The Second, Fourth, Ninth, and Tenth Circuits had construed section 521(2)(A) to allow a debtor who is current on loan payments to retain an asset without redeeming or reaffirming.[23] The Fourth and Ninth Circuits reasoned that the plain language of section 521(2)(A) permitted ride-through, because the phrase "if applicable" indicated that a debtor was not limited to the options given by statute.[24] The Second and Tenth Circuits focused on the function of the statute and its

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[20] Outside of bankruptcy, secured creditors have the right to repossess collateral following an event of default. *See* U.C.C. § 9-609(a)(1) (2000); *infra* note 138.

[21] In 1995, an auto industry executive stated that new car lenders creditors were undersecured by an average of $4,000 at the time the debtor filed bankruptcy. *See* Culhane & White, *Debt After Discharge, supra* note 18, at 741-42 (citing confidential conversation between Elizabeth Warren and industry executive).

[22] *In re* Price, 281 B.R. at 240-41.

[23] *In re* Price, 281 B.R. at 242 (citing McClellan Fed. Credit Union v. Parker (*In re* Parker), 139 F.3d 668, 673 (9th Cir. 1998); Home Owners Funding Corp. of Am. v. Belanger (*In re* Belanger), 962 F.2d 345, 348 (4th Cir. 1992); Capital Commc'ns Fed. Credit Union v. Boodrow (*In re* Boodrow), 126 F.3d 43, 51 (2d Cir. 1997); Lowry Fed. Credit Union v. West, 882 F.2d 1543, 1547 (10th Cir. 1989)).

[24] *In re* Parker, 139 F.3d at 673 ("[T]he only mandatory act is the filing of the statement of intention . . . Then, 'if applicable,' – that is, if the debtor plans to choose any of the three options listed later in the statute . . ."); *In re* Belanger, 962 F.2d at 348 ("The phrase 'if applicable' is redundant if . . . the options given to the debtor are considered to be exclusive.").

enforcement mechanisms to reach the same conclusion.[25] In any of these four circuits, the Prices could have elected common-law ride-through.

The Credit Union protested. Against the weight of four permissive circuits, the Credit Union cited decisions by the First, Fifth, Seventh, and Eleventh Circuits that explicitly rejected common-law ride-through.[26] Citing the same statutory text, these four circuit interpreted the "if applicable" language to require a debtor to specify one of the three options if *retention* was applicable; in other words, if the debtor intended to retain the asset post-bankruptcy.[27] The four rejecting circuits also advanced competing policy arguments, worrying that that no debtor would reaffirm if ride-through were available,[28] and that ride-through would increase credit rates and expose creditors to undue risk.[29] Following this logic, the Credit Union argued that because the Prices hoped to retain the vehicles, they were limited to the three statutory options.

Facing a fifty-fifty circuit split, the Prices flipped a lucky coin. The Third Circuit joined the Second, Fourth, Ninth, and Tenth Circuits in permitting common-law ride-through, reversing

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[25] *In re* Boodrow, 126 F.3d at 51 (finding that "§ 521(2) appears to serve primarily a notice function, not necessarily to restrict the substantive options available to a debtor who wishes to retain collateral securing a debt"); Lowry Fed. Credit Union, 882 F.2d at 1547 ("[A]lthough we regard as mandatory the provisions of [§ 521], we do not believe those provisions make redemption or reaffirmation the exclusive means by which a bankruptcy court can allow a debtor to retain secured property.").

[26] *In re* Price, 281 B.R. at 244.

[27] Bank of Boston v. Burr *(In re* Burr), 160 F.3d 843, 847 (1st Cir.1998); Johnson v. Sun Fin. Co. (*In re* Johnson), 89 F.3d 249, 252 (5th Cir.1996); Taylor v. AGE Fed. Credit Union (*In re* Taylor), 3 F.3d 1512, 1516 (11th Cir.1993); *In re* Edwards, 901 F.2d 1383, 1387 (7th Cir.1990). *See also* Ned W. Waxman, *Redemption or Reaffirmation: The Debtor's Exclusive Means of Retaining Possession of Collateral in Chapter 7*, U. PITT. L. REV. 187, 196-97 (1994) ("Where, then, is the remedy of retention authorized in the Code? Nowhere!").

[28] *In re* Edwards, 901 F.2d at 1386 (noting that "[n]o debtor would reaffirm personal liability unless required to do so"); *In re* Taylor, 3 F.3d at 1516 (comparing ride-through to a "de facto reaffirmation agreement" in which a creditor has "no recourse against the debtor"). The Ninth Circuit put the point more strongly, "If ride-through existed, any lawyer who advised his client to make a reaffirmation offer on the original contract terms would be guilty of malpractice . . . [Why] incur the risk of personal liability when one could safely achieve the same ends by ride-through?" *In re* Dumont, 581 F.3d at 1114.

[29] *E.g.*, *In re* Taylor, 3 F.3d at 1516 ("Allowing a debtor to retain collateral without reaffirming or redeeming gives the debtor . . . a 'head start' since the debtor effectively converts his secured obligation from recourse to nonrecourse with no downside risk for failing to maintain or insure the lender's collateral.").

a bankruptcy court holding for the Credit Union.[30] After *In re Price*, debtors in the Third Circuit could retain encumbered collateral post-bankruptcy as long as they did not miss a scheduled payment. In effect, post-bankruptcy debts became nonrecourse, allowing a creditor to repossess but not to recover any repayment deficiency.[31]

Following *In re* Price, the Sixth Circuit rejected common-law ride-through,[32] while the Eighth Circuit never reached a decision on the issue.[33] The resulting five-five circuit split continued until the eve of BAPCPA. Not only did the circuit split create geographic inequities for debtors and creditors, but it also violated an explicit constitutional mandate directing Congress to establish "uniform Laws on the subject of Bankruptcies throughout the United States."[34] Based on problems associated with common-law ride-through, one professor called it the "most controversial consumer credit issue arising in cases under the United States Bankruptcy Code."[35]

B. The BAPCPA Amendments

In 2005, Congress recodified Bankruptcy Code section 521(2)(A) as section 521(a)(6), leaving intact its core provisions. Post-BAPCPA, debtors must file a statement of intention

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[30] The Third Circuit first found the text of section 521 ambiguous, and so contextualized it among related Bankruptcy Code provisions. Price v. Delaware State Police Fed. Credit Union (*In re* Price), 370 F.3d 362, 368 (3d Cir. 2004). Based on extensive "substantive rights" to collateral retention elsewhere in the Code, the court concluded that section 521(2) "is not intended to deprive the Prices of broad retention options," including ride-through. *Id.* at 372-74. The Price court also resisted the characterization of ride-through as a "fourth option," insisting instead that it was an ever-present choice for debtors and utterly consistent with bankruptcy policy. *Id*. at 372-73. Other courts, however, have termed it "the fourth option," an exploitation of a loophole rather than an affirmative statutory right. *E.g.*, *In re* Burr, 160 F.3d at 847.

[31] U.C.C. § 9-615 (2000); Culhane & White, *Debt After Discharge*, *supra* note 18, at 719 ("The effect [of reaffirmation] is to transform the claim into a nonrecourse debt. The debtor's personal liability has been discharged but the lien lives on as a strong incentive to voluntary payment.").

[32] *See* Gen. Motors Acceptance Corp. v. Bell (*In re* Bell), 700 F.2d 1053, 1054-55, 1058 (6th Cir. 1983).

[33] *See* Sanabria v. Am. Nat'l. Bank (*In re* Sanabria), 317 B.R. 59, 60-61 & nn.2-3 (8th Cir. 2004).

[34] U.S. CONST. art. I, § 8, cl. 4.

[35] Waxman, *supra* note 27, at 187.

declaring whether they will redeem collateral, reaffirm debt, or surrender the asset to the secured creditor.[36] The BAPCPA amendments did not change the terms of surrender, but raised the cost of redemption by requiring a debtor to pay "the price that a retail merchant would charge," rather than liquidation value, to redeem.[37]

The BAPCPA amendments also increased the cost of reaffirmation by imposing new procedural safeguards. Before BAPCPA, reaffirming debtors and creditors had to comply with a statutory checklist, but BAPCPA ramped up the requisite financial disclosures. Post-BAPCPA section 524(c) requires a creditor to make specific disclosures to a reaffirming debtor, and requires the debtor's lawyer to file an affidavit certifying that the debtor will not suffer undue hardship as a result of the reaffirmation agreement.[38] Section 524(a)(6) further requires a court to review the agreement if the lawyer refuses to sign the affidavit, if the debtor's income falls short of reaffirmation payments,[39] or if the debtor is pro se.[40] Courts will reject any reaffirmation agreement that "impos[es] an undue hardship on the debtor or a dependent of the debtor" or is

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[36] 11 U.S.C. § 521(a)(6) (2010).

[37] *See* 11 U.S.C. § 722 (2010) (allowing a Chapter 7 debtor to redeem "[b]y paying the holder of such lien the amount of the allowed secured claim of such holder that is secured by such lien in full at the time of redemption"); 11 U.S.C. § 506(a)(2) (2010) (stating that for Chapter 7 debtors, the value of the secured claim on personal property "shall be determined based on the replacement value," defined as "the price a retail merchant would charge for property of that kind considering the age and condition of the property at the time value is determined."). The BAPCPA amendments codified U.S. Supreme Court decision in *Rash*, which required replacement value in Chapter 13 cramdowns, as applicable to Chapter 7 debtors as well. *See supra* note 17. Prior to BAPCPA, courts were mixed on whether *Rash* applied to Chapter 7 debtors; many continued to require liquidation value to redeem. *Id.* Although in some circuits revised section 722 merely codified existing common law, the net effect of BAPCPA was to "call for a higher price for redemption than under case law prior to the [BAPCPA]." Jean Braucher, *Rash and Ride-Through Redux: The Terms for Holding on to Cars, Homes and Other Collateral Under the 2005 Act*, 13 AM. BANKR. INST. L. REV. 457, 468 (2005) [hereinafter Braucher, *Rash and Ride-Through Redux*].

[38] *See* 11 U.S.C. § 524(c) (2010). For a detailed discussion of the new procedural requirements for lawyers, debtors, and the court, *see also* David B. Wheeler & Douglas E. Wedge, *A Fully-Informed Decision: Reaffirmation, Disclosure, and the Bankruptcy Abuse and Consumer Protection Act of 2005*, AM. BANKR. L.J. 789 (2005).

[39] This is particularly important because "many among the debtors' bar staunchly refuse to endorse a client's reaffirmation efforts." Wheeler & Wedge, *supra* note 38, at 804.

[40] 11 U.S.C. §§ 524(d), 524(c)(6)(A) (2010). Courts also reviewed reaffirmation agreements filed by pro se debtors for undue hardship under the pre-BAPCPA Bankruptcy Code. *See* 11 U.S.C. § 524(c)(3) (2000).

not "in the best interest of the debtor."[41] The agreement is enforceable only after creditor, debtor, and judicial certification.

Unlike the explicit revisions with respect to redemption and reaffirmation, the BAPCPA amendments did not address common-law ride-through. In fact, commentators expressed confusion about whether they had any effect on ride-through at all. Shortly after the enactment of BAPCPA, an American Bankruptcy Institute online poll reported that thirty-two percent of respondents "agreed strongly" that BAPCPA eliminated common-law ride-through, but twenty-eight percent "strongly disagreed" with the same statement.[42] Courts were equally bewildered. A bankruptcy court compared deciphering the effect of BAPCPA on ride-through to solving "a Rubik's cube that had arrived with a manufacturer's defect,"[43] and the Ninth Circuit called it "hardly the model of a well-drafted statute."[44]

To the muddled text of the BAPCPA amendments, the skeletal legislative record added little clarity. In a 2005 article forecasting the effect of BAPCPA on collateral retention in Chapters 7 and 13, Professor Braucher noted that "[t]here is no Senate committee report, and the House Judiciary Committee report contains only a paraphrase of the provisions addressing ride-through and valuation."[45] Indeed, the House Judiciary Committee report does not contain the phrase "ride-through" at all.[46]

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[41] 11 U.S.C. §§ 524(d), 524(c)(6)(A) (2010).

[42] Philip R. Principe, *Did BAPCPA Eliminate the "Fourth Option" for Individual Debtors' Secured Personal Property?*, AM. BANKR. INST. J., Oct. 2005, at 6.

[43] *In re Donald*, 343 B.R. 524, 529 (Bankr. E.D.N.C. 2006).

[44] Dumont v. Ford Motor Credit Co. (*In re* Dumont), 581 F.3d 1104, 1110 (9th Cir. 2009).

[45] Braucher, *Rash and Ride-Through Redux, supra* note 37, at 482 n.13; *see also In re* Dumont, 581 F.3d at 1111 (noting that, in interpreting the BAPCPA, "legislative history is not an able guide").

[46] H.R. Rep. No. 109-31 (2005).

Still, many believe that Congress intended BAPCPA to eliminate ride-through.[47] Creditors' representatives heavily influenced the drafting process.[48] While the public record does not capture Congressional accession to their demands, Professor Whitford has noted that eliminating common-law ride-through was "high on the wish lists" of influential creditor interest groups.[49] If Congress complied with creditor demands – or, as one bankruptcy court suggests, employed creditor groups to draft the amendments[50] – it is almost certain that BAPCPA meant to eliminate common-law ride-through. Still, the messy drafting of BAPCPA gave way to fractured opinions on its interpretation,[51] and without a clear congressional directive, the fate of ride-through fell to the courts.

C. *In re Miller*: The Death of Ride-Through

Nearly a decade after *In re Price*, Kimberly Miller filed a Chapter 7 bankruptcy petition in Delaware.[52] When Miller filed bankruptcy, Chrysler Financial had a purchase money security interest in a Chrysler Town and Country minivan that Miller had purchased from a dealer in

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47 *E.g.*, John C. Anderson, *Highlights of the Bankruptcy Abuse Prevention and. Consumer Protection Act of 2005 – Part 1 – Consumer Cases*, 33 S.U. L. REV. 1, 14 (2005) (observing that BAPCPA "requires that the debtor reaffirm the debt").

48 *E.g.*, Braucher, *Rash and Ride-Through Redux*, *supra* note 37, at 457 (scorning BAPCPA as "a case study of what can go wrong when an interest group uses its muscle to pass a complex piece of legislation without a careful, expert drafting process.").

49 William C. Whitford, *A History of the Automobile Lender Provisions of BAPCPA*, 2007 U. ILL. L. REV. 143, 172 (2007).

50 *In re* Steinhaus, 349 B.R. 694, 706 (Bankr. D. Idaho 2006) ("Congress drafted, or allowed to be drafted by others and then enacted, provisions with 'loose' and imprecise language.").

51 Professor Braucher urged courts to interpret the ambiguity favorably for consumers to avoid rewarding creditor groups that had dominated the drafting process for their statutory mess. Braucher, *Rash and Ride-Through Redux*, *supra* note 37, at 458. A Student Note argued that the textual changes pursuant to BAPCPA were sufficiently ambiguous that the pre-2005 circuit split should continue. Christopher M. Hogan, *Will the Ride-Through Ride Again?*, 108 COLUM. L. REV. 882, 926 (2008); *but see In re* Dumont, 581 F.3d at 1112 ("It would raise serious constitutional questions for us to conclude that Congress affirmatively intended to promote the non-uniform system caused by the circuit split over ride-through.").

52 *In re* Miller, 443 B.R. 54, 55 (Bankr. D. Del. 2011). Miller filed her bankruptcy petition on June 30, 2010. *Id*.

2006.[53] Like the Prices, Miller had obligations under section 521 with respect to the encumbered vehicle. But unlike the Prices, Miller filed after the enactment of BAPCPA.

Kimberly Miller's Chapter 7 petition placed the perplexing question of post-BAPCPA ride-through squarely before the Delaware Bankruptcy Court. Like the Prices, Miller was dissatisfied by her options under the Code. She did not want to surrender her vehicle, could not afford to redeem, and wished to avoid the renewed personal liability and costs associated with reaffirmation. Accordingly, Miller neglected to check either "reaffirm" or "redeem" on her section 521 statement of intention.[54] Citing *In re Price*, Miller asserted that because she was up-to-date on loan payments, she would ride-through the car in bankruptcy.[55]

To determine whether BAPCPA eliminated ride-through, the court parsed the amendments. New section 521(a)(6) added a single phrase to section 521(2)(A). To the flush language of section 521(a) stating that "nothing in subparagraphs (A) and (B) . . . shall alter the debtor's or the trustee's rights with regard to such property under this title," section 521(a)(6) appended "except as provided in section 362(h)."[56] Section 362(h), also new under BAPCPA, allowed for the termination of the automatic stay[57]

> (1) . . . if the debtor fails within the applicable time set by section 521 (a)(2)—
>
> > (A) to file timely any statement of intention required under section 521 (a)(2) with respect to such personal property or to indicate in such statement that the debtor will either surrender such personal property or retain it and, if retaining such personal property, either redeem such

[53] *Id.* at 55. State law rather than the Bankruptcy Code defines the term "purchase money security interest." The Bankruptcy Code treats a purchase money security interest as a special form of secured debt.

[54] *Id.*

[55] *Id.* at 56.

[56] 11 U.S.C. § 521(a)(2)(*) (2010).

[57] The automatic stay is an injunction against creditor repossession, triggered by filing of a bankruptcy petition. *See* 11 U.S.C. § 362 (2010).

> personal property pursuant to section 722, enter into an agreement of the kind specified in section 524 (c) . . . ; and (B) to take timely the action specified in such statement . . . unless such statement specifies the debtor's intention to reaffirm such debt on the original contract terms and the creditor refuses to agree to the reaffirmation on such terms.[58]

The *Miller* court reasoned that the amendments to section 521 did not by themselves eliminate ride-through. But section 362(h)(1)(A) evidently required surrender, redemption, or reaffirmation[59] to enforce the automatic stay. Because Miller intended to merely "retain collateral and continue to make regular payments," her election was unsupported by BAPCPA.[60] Rather, the post-BAPCPA Code "requires a debtor to do more than merely stating that she intends to continue to make payments on a debt."[61] *In re Price* was no longer good law, and common-law ride-through no longer an option.

So far, the *Miller* holding reflects a national consensus, as courts have referenced the statutory text and each other to conclude that BAPCPA eliminated common-law ride-through.[62] Post-BAPCPA, only three statutory options remain available to Chapter 7 debtors under section 521. They must either redeem or surrender the collateral, or reaffirm the secured debt. The

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[58] 11 U.S.C. § 362(h)(1) (2010).

[59] Reaffirmation is not plainly listed, but the text refers to an "agreement of the kind specified by section 524(c)." For further discussion of section 524(c), *see supra* notes 38-41 and accompanying text.

[60] *In re* Miller, 443 B.R. 54, 58 (Bankr. D. Del. 2011).

[61] *Id*. at 59. While Chapter 7 debtors could no longer elect to ride-through an asset, the *Miller* court noted that the BAPCPA had "narrowed," rather than eliminated, the ride-though option. *Id.* at 58. This language was deliberate: in 2008, the Delaware Bankruptcy Court permitted a debtor to ride-through when the debtor had signed a valid reaffirmation agreement that was later rejected by the court. *See In re* Baker, 390 B.R. 524, 532 (Bankr. D. Del. 2008). This construction, termed "backdoor ride-through," is discussed further *infra* Part III(C).

[62] *E.g.*, *In re* Linderman, 435 B.R. 715, 718 (Bankr. M.D. Fla. 2009) ("Nationally, debtors no longer can keep personal property without reaffirming the debt or redeeming the property. All debtors are treated similarly in every circuit."); *see generally* Christopher McGowan Badger, *Coastal Federal Credit Union v. Hardiman: You Can Still "Ride-Through" the Eastern District of North Carolina*, 88 N.C. L. REV. 2249, 2255-56 (2010).

remainder of this paper considers the insufficiency of post-BAPCPA asset retention options, illustrating the advantages of statutory ride-through over the status quo.

II. ECONOMIC ANALYSIS OF SECTION 521

The two seemingly straightforward asset retention options listed in post-BAPCPA section 521 mask a more complex reality. After examining the role of each asset retention option in practice, it becomes apparent that most, and even the vast majority, of secured debt in Chapter 7 bankruptcy is not reaffirmed, and yet the assets are neither redeemed nor surrendered. In 1997, Professors Culhane and White observed that some debtors and creditors were reaching asset retention agreements outside of section 521.[63] This Part explains that result, employing economic analysis and empirical evidence to explain why rational debtors and creditors avoid redemption, reaffirmation, and surrender. The framework underpins the analysis of this Note, providing a context both to explain debtor-creditor avoidance of section 521 and also to evaluate the merit of alternatives.

A. The Analytic Framework

To appreciate the situation of Bowden, Miller, the Prices, and their secured creditors, it is necessary to first understand the structural incentives of each. Though each debtor-creditor pair shares a stake in the same asset, their subjective valuations of that asset differ. Consider three

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[63] Culhane and White discovered that although seventy-two percent of debtors indicated that they intended to reaffirm their vehicle debt, two-thirds of those reaffirmations were never filed in court. Culhane & White, *Debt After Discharge*, *supra* note 18, at 739. They then traced motor vehicle records and found "quite a few" still registered to non-reaffirming debtors. On this basis, Culhane and White concluded those parties had reached a retention agreement outside of court. *Id.* at 741; *see also U.S. Bankr. Ct., Dist. of Ariz.*, *The Honorable Eileen W. Hollowell Discusses Reaffirmation*, http://www.azb.uscourts.gov/default.aspx?PID=84 (advising Chapter 7 debtors that a creditor may say, "We don't want to bother with [reaffirmation]. Don't worry; just make your payments. Everything with be fine.") [hereinafter *Hon. Hollowell on Reaffirmation*].

values: V_D, V_C, and L. V_D is the value of the asset to the debtor at the time of filing bankruptcy. V_C is the value of the same asset to the secured creditor, or its liquidation value.[64] L is the loan outstanding on the asset when the debtor files the Chapter 7 petition. It will generally be the case that $V_D > L > V_C$.

Debtors typically value the asset above the value of the outstanding loan, $V_D > L$, for three reasons. First, debtors emerge from Chapter 7 bankruptcy as subprime borrowers who will struggle to secure a loan immediately after bankruptcy.[65] Whether a dishwasher or car, debtors come to rely upon an asset, and the inability to replace the asset disincentivizes surrender.[66] Second, there are transaction costs involved in searching for, obtaining, and in the case of a motor vehicle, registering a replacement asset. These costs can be avoided through asset retention. Third, psychological literature has shown that individuals exhibit a strong preference for assets they already possess.[67] Empirical evidence supports the assertion that debtors highly

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[64] Liquidation value might also be called "salvage value"; it is the price the creditor could obtain upon reselling the asset in the market.

[65] Katherine Porter, *Life After Debt: Understanding the Credit Restraint of Bankruptcy Debtors*, 18 AM. BANKR. INST. L. REV. 1, 9-16 (2010) (describing how few debtors had taken out loans within the year following bankruptcy, but three years out the majority had secured new credit).

[66] For many debtors, vehicles are essential for a daily work commute or for transporting family members. *See* Dumont v. Ford Motor Credit Co. (*In re* Dumont), 383 B.R. 481, 484 (B.A.P. 9th Cir. 2008) *aff'd*, 581 F.3d 1104 (9th Cir. 2009) ("Debtors usually need a car to travel to and from work, school, medical appointments, and other important activities. Having just filed for bankruptcy, they understandably expect to experience difficulty securing financing for another vehicle.").

[67] This phenomenon has been called the "endowment effect" or "status quo bias." It takes root in a series of studies demonstrating that people demand a higher price for product they own than they are willing to pay for the same product. *E.g.*, Daniel Kahneman, Jack L. Knetsch, & Richard H. Thaler, *Experimental Test of the Endowment Effect and the Coase Theorem*, 98 J. POLITICAL ECON. 1325, 1342 (1990) (finding a strong and immediate endowment effect, expressed as reluctance to trade, among subjects who were randomly awarded certain mugs or pens).

value collateral: a high percentage of debtors hope to retain collateral after emerging from bankruptcy[68] and many reaffirm the debt at a higher interest rate.[69]

It will also be true that creditors value the asset less than the outstanding loan, $L > V_C$, because consumer debts are typically undersecured, or have negative equity.[70] Used household goods, like washing machines or refrigerators, can be resold only at a fraction of their retail value. Motor vehicles depreciate most the moment they are driven from the lot, and yet are paid off according to a flat monthly schedule,[71] leaving new car lenders undersecured by an average of $4,000 at the time a debtor declares bankruptcy.[72] While not all consumer debt will adhere to this ordinal ranking, this Note assumes $V_D > L > V_C$ for encumbered assets.

B. The Impracticality of Surrender, Redemption, and Reaffirmation

Assuming $V_D > L > V_C$, economic analysis and empirical evidence show that rational debtors and creditors are likely to avoid each of the three options available under section 521. The first option, surrender, creates a social loss. Redemption is attractive but will rarely be

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[68] Culhane & White, *Debt After Discharge*, *supra* note 18, at 739 (finding that seventy-nine percent of Chapter 7 debtors intended to retain their encumbered vehicles through bankruptcy); *In re* Dumont, 581 F.3d at 1108 (noting that debtors frequently reaffirm the full value of "underwater" debts).

[69] Culhane & White, *Debt After Discharge*, *supra* note 18, at 755-56 (observing double-digit reaffirmation interest rates, with one debtor reaffirming unsecured credit card debt at an astonishing sixty percent).

[70] *E.g.*, Marianne B. Culhane & Michaela M. White, *But Can She Keep the Car? Some Thoughts on Collateral Retention in Consumer Chapter 7 Cases*, 7 FORDHAM J. CORP. & FIN. L. 471, 472 (2002) ("Consumer creditors are frequently undersecured.") [hereinafter Culhane & White, *Thoughts on Collateral Retention*]. A creditor is undersecured when the outstanding debt is greater than the fair market value of the asset.

[71] In the automobile industry, this is sometimes referred to as "drive-off depreciation." Prior to the enactment of the BAPCPA, an automobile creditor representative testified before the House Judiciary Committee that "[secured vehicle lenders] suffer the greatest losses . . . in the early years of the vehicles [sic] life when depreciation is the greatest." William C. Whitfod, *A History of the Automobile Lender Provisions of the BAPCPA*, 2007 U. ILL. L. REV. 143, 178 (2007) (citing *Bankruptcy Reform Act of 1998; Responsible Borrower Protection Act; and Consumer Lenders and Borrowers Bankruptcy Accountability Act of 1998: Hearing on H.R. 3150, H.R. 2500, and H.R. 3146 Before the Subcomm. on Commercial and Admin. Law of the H. Comm. on the Judiciary*, 105th Cong., pt. 3, at 88 (1998)). *See also In re* Robson, 369 B.R. 377, 382 (Bankr. N.D. Ill. 2007) ("Generally, vehicles depreciate the most when they are newest . . .").

[72] *See supra* note 21.

feasible. Reaffirmation, finally, is laden with transaction costs and subject to judicial rejection. More often than not, none of the three options will yield a satisfactory equilibrium outcome.

i. Surrender: The White Flag of Deadweight Loss

Debtors value collateral at V_D, an amount greater than the outstanding loan. Creditors, on the other hand, value the asset only at its resale value, V_C.[73] By transferring collateral from the debtor to creditor, surrender imposes a deadweight loss of $V_D – V_C$, causing economic distortion by forcing a transfer of an asset from a high-value to low-value user.[74] Moreover, because $V_D > L$, a debtor will not voluntarily surrender an asset; and because $L > V_C$, a creditor would prefer continuing to collect payments to repossessing the asset. Surrender represents a bargaining failure, obtained only if all other statutory options fail.

ii. Redemption: They Would if They Could

Redemption is almost always infeasible for debtors in practice. To redeem encumbered collateral, a debtor must have sufficient cash to pay the full amount of outstanding lien. Because debtors in bankruptcy are liquidity-constrained, they are generally unable to redeem collateral.[75]

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[73] The creditor retains an unsecured claim for $V_C – L$, but will collect only a minute fraction of that amount. After resale, the creditor retains an unsecured claim for the deficiency, to be asserted against other unsecured creditors in bankruptcy proceedings. 11 U.S.C. § 506(a) (2010). Such claims are virtually worthless, as unsecured creditors collect just a few cents on the dollar in Chapter 7 bankruptcy.

[74] The same argument applies to repossession, which is a functionally equivalent creditor remedy. Professor Schwartz notes that "[r]epossession 'destroys value' because individual debtors commonly value goods in excess of their market prices but repossessing creditors at best resell at these prices. Because repossession imposes greater harms on debtors than it gains for creditors, it actually minimizes social welfare." Alan Schwartz, *The Enforceability of Security Interests in Consumer Goods*, 26 J.L. & ECON. 117, 119 (1983); *see also* Culhane & White, *Thoughts on Collateral Retention*, *supra* note 70, at 474 ("[R]etention of collateral by Chapter 7 debtors ought to be facilitated, but only where retention will further the fresh start and yield creditors more than liquidation value.").

[75] *E.g.*, *In re* Price, 370 F.3d at 376 (noting that "chapter 7 debtors . . . are, by definition, insolvent and unlikely to possess the funds to buy their secured property outright"); *Hon. Hollowell on Reaffirmation*, *supra* note 63 (advising debtors that "sometimes [redemption] is an option; rarely, though, because usually it's more money than you're going to have").

Empirical evidence supports the conclusion that debtors are rarely in a position to redeem. In 1997, Professors Culhane and White found that although seventy-nine percent of Chapter 7 debtors intended to retain their encumbered asset through bankruptcy, only four percent of debtors hoped to do so by redeeming.[76] This is significant because redemption offers a relatively inexpensive method of collateral retention, requiring only retail value as opposed to the full outstanding debt.[77] Before BAPCPA, if debtors could afford to redeem collateral, they almost certainly would; yet they did not.

Following the BAPCPA amendments, it is even less likely that a debtor would redeem, because BAPCPA raised the cost of redemption. At the time of the Culhane and White study, debtors in many districts could redeem collateral by paying liquidation value, V_C.[78] The post-BAPCPA Code requires retail value to redeem, so the percentage of redeeming debtors should be even lower than the four percent observed by Culhane and White.[79] In sum, redemption is preferred by debtors, but only in the rare circumstance in which it is available.

iii. Reaffirmation: Transaction Costs and Uncertainty

Following the constructive repeal of common-law ride-through, reaffirmation is the single statutory alternative to redemption for post-bankruptcy collateral retention. On its face, it

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76 Culhane & White, *Debt After Discharge*, *supra* note 18, at 739.

77 Redeeming debtors pay only retail value for the collateral. *See supra* note 37. To reaffirm or ride-through debt, a debtor must pay the entire outstanding loan. *See supra* note 37.

78 *See supra* note 17. Because a debtor typically values an asset at above liquidation value, redemption was attractive. *See* Barry Adler, Ben Polak & Alan Schwartz, *Regulating Consumer Bankruptcy: A Theoretical Inquiry*, 29 J. LEGAL STUD. 585, 601 (2000).

79 Given the attractiveness of redemption and its infeasibility for the average consumer debtor, scholars have argued that courts should permit redemption by installments. Culhane & White, *Thoughts on Collateral Retention*, *supra* note 70, at 492-93 (citing Jean Braucher, *Increasing Uniformity in Consumer Bankruptcy: Means-Testing as a Distraction and the National Bankruptcy Review Commission's Report as a Starting Point*, 6 AM. BANKR. INST. L. REV. 1, 23 (1998); William Whitford, *Has the Time Come to Repeal Chapter 13?*, 65 IND. L.J. 85 (1989)). So far, however, the idea lacks legislative and judicial traction.

is an attractive option. Reaffirmation agreements typically require a debtor to reaffirm *L*. Because $V_D > L > V_C$, in theory, debtors and creditors should each get a surplus from entering a reaffirmation agreement as compared to surrendering the asset.[80] Yet like redemption, reaffirmation is rare in practice, for two reasons.

First, uncertainty about judicial approval may deter debtors and creditors from reaffirming debt. Reaffirmation agreements frequently do not succeed in court, either because they fail the section 524(c)(6) requirement of being in the debtor's best interests,[81] or because the parties withdraw the agreement before judicial review.[82] In 2010, a total of 359,972 reaffirmation agreements were filed, but only 2,801 – less than two percent – of the cases had reaffirmation agreements approved.[83] Particularly under BAPCPA's more stringent reaffirmation requirements, filing an agreement does not ensure that debt will be reaffirmed.

Second, reaffirmation agreements are costly, so even if they were strictly enforceable, debtors and creditors might avoid entering one. Professor Scott Ehrlich points out that the cost of complying with the reaffirmation checklist – including the requisite disclosures, income

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80 *See* Adler et al, *supra* note 78, at 601 (making this argument).

81 The BAPCPA requires courts to reject a reaffirmation agreement upon finding that the agreement either would impose an undue hardship on the debtor or the debtor's dependents, or is not in the debtor's best interest. *See* 11 U.S.C. § 524(c)(6)(A) (2010).

82 *See* discussion *infra* Part II(C)(ii).

83 U.S. BANKRUPTCY COURTS, REAFFIRMATION AGREEMENTS BY INDIVIDUAL DEBTORS WITH PREDOMINANTLY NONBUSINESS DEBTS 2010, http://www.uscourts.gov/Statistics/BankruptcyStatistics.aspx (follow "Calendar Year 2010" hyperlink under "Bankruptcy Abuse Prevention and Consumer Protection Act Statistics"; then follow "Table 4" hyperlink). The number of reaffirmation agreements filed in the United States has steadily risen in the past several years, from 113,634 agreements filed in 2007 to more than triple that number in 2010. U.S. BANKRUPTCY COURTS, REAFFIRMATION AGREEMENTS BY INDIVIDUAL DEBTORS WITH PREDOMINANTLY NONBUSINESS DEBTS 2007, http://www.uscourts.gov/Statistics/BankruptcyStatistics.aspx (follow "Calendar (follow "Calendar Year 2007" hyperlink under "Bankruptcy Abuse Prevention and Consumer Protection Act Statistics"; then follow "Table 4" hyperlink).

The report does not distinguish between reaffirmations of secured and unsecured debt, and many of the rejected agreements may have involved unsecured debt. Because more than half of consumer debt is secured, however, it is likely that at a significant portion of the reaffirmation agreements involved secured debt. *See supra* note 7. It is also unclear what percent of the ninety-eight missing reaffirmations were rejected in court. Some may have been withdrawn before judicial review. *See* discussion *infra* Part II(C)(ii).

schedules, and affidavits[84] – typically ranges from "a few hundred to several thousand dollars for each agreement."[85] This financial burden may outweigh any surplus obtained through reaffirmation. In that case, rational debtors and creditors will elect to negotiate outside of court.

From the statutory options emerges a conundrum. Most debtors cannot afford to redeem, and debtors and creditors jointly avoid surrender. Under section 521, the only other option is reaffirmation. Yet in 2010, only a small fraction of all Chapter 7 bankruptcies resulted in court-sanctioned reaffirmation agreements. Evidently, the vast majority of the secured debt in Chapter 7 bankruptcy is treated outside of section 521.

III. EXTRA-STATUTORY ALTERNATIVES

Because Chapter 7 debtors and creditors rationally avoid all three post-BAPCPA asset retention options, alternatives have emerged to fill the void. This Part considers options that exist outside of section 521. Before BAPCPA, debtors might convert to Chapter 13, and creditors might forbear on their right to repossess collateral, leading to a de facto ride-through arrangement. Following BAPCPA, these two options remain available, along with an emerging third, backdoor ride-through. A comprehensive understanding of asset retention options provides a backdrop for meaningful normative analysis.

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[84] *See* 11 U.S.C. § 524(c); *see also* discussion *supra* notes 38-41 and accompanying text. For a sample reaffirmation form, *see* U.S. CTS. BANKR. COMMITTEE, REAFFIRMATION AGREEMENT COVER SHEET, *available at* http://www.uscourts.gov/FormsAndFees/Forms/BankruptcyForms.aspx (follow "B 27" hyperlink under "Part I - Official Forms, Instructions, and Committee Notes").

[85] Scott B. Ehrlich, *The Fourth Option of Section 521(2)(a) – Reaffirmation Agreements and the Chapter 7 Consumer Debtor*, 53 MERCER L. REV. 613, 616 (2002).

A. Pre-BAPCPA: Chapter 13 and Forbearance

Professor Ehrlich argued that eliminating common-law ride-through would ultimately prove disastrous to creditors because reaffirmation imposed significant transaction costs on all parties to the bankruptcy proceeding.[86] Yet less than five years after his article was published, creditors returned to Congress to lobby *in favor of* reaffirmation.[87] Though Professor Ehrlich's analysis was robust, his doomsday forecast failed because he overlooked the alternatives that existed outside of the Code. In reality, prior to BAPCPA, a debtor might avoid section 521 entirely by converting to Chapter 13. Even more likely, a creditor who wished to avoid the transaction costs associated with reaffirmation might simply agree to forbear on repossession rights so long as the debtor made regular payments. It is likely that these extrastatutory options dominated the section 521 options before BAPCPA; and post-BAPCPA, they have likely become even more common. As Professor Ehrlich's failed prediction reveals, these options are essential to understand the incentives faced by debtors and creditors in practice.

i. Conversion to Chapter 13

At first glance, converting to Chapter 13 bankruptcy seems an attractive option for debtors who are dissatisfied with the Chapter 7 retention options. Whereas Chapter 7 allows individual filers to discharge unsecured debts in exchange for forfeiting assets, Chapter 13 allows a debtor to retain assets in exchange for paying a portion of future income to creditors.[88]

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[86] Ehrlich, *supra* note 85, at 696 (admonishing creditors to "[b]e careful what you ask for, you just may get it").

[87] *See supra* note 49 and accompanying text.

[88] Within fifteen days of filing a bankruptcy petition, a Chapter 13 debtor must propose a creditor repayment plan, under which the debtor commits a portion of future income to satisfying creditor claims. 11 U.S.C. §§ 1332,

Consumer debtors may elect to file either Chapter 7 or 13 petitions, and a debtor who files a Chapter 7 petition may later convert to Chapter 13.[89]

The disappearance of common-law ride-through left debtors to choose between the less attractive asset retention options under section 521. In theory, then, more debtors should file or convert to Chapter 13 petitions following BAPCPA. But the empirical evidence on this point is inconclusive. Before BAPCPA, a student Note observed a loose correlation between circuits allowing common-law ride-through and Chapter 13 filings,[90] but an empirical study declared a similar hypothesis "unfounded."[91] Rather, it seems likely that other considerations outweigh asset retention in the choice to file either a Chapter 7 or 13 petition.[92]

Following the BAPCPA amendments, it is even less likely that Chapter 7 debtors would convert to Chapter 13, because BAPCPA also raised the price of Chapter 13 collateral retention as part of a plan to deter abusive filers.[93] Before BAPCPA, all secured claims on consumer assets were bifurcated in bankruptcy.[94] Bifurcation divided claims into a secured portion for the value

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1333 (2010). To be approved, a Chapter 13 plan must award creditors at least as much as they would have received in Chapter 7. 11 U.S.C. § 1325(a)(4) (2010).

[89] *See* 11 U.S.C. § 706(a).

[90] Hogan, *supra* note 51, at 909.

[91] Culhane & White, *Debt After Discharge*, *supra* note 18, at 726 ("Districts with both a right to ride-through and a high Chapter 13 percentage would, we thought, have the lowest reaffirmation rates of all. Now that the facts are in, it is clear that our Chapter 13 theory was unfounded . . . [T]here is no correlation, direct or inverse, between Chapter 13 and reaffirmation rates within our districts.").

[92] For example, filers who are lured by the fresh start offered by Chapter 7 may be reluctant to agree to a payment plan awarding their future income to creditors.

[93] The BAPCPA attempted to curb abusive bankruptcy filings by raising the cost of collateral retention in Chapter 13, and then pushing high-income Chapter 7 debtors into Chapter 13. To target abusive filers, BAPCPA revised section 707(b) to implement a means test, which denied Chapter 7 relief to debtors who either acted in bad faith or had sufficient income to repay debts. The BAPCPA requires debtors who fail the means test to file petitions under Chapter 13. 11 U.S.C. § 707(b) (2010). For a general discussion of the application of the means test and its effect for individual filers, *see generally* Eugene R. Wedoff, *Means Testing in the New § 707(b)*, 79 AM. BANKR. L.J. 231, 231 (2005). For a discussion of its history, *see generally* Susan Jensen, *A Legislative History of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 79 AM. BANKR. L.J. 485 (2005).

[94] 11 U.S.C. § 506(a) (2000).

of the collateral and an unsecured claim for the deficiency.[95] Because creditors collect little of their unsecured claims,[96] bifurcation ultimately reduced debtor repayment. The post-BAPCPA Code no longer bifurcates the claims of secured creditors if the asset was acquired within the previous year, or if the secured asset is a car that was purchased within the 910 days before bankruptcy.[97] Instead, the entire loan is treated as secured debt and full repayment is required.[98]

By requiring full repayment for certain types of collateral, BAPCPA makes Chapter 13 a less desirable means of asset retention. If evidence on the correlation between Chapter 13 filings and the existence of common-law ride-through was mixed before BAPCPA, after BAPCPA conversion is even less likely.[99] In fact, Professor Braucher predicts the converse effect: "[W]ith higher repayment requirements for some collateral in chapter 13, many debtors who would have filed in chapter 13 before will now file in chapter 7."[100]

ii. Forbearance Agreements and Other Out-of-Court Bargains

Rather than file a reaffirmation agreement, debtors and creditors may enter a repayment agreement outside of court. In so doing, they avoid the cost of filing a reaffirmation agreement,

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95 *Id*.
96 *See supra* note 73.
97 11 U.S.C. § 1325(a)(*) (2010).
98 *Id*.
99 Professor Adler and colleagues analyzed the payoff to debtors and creditors of converting from Chapter 7 to Chapter 13 under the pre-BAPCPA Code. They demonstrated that a debtor would only convert to Chapter 13 when the present value of payments to creditors in Chapter 13 is less than $V_D - \beta(V_D - V_C)$, where β represents the debtor's bargaining power in Chapter 7 bankruptcy. Adler et al, *supra* note 78, at 605-6. Using this equation, Professor Adler concluded that debtors would prefer Chapter 13 in four situations: when their Chapter 13 payments are small; V_D, the value to the debtor, is large; β, the debtor's bargaining power in Chapter 7, is small; and $(V_D - V_C)$, the total surplus between debtor and creditor value, is small. *Id*. at 606. The BAPCPA amendments did not affect V_D or V_C, but the on the right-hand side of the equation, but increased the required payments to creditors. The Adler model thus supports the conclusion that fewer Chapter 7 debtors would convert to Chapter 13 following the BAPCPA. Author's note: As published, the article adds rather than subtracts V_D and $\beta(V_D - V_C)$. The typographical error has been corrected here.
100 Braucher, *Rash and Ride-Through Redux*, *supra* note 37**,** at 459 n.9. For further discussion of the failure of debtors to complete Chapter 13, *see infra* note 133 and accompanying text.

along with the risk of judicial rejection. Two forms of out-of-court bargains exist. The first, "rogue reaffirmations," are illegal reaffirmation agreements obtained when creditors approach debtors directly to reaffirm, rather than filing with the court as required by section 524. Despite their unenforceability, rogue reaffirmations were once popular, comprising one-half of all reaffirmation agreements.[101] During the 1990s, their prevalence was curbed by a series of class action lawsuits that resulted in sizable sanctions against major retailers.[102] Rogue reaffirmations have generated no major litigation since that time, and although data is unavailable, it is likely that their frequency has subsided.

Alternatively, and more commonly, creditors may simply forbear on repossession rights. A forbearing creditor agrees not to repossess collateral as long the debtor continues making regular loan payments, leading to a form of voluntary ride-through. Forbearance agreements are particularly likely in two circumstances. First, if a creditor suspects that a court might reject the reaffirmation agreement on the basis of undue hardship, and the resale value of the collateral (V_C) is low, the creditor might acquiesce with the expectation that a few monthly payments will be worth more than repossession. Alternatively, a creditor might believe that a fresh-start debtor

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[101] 1 NATIONAL BANKRUPTCY REVIEW COMMISSION, BANKRUPTCY: THE NEXT TWENTY YEARS 163 (2d ed. 1997). For further discussion, *see* Culhane & White, *Debt After Discharge*, *supra* note 18, at 717. The investigation revealed ugly facts. To evince rogue reaffirmations from debtors, creditors used everything from "offers of post-bankruptcy credit" to "deceptive threats of repossession." Culhane & White, *Thoughts on Collateral Retention*, *supra* note 70, at 483. Not only did unsuspecting debtors believe the agreements were binding, but because rogue reaffirmations look identical to valid agreements, even courts had to check records to ascertain validity.

[102] During the 1990s, the Commission responded to repeated allegations against major retailers by conducting a thorough investigation, which resulted in numerous lawsuits and hefty settlements. Sears, for example, settled a class action related to rogue reaffirmations for $320 million. See *In re* Melendez, 224 B.R. 252, 261-64 (Bankr. D. Mass. 1998). Within two years, similar class actions were brought against General Motors and Circuit City, and a coalition of state attorneys general brought suit against Federated Department Stores. *See* Ehrlich, *supra* note 85, at 628-29.

will ride-through the asset to full repayment.[103] In that case, the personal liability secured by reaffirmation is worthless, and the agreement presents needless transaction costs.

Before BAPCPA, Professors Culhane and White provided some evidence that out-of-court bargaining – either in the form of rogue reaffirmations or forbearance agreements – did in fact occur.[104] Out-of-court bargaining likely occurs more frequently in the post-BAPCPA world. By making the section 521 collateral retention options less feasible, BAPCPA increased the incentives of both debtors and creditors to reach other methods of retention in order to avoid surrender.[105] If the 1990s litigation effectively deterred rogue reaffirmations, that out-of-court bargaining is likely to take the form of forbearance agreements.

B. Post-BAPCPA: Backdoor Ride-Through

Since BAPCPA, backdoor ride-through has emerged as a new form of asset retention. Compared with forbearance agreement, which occurs in lieu of judicial proceedings, and common-law ride-through, which allowed a debtor in five circuits to elect ride-through treatment, backdoor ride-through is an ex post remedy applied by courts. To qualify for backdoor ride-through, a debtor must comply with the requirements of section 524,[106] including filing a

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[103] Braucher, *Rash and Ride-Through Redux*, *supra* note 37**,** at 476 (noting that a Chapter 7 debt discharge helps debtors pay secured debts, and "this gain in creditworthiness may more than offset the creditor's loss of recourse against the debtor personally after discharge."). This also helps explain why reaffirmation agreements frequently exceed a debtor's ability to pay. *See infra* notes 126-128 and accompanying text. Creditors pursue reaffirmation in lieu of ride-through when continued personal liability adds value; in other words, when the debtor will likely fail to repay.

[104] Culhane & White, *Debt After Discharge*, *supra* note 18, at 739-41.

[105] For further discussion, *see* Braucher, *Rash and Ride-Through Redux*, *supra* note 37**,** at 462-63 (predicting that eliminating ride-through across all jurisdictions would lead to an increase in voluntary ride-through among creditors).

[106] 11 U.S.C. §§ 521(a)(2), 521(a)(6), 362(h) (2010).

reaffirmation agreement. Then, if the court rejects the agreement,[107] the court may instead allow the debtor to ride-through the asset. This opens a limited ride-through option for debtors whom the court believes will be unduly burdened by a reaffirmation agreement, and is recognized in a growing number of jurisdictions.

The North Carolina case *Coastal Federal Credit Union v. Hardiman* is illustrative.[108] When Landon and Daffney Hardiman filed Chapter 7 bankruptcy, the couple had an outstanding loan of more than $20,000 on a Chevrolet Equinox with fair market value of $9,000. The couple entered a reaffirmation agreement with Coastal, their lender.[109] Based on pre-petition income and expenses, the court observed that the Hardimans would run a monthly deficit of more than $1,000 after making reaffirmation payments.[110] Yet the Hardimans insisted they could comply with the reaffirmation terms. They admitted that "it would be hard sometimes," but relied upon their Chevrolet to transport their three children and refused to surrender.[111]

The court ultimately found that the agreement imposed undue hardship and could not be accepted. Nonetheless, the court allowed the Hardimans to retain their vehicle. Because the Hardimans had attempted to reaffirm, the court reasoned, they met the burden of sections 521(a)(1) and 362(h), which required entering a reaffirmation agreement.[112] Although the reaffirmation agreement was rejected, the automatic stay continued under section 362, so the

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107 A court will reject a reaffirmation agreement upon finding that it imposes an undue burden or is against the debtor's best interests. *See supra* note 41.

108 Coastal Fed. Credit Union v. Hardiman, 398 B.R. 161, 165 (E.D.N.C. 2008); *see also generally* Badger, *supra* note 62 (discussing the facts of the case, and arguing that the *Hardiman* holding should be nationally adopted because it is consistent with the BAPCPA and consumer bankruptcy policy).

109 Hardiman, 398 B.R. at 166.

110 The bankruptcy court expressed concern with discrepancies between the pre-payment income asserted by the Hardimans in their initial Chapter 7 application and in the filed reaffirmation agreement. *Id.*

111 *Id.*

112 11 U.S.C. § 524(c).

Hardimans were able to backdoor ride-through their vehicle. Coastal appealed, protesting that the result reached by the court was absurd and out of line with Congressional intent.[113] The *Hardiman* court rejected both arguments,[114] and so far, other courts have ruled likewise.[115]

C. The Big Picture: Asset Retention after BAPCPA

An examination of debtor and creditor incentives, in tandem with empirical evidence, suggests that a vast amount of secured debt in Chapter 7 bankruptcy is channeled outside of section 521. Debtors may convert from Chapter 7 to Chapter 13, though few debtors will take advantage of this statutory option after BAPCPA. Debtors and creditors may also achieve resolution outside of court, typically in the form of a forbearance agreement. Finally, if debtors and creditors agree to unsustainable reaffirmation terms, courts may convert a rejected reaffirmation agreement into backdoor ride-through. While empirical evidence on the options outside 521 options is thin, it is likely that they dominate the statutory options in practice. Even before BAPCPA, debtors and creditors avoided surrender, redemption, and reaffirmation. As the attractiveness of statutory asset retention options suffers under the BAPCPA amendments, the avenues outside of 521 will attract more traffic.

In sum, by creating a dearth of feasible asset retention options by statute, BAPCPA incentivized debtors and creditors to seek recourse outside of the Bankruptcy Code. The next

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[113] *Id*. at 167. *Cf*. Hogan, *supra* note 51, at 918 ("This backdoor ride-through could be accused of bordering on judicial activism, or at least operating contrary to congressional intent.").

[114] The court found "plausible reasons" Congress might have mandated this outcome and no clear expression of contrary legislative intent. Hardiman, 398 B.R. at 179.

[115] *E.g.*, *In re* Blakeley, 363 B.R. 225, 230 (Bankr. D. Utah 2007) ("Having entered into the reaffirmation agreement 13 days after the first meeting of creditors, Debtor fully complied with the requirement under § 521(a)(6), and the remedy found under § 521(a)(6) in inapplicable to this Debtor."); *In re* Baker, 390 B.R. 524, 532 (Bankr. D. Del. 2008), *aff'd*, 400 B.R. 136 (D. Del. 2009) ("[B]ecause the Debtors timely entered into a reaffirmation agreement (regardless of whether the agreement was approved by the Court) they may retain their vehicle while staying current on their loan payments").

Part illuminates the policy problems associated with Chapter 7 asset retention following BAPCPA, while the following Part illustrates why the post-BAPCPA developments have strengthened policy arguments in favor of statutory ride-through.

IV. THE SHORTCOMINGS OF THE STATUS QUO

Consumer bankruptcy policy has three goals: to protect creditors' interests, give debtors a fresh start,[116] and promote national uniformity of law.[117] The post-BAPCPA Code falls short with respect to each objective. Part A shows how the system fails to guarantee a fresh start to debtors. Part B illustrates how the BAPCPA amendments may press unforeseen risks on secured creditors – an observation with both theoretical and political implications. Finally, Part C illustrates the irregularity and uncertainty with which the current law is applied.

A. A Disservice to Debtors

Both reaffirmation and the options outside section 521 are misaligned with the fresh start policy and a debtor's general economic interests. Scholars have long argued against reaffirmation as a violation of the fresh start policy. Moreover, as this section demonstrates, the options that have developed outside section 521 are no more helpful to Chapter 7 debtors.

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[116] *See, e.g.*, Burlingham v. Crouse, 228 U.S. 459, 473 (1913) ("It is the twofold purpose of the bankruptcy act to convert the estate of the bankrupt into cash and distribute it among creditors, and then to give the bankrupt a fresh start with such exemptions and rights as the statute left untouched.").

[117] U.S. CONST. art. I, § 8, cl. 4 (empowering Congress to establish "uniform Laws on the subject of Bankruptcies throughout the United States").

i. The General Case Against Reaffirmation

Chapter 7 protects the paradigmatic honest debtor by allowing individuals to file a petition and claim a fresh start.[118] Yet the fresh start policy is more than a moral guidepost. It also prevents the development of an insolvent underclass, incentivizes creditors to monitor debtors, and protects creditors by allowing them to discharge failed loans.[119] It has been repeatedly observed by bankruptcy scholars, courts, and policymakers that reaffirmation agreements violate the fresh start policy, because they renew personal liability for pre-bankruptcy debts following the Chapter 7 discharge.[120]

Reaffirmation agreements are also problematic in economic terms. Reaffirming secured debt gives rise to a social surplus of $V_D - V_C$, and so could theoretically benefit both debtors and creditors.[121] But under the current Code, the majority of reaffirmation surplus goes to creditors. Barry Adler and his colleagues demonstrate that if bargaining power were shared, a debtor and

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[118] H.R. Rep. No. 95-595, at 125 (stating that the purpose of Chapter 7 is for debtors to "obtain a fresh start, free from creditor harassment and free from the worries and pressures of too much debt").

[119] Thomas H. Jackson, *The Fresh-Start Policy in Bankruptcy Law*, 98 HARV. L. REV. 1393, 1395 n.5 (1985). At 1426 ("Discharge . . . heightens creditors' incentives to monitor: by providing for a right of discharge, society enlists creditors in the effort to oversee the individual's credit decisions even when the individual has not fully mortgaged his future."); Charles G. Hallinan, *The "Fresh Start" Policy in Consumer Bankruptcy: A Historical Inventory and an Interpretive Theory*, 21 U. RICH. L. REV. 49, 57 (1986) (identifying as reasons for Chapter 7 bankruptcy "a perception of insolvent debtors as potentially valuable contributors to the nation's economic development, whose participation in the economy was impeded by the hopelessness of their financial conditions," as well as a secondary argument rooted in "social utility" and a lack of blameworthiness); Eric A. Posner, *Should Debtors Be Forced into Chapter 13?*, 32 LOY. L.A. L. REV. 965, 969 (1999) ("The bankruptcy law is motivated in part by the fear that tough loan-forgiveness laws would produce a class of people who would be continually dependent on social welfare programs.").

[120] *E.g.*, H.R. Rep. No. 95-595, at 163 ("To the extent reaffirmations are enforceable, the 'fresh start' goal of the discharge provisions is frustrated."); *In re* Wilhelm, 369 B.R. 882, 883 (Bankr. M.D.N.C. 2007) ("Reaffirmation agreements are . . . contrary to one of the primary goals of the Bankruptcy Code: to provide a debtor with a fresh start."); Culhane & White, *Debt After Discharge*, *supra* note 18, at 765 ("Reaffirmation . . . too often it burdens and impedes [the fresh start].").

[121] *See supra* Part II(B)(iii).

creditor would each benefit from entering a reaffirmation agreement.[122] If the debtor has no bargaining power, however, the debtor is made worse off by reaffirming.[123] The latter case is arguably closer to reality due to two underlying inequities. First, creditors are better able to handle delays in the negotiation process.[124] Second, creditors have less to lose if the parties cannot agree to a reaffirmation agreement.[125] Indeed, the House Judiciary Committee observed that the "unequal bargaining position of debtors and creditors, and the creditors' superior experience in bankruptcy matters" leads to an overabundance of reaffirmations.[126]

Furthermore, Chapter 7 debtors frequently agree to reaffirmation terms they cannot hope to satisfy.[127] Despite the procedural safeguards of section 524(a)(6), one empirical study found that among reaffirming debtors, "[f]ewer than half . . . had any income remaining after expenses and reaffirmation payments, and only a third had more than $100 per month left."[128] This is particularly problematic because if debtors default on reaffirmation payments, they are worse off

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122 Adler et al, *supra* note 78, at 601.

123 *Id*. at 604 ("[W]hen the creditor has market power ex ante and bargaining power ex post, the borrower, who is likely a relatively poor person, not only realizes little ex post surplus but also faces a higher interest rate").

124 A debtor must comply with the section 521 timeline to propose a reaffirmation agreement. *See* U.S.C. § 521(a)(1)-(2). A creditor who refuses to negotiate may repossess the asset after 45 days and resell for liquidation value. 11 U.S.C. § 521(a)(*). For a discussion of bargaining power in two-party agreements, *see* JOEL WATSON, STRATEGY: AN INTRODUCTION TO GAME THEORY 216-222 (2nd ed. 2008).

125 Upon surrender, the creditor loses $V_C – L$, and the debtor loses $L – V_D$. *See supra* Part II(B)(i). It may not always be the case that debtors suffer a greater loss as a result of failed reaffirmation, but the creditor's loss is monetary where the debtor loses a literally irreplaceable asset. *See supra* note 66.

126 H.R. Rep. No. 95-595, at 163; *see also* Ehrlich, *supra* note 85, at 616-17 (noting that creditors occupy "an unfair bargaining position where they can demand fees and changes in payment terms as a condition to agree to the reaffirmation").

127 Bankruptcy Judge Mary Diehl explains the realities of Chapter 7 reaffirmation agreements for unrepresented debtors: "[Creditors] say, 'We know you really want to keep this car, so just sign here, and you can keep paying this car at 27% interest . . .' The debtor will sign this without ever undertaking the analysis of whether they can afford it . . ." The Honorable Mary Grace Diehl et al., *The Consumer Bankruptcy Panel: Views from the Bench – Five Years of BAPCPA*, 26 EMORY BANKR. DEV. J. 225, 239-40 (2010). *See also* Culhane & White, *Thoughts on Collateral Retention*, *supra* note 70, at 479-80 ("Experience under the Act of 1898 showed that . . . debtors all too often reaffirmed beyond their ability to repay . . . "); Adler et al, *supra* note 78, at 601 ("Debtors are said often to make foolish reaffirmation bargains, in which they give up too much for what they get.").

128 Culhane & White, *Debt After Discharge*, *supra* note 18, at 759.

than if they had simply surrendered. They both lose the underlying asset and face continued liability for any repayment deficiency, which they may be unable to discharge because the Code limits repeat bankruptcy filings.[129] From a debtor's perspective, reaffirmation is riddled with pitfalls, so it is no surprise that reaffirmation agreements are "largely creditor-driven."[130]

ii. The Trouble with the Alternatives

The asset retention options available outside section 521, while an improvement over reaffirmation, equally fail to protect debtor's interests. First, Chapter 13 is inconsistent with the policy goals underlying Chapter 7.[131] Rather than a fresh start, Chapter 13 offers asset retention in exchange for garnishing wages, which by definition impairs post-bankruptcy earning power. Moreover, as with reaffirmation agreements, debtors frequently agree to Chapter 13 repayment plans they cannot maintain.[132] The U.S. Supreme Court has noted that the "vast majority" of Chapter 13 plans fail.[133]

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[129] *See* Badger, *supra* note 62, at 2266 (citing 11 U.S.C. § 727(a)(8) (2006)).

[130] 1 NATIONAL BANKRUPTCY REVIEW COMMISSION, *supra* note 101, at 146. In the past, creditors have "aggressively pursued debtors for reaffirmations." Culhane & White, *Thoughts on Collateral Retention*, *supra* note 70, at 479-80. To secure reaffirmation agreements, creditors have even resorted to "misleading information or threats." Ehrlich, *supra* note 85, at 625. Under creditor pressure, debtors in circuits that allowed ride-through prior to BAPCPA regularly reaffirmed debts. *See* Culhane & White, *Debt After Discharge*, *supra* note 18, at 726 (finding an inverse relationship between the ride-through option and reaffirmation agreements, but noting that a significant number of debtors in ride-through districts nonetheless reaffirmed). This runs counter to economic rationality. *See supra* note 28 and accompanying text.

[131] *E.g.*, Posner, *supra* note 119, at 969 (arguing that the means test, which targets abusive Chapter 7 filers by pushing them into Chapter 13, "would defeat a purpose of bankruptcy law"). For further discussion of the means test, *see supra* note 93.

[132] Estimates of debtor default on Chapter 13 repayment plans rate range from approximately two-thirds, *see* Scott Norberg, *Consumer Bankruptcy's New Clothes: An Empirical Study of Discharge and Debt Collection in Chapter 13*, 7 AM. BANKR. L. REV. 415, 440 (1999) (finding a 68% failure rate), to 97% in certain districts, *see* William C. Whitford, *The Ideal of Individualized Justice: Consumer Bankruptcy as Consumer Protection, and Consumer Protection in Consumer Bankruptcy*, 68 AMER. BANKR. L.J. 397, 410 (1994).

In 2010, "the majority of the chapter 13 cases closed were dismissed, not closed due to plan completion." BANKRUPTCY REPORT 2010, *supra* note 7, at 14. In total, only 14 percent of debtors who closed their Chapter 13 cases in 2010 successfully completed their repayment plans – up from 6 percent in 2009. *Id*. at 16.

[133] Associates Commercial Corp. v. Rash, 520 U.S. 953, 693 (1997).

Creditor forbearance, on the other hand, protects the fresh start. Because forbearance agreements are nonrecourse, if a debtor fails to make a scheduled repayment following bankruptcy, a secured creditor may repossess the asset and nothing further. But forbearance agreements create other problems. Creditors will voluntarily forbear only when it suits their own interests, requiring only the riskiest debtors to reaffirm debt. Moreover, secured creditors are repeat players in consumer bankruptcy proceedings, so they are familiar with the nonstatutory options. Experienced counsel may also some debtors of the options outside section 521. Pro se or poorly advised debtors, however, will proceed unaware of non-statutory alternatives, which aggravates bargaining inequities.

Finally, backdoor ride-through could prove helpful to debtors, because it keeps loans nonrecourse after bankruptcy, but it is applied too unpredictably to confer benefit on Chapter 7 debtors as a class. If backdoor ride-through were to become commonplace, it might have an additional pro-debtor effect of discouraging creditors from pressing unduly exacting reaffirmation terms.[134] So far, however, the irregularity with which courts apply backdoor ride-through[135] and its uncertain status in many jurisdictions[136] will likely curtail any deterrent effect. In sum, despite its "Consumer Protection" title, BAPCPA failed to improve the position of Chapter 7 debtors.

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[134] Backdoor ride-through is detrimental to creditors for the reasons discussed *infra* Part III(B).

[135] Because backdoor ride-through requires a finding of undue hardship under the terms of a reaffirmation agreement, only poorer debtors who appear before attentive judges may access it.

[136] *See infra* Part III(C).

B. Backdoor Ride-Through and Creditor Risk

The interest in protecting creditors' interests serves as an important policy counterweight to the fresh start. Secured lending is integral to the U.S. economy, and Congress accordingly extends generous protection to secured creditors.[137] Outside of bankruptcy, creditors have the right to repossess secured collateral and retain the proceeds on sale, guaranteeing them at least liquidation value.[138] In bankruptcy, secured creditors likewise receive at least the value of their nonbankruptcy claims and potentially much more. Redemption and reaffirmation agreements, for example, actually improve the position of secured creditors over a nonbankruptcy state, by allowing a creditor to collect a portion of the deficiency in addition to the asset value.[139] These interests are both theoretical and practical, because well-funded lobbyists represent creditors' interests in Congress, with impactful results.

If secured debt is designed for creditor protection, backdoor ride-through represents a likely unintended departure from Congressional goals. Rather than protect creditors, backdoor ride-through exposes them to their riskiest debtors, enforcing a binding nonrecourse debt agreement after bankruptcy. Three variables illustrate the source of potential creditor loss. A_0 is the value of the asset at the time of bankruptcy. A_R is the asset value at the time of repossession.

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[137] *In re Dumont*, 581 F.3d at 1111 ("Because of the importance of secured lending to the nation's economy, secured creditors have been the subject of particular congressional solicitude.").

[138] Outside of bankruptcy, following default, a secured creditor has the right to repossess the collateral securing the loan. *See* U.C.C. § 9-609(a)(1) (2000). The repossession remedy affords a creditor the right to enter the debtor's premises, repossess the collateral, and dispose of the collateral in a "commercially reasonable" method. U.C.C. § 9-610; U.C.C. § 9-627 (defining "commercially reasonable"). When a consumer files Chapter 7 bankruptcy, however, an "automatic stay" is triggered, which prevents creditors from reclaiming assets. 11 U.S.C. § 362 (2010).

[139] A creditor collects retail value of collateral from redemption, liquidation value from surrender, and the value lien value when a debtor reaffirms. *See supra* Part II(B)(i)-(iii). The Code further stipulates that if a debtor fails to comply with section 521 notice requirements, a creditor is entitled to take whatever action as to such property [] is permitted by applicable nonbankruptcy law." 11 U.S.C. § 521(a)(*).

P represents the total payments on collateral received by the debtor between time bankruptcy and repossession. A creditor could be made worse off by ride-through only if $A_0 - A_R > P$, or if the post-petition reduction in asset value due to depreciation and damage outweighs the offsetting payments received during the same time period.

In lobbying against common-law ride-through, creditors protested that their interests would not be adequately protected if consumers could retain an asset without renewing personal liability. Without liability for reduced collateral value, they argued, a debtor had no incentive to maintain the value of the collateral between bankruptcy and later default.[140] The debtor might intentionally damage the asset, sabotaging creditor collection. Alternatively, the asset might depreciate too quickly for the loss of value to be offset by incoming payments. Either way, $A_0 - A_R > P$, so the creditor would suffer a loss.

In general, it is unlikely that a ride-through debtor would damage assets post-bankruptcy.[141] But a creditor would face the greatest concern when the expected payment P is low, as when default is expected after few payments. Likewise, if the expected damage or depreciation, $A_0 - A_R$, is high, a creditor might prefer to repossess rather than risk further value impairment. This situation characterizes backdoor ride-through. In order to qualify for backdoor ride-through, a court must find undue hardship, meaning the debtor has relatively low income compared to required payments. In that case, the value of incoming payments P is small, and from a creditor's perspective, the debtor is likely to default. Further, if the debtor knows that long-term asset retention is unlikely, the debtor has reduced incentive to maintain the collateral,

[140] 1 NATIONAL BANKRUPTCY REVIEW COMMISSION, *supra* note 101, at 167 (noting that creditors "wanted debtors to have an incentive to take care of the collateral and felt that personal liability provided that incentive."). In economic terms, this distortion of incentives is called the "moral hazard" problem.

[141] *See infra* note 164 and accompanying text.

so the expected damage and depreciation $A_0 - A_R$ will be large. Finally, by continuing the automatic stay, backdoor ride-through creates a binding nonrecourse retention remedy, limiting post-bankruptcy repossession rights beyond those available with common-law ride-through.

In sum, by granting debtors who are least able to pay a continued right to retain collateral without renewing personal liability, backdoor ride-through both exposes creditors to their riskiest pool of consumer debtors, and introduces a gambling aspect to reaffirmation agreements. This Note will return to both of these drawbacks to back-door ride through in Part IV(C)(ii), emphasizing the advantages of statutory over backdoor ride-through from a creditors' perspective.

C. The Jurisdictional Patchwork of Backdoor Ride-Through

As the dust settles, BAPCPA seems to have resolved the five-five circuit split by extinguishing common-law ride-through. But pulling the strings to patch one area of the bankruptcy net has created another gap. One by one, courts that reject reaffirmation agreements must consider whether the debtor may take advantage of backdoor ride-through.

The new puzzle has not created a circuit split, but adds unpredictability and irregularity to the treatment of secured debt in Chapter 7 proceedings, which in turn frustrates the constitutional mandate to create uniform bankruptcy laws.[142] Most bankruptcy courts that have reached the issue have allowed backdoor ride-through,[143] but many have not yet ruled on the issue.[144] Some

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[142] U.S. CONST. art. I, § 8, cl. 4.

[143] In December 2011, the Bankruptcy Court for the Eastern District of Michigan denied a creditor motion for rehearing after the court had allowed a debtor to backdoor ride-through. *In re* Reed, No. 10-67727, 2011 WL 6328677, at *1 (Bankr. E.D. Mich. Dec. 14, 2011). In its analysis, the court first cited seven post-BAPCPA opinions endorsing backdoor ride-through. *Id.* at *3. The court further reasoned that "[s]ince Congress didn't remove 'if applicable' with passage of BAPCPA even though this language was heavily relied upon by courts to justify ride-

courts, including the Ninth Circuit, specifically reserved the question.[145] Other courts impose additional preconditions to backdoor ride-through. At least one bankruptcy court expressed reluctance to allow backdoor ride-through if the debtor's lawyer has refused to sign the reaffirmation agreement,[146] and the *Hardiman* court suggested that a creditor could obtain relief from backdoor ride-through by showing "cause" under section 362(d).[147]

Finally, even in districts where backdoor ride-through is firmly established, it is difficult to predict to whom the new rule will apply. The process for evaluating reaffirmation agreements under BAPCPA is not uniform.[148] Because backdoor ride-through arises from rejected reaffirmation agreement, it cannot hope to be either.

V. THE POST-BAPCPA CASE FOR STATUTORY RIDE-THROUGH

In the wake of BAPCPA, the consumer bankruptcy system has become a labyrinth of inequity, failing to protect both debtors and creditors and thwarting national uniformity. This Part advocates modifying section 521 to replace reaffirmation with statutory ride-through, adding a reinstate-and-cure provision for debtors who have fallen behind on payments. It first describes the proposed reform and its anticipated impact. It then discusses the enhanced policy merit of statutory ride-through following BAPCPA. In particular, while ride-through has been urged as a

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through provisions, such congressional inaction, while not dispositive, suggests a lack of intention to eliminate the ride-through option espoused by many courts." *Id*. at *4.

[144] This is due partly to a recurrent problem of mootness. *See infra* note 168 and accompanying text.

[145] *In re* Dumont, 581 F.3d at 1112 (acknowledging that the decision "leaves the law of ride-through unclear, creating uncertainty for many Chapter 7 debtors and creditors alike") (citations omitted).

[146] *In re* Harvey, 452 B.R. 179, 186-87 (Bankr. W.D. Va. 2010) (reasoning that allowing backdoor ride-through in this case would create "a very powerful incentive to debtors and their counsel not to make the hard choices themselves but to try and put them before the court").

[147] Hardiman, 398 B.R. at 183.

[148] *See* Lisa A. Napoli, *Reaffirmation After the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005: Many Questions, Some Answers*, 81 AM. BANKR. L.J. 259, 271-74 (2007) (describing how the BAPCPA amendments to section 524 resulted in "non-uniform procedures for the evaluation of reaffirmation agreements").

pro-debtor policy, this Part describes how it would also benefit creditors as compared to backdoor ride-through. Finally, it considers the ex ante impact of backdoor ride-through, arguing that it should not adversely affect the interest rates and availability of loans to subprime borrowers.

A. Blueprint for Reform

Codifying backdoor ride-through would require little textual revision, modifying only the options available for secured collateral under section 521. Under proposed section 521, a debtor who is current on payments may elect one of three options for treatment of secured collateral: surrender, redemption, or ride-through.[149] Section 362(h), specifying that a debtor is limited to the section 521 options, is removed from the Code.[150]

The redemption and surrender options exist as under BAPCPA.[151] Statutory ride-through, unlike common-law ride-through prior to BAPCPA, applies in all circuits and incorporates a reinstate-and-cure provision akin to the one in Chapter 13.[152] Under the reinstate-and-cure provision, a debtor who has fallen behind on payments prior to filing a Chapter 7 petition may cure any default "within a reasonable time" of the bankruptcy filing.[153] After electing ride-through, the debtor continues to make payments according to the original loan schedule. If a

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[149] Compared to current section 521, the proposed text replaces reaffirmation with ride-through. *See* text accompanying *supra* note 15.

[150] By endorsing ride-through, the dominant option outside section 521, the revision voids the need for the specific limiting provision of BAPCPA. *See supra* text accompanying notes 56-59.

[151] There are compelling arguments for reducing the cost of redemption to V_C, or liquidation value, as it was before BAPCPA in many circuits. *See supra* note 17. Allowing secured creditors to collect retail value enables them to collect both the secured and a portion of the unsecured claim in bankruptcy. Thus when a debtor redeems, secured creditors take some of the funds otherwise payable to unsecured creditors. This Note supports the position that liquidation value would better effectuate the maxim that "equity delights in equality," but focuses primarily on ride-through rather than the cost of redemption as a corrective policy measure.

[152] *See* 11 U.S.C. § 1322(b)(5).

[153] *Id.*

ride-through debtor commits an act of default after emerging from bankruptcy, the creditor may repossess the asset but may not assert a claim against the debtor for the deficiency.

The proposed revisions modify debtor and creditor incentives as well as the equilibrium outcome. Assuming $V_D > L > V_C$,[154] debtors and creditors will continue to avoid surrender, and redemption will be largely infeasible.[155] Thus both debtors and creditors will prefer ride-through, much as it seemed they would prefer reaffirmation under the post-BAPCPA Code.[156] When ride-through replaces reaffirmation, however, debtors and creditors have less reason to seek out extra-statutory options. Debtors and creditors avoid reaffirmation because it costly and uncertain,[157] and instead reach out-of-court arrangements, including rogue reaffirmations and forbearance agreements. The proposed statute disincentivizes both extra-statutory options. Creditors would no longer press rogue reaffirmations because reaffirmation agreements would be strictly unenforceable, and would no longer forbear because an equivalent remedy is a statutory recourse for debtors. For the same reason, courts would no longer apply backdoor ride-through.[158] Finally, debtors could still convert to Chapter 13, but an expanded right to collateral retention in Chapter 7 makes conversion even less likely than under BAPCPA.

In sum, the major shortcomings of the current system are extinguished by replacing reaffirmation with ride-through. By making the formal options for asset retention more attractive, the proposed Code incentivizes outcomes within the legal boundaries of Chapter 7. The next Part shows how statutory ride-through protects the interests of debtors and creditors as well.

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[154] *See supra* Part II(A).
[155] *See supra* Part II(**Error! Reference source not found.**)(ii).
[156] *See supra* Part II(B)(iii).
[157] *Id.*
[158] Backdoor ride-through requires both a reaffirmation agreement and finding of undue hardship. *See supra* Part III(C). Without reaffirmation, there is no backdoor ride-through.

B. Justifying Ride-Through in a Post-BAPCPA World

The asset retention mess left by BAPCPA would be adequately swept aside by statutory ride-through. Measuring statutory ride-through against the three bankruptcy policy objectives – ensuring a fresh start, protecting creditors, and promoting uniformity – statutory ride-through outperforms the status quo with respect to all three.

Scholars, judges, and policymakers have long recognized statutory ride-through as a pro-debtor policy.[159] A ride-through debtor simply continues pre-petition loan payments, and is bound only by the original contract. This cures the fresh start problems associated with reaffirmation, and also saves the cost of negotiating and filing a reaffirmation agreement.[160] Following BAPCPA, the pro-debtor arguments have increased salience. A debtor who reaffirms under current law is uncertain whether that agreement will yield reaffirmation, a forbearance agreement, or backdoor ride-through. By allowing debtors to elect ride-through, the proposed statutory options eliminate the need to seek recourse outside the Bankruptcy Code.[161] Instead, the revised text promises both simplification and increased transparency by telling debtors exactly what their options are.

Although ride-through has generally been framed as a pro-debtor policy, there is a compelling argument that – particularly after BAPCPA – it might be framed as a pro-creditor policy as well. As Professor Ehrlich noted prior to BAPCPA, not only will statutory ride-through almost always yield liquidation value V_C to secured creditors, but in most cases will allow them

[159] In 2002, Professor Ehrlich published a thorough analysis of the pre-BAPCPA status of ride-through, arguing that ride-through, or the "Notification Interpretation," should be more widely adopted. *See generally* Ehrlich, *supra* note 85. Among other arguments, Professor Ehrlich pointed out that the ride-through voids the need for reaffirmations, and so better implements the fresh start policy of Chapter 7. *Id.* at 667.

[160] *See supra* notes 84-85 and accompanying text.

[161] *See* discussion *supra* Section V(**Error! Reference source not found.**).

to collect the outstanding loan *L*, putting them in the same place as if the debtor had reaffirmed.[162] This section examines more closely the reasons secured creditors have argued against statutory ride-through, and shows why the post-BAPCPA developments in asset retention – and in particular, backdoor ride-through – present good reasons for pro-creditor Congress to consider adopting statutory ride-through.

There are three reasons to believe that statutory ride-through protects creditors' interests. First, even if a ride-through debtor does not wholly repay the outstanding loan, a creditor will generally obtain V_C, her nonbankruptcy outcome. As discussed in Part III(**Error! Reference source not found.**), as long as the pre-petition payment schedule offsets depreciation and damage, a creditor will be no worse off repossessing after post-bankruptcy default.[163] By electing to ride-through the asset rather than simply surrender, a debtor signals a strong interest in retaining the collateral and so has little incentive to damage or destroy it. For this reason, the Third Circuit called the fear that debtors would intentionally damage ride-through assets "overstated and entirely hypothetical."[164]

Second, in the majority of cases, debtors who elect ride-through complete all outstanding loan payments, so creditors collect *L*. Two observations support this proposition. Very few

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[162] Reaffirming debt allows a creditor to re-secure debt up to *L*, the value of the lien. Ride-through, on the other hand, allows the creditor to capture V_C plus regular payments made by the debtor following bankruptcy. If the debtor completes all payments, the creditor will receive *L*, the amount of the original lien.

Similarly, edemption and surrender continue to guarantee secured creditors at least the value of their non-bankruptcy claim, V_C. To redeem, a debtor must pay retail value, which gives the creditor more than V_C. *See supra* note 37. A secured creditor collects her lowest payoff, liquidation value V_C, when the debtor surrenders the asset. *See* text accompanying *supra* note 73.

[163] *See* discussion *supra* Part III(A).

[164] *In re* Price, 370 F.3d 362, 377 (3d Cir. 2004). Instead, the court reasoned, "[i]t is just as reasonable to assume, given the difficulty insolvent consumers may have in obtaining future financing, that such debtors would have ample incentive to maintain their collateral, such as their automobiles, in good condition." *Id*. Professor Ehrlich further develops this argument, pointing out that a debtor with equity in the collateral has strong incentives to maintain its value, and that the personal liability that accompanies reaffirmation agreements is unlikely to improve the debtors' incentives in any case. Ehrlich, *supra* note 85, at 655-56.

Chapter 7 cases result in enforceable reaffirmation agreements. In 2010, only a fraction of a percentage of Chapter 7 bankruptcy petitions included approved reaffirmation agreements.[165] Instead, as Culhane and White demonstrate, many creditors agree to forbear even when reaffirmation is available.[166] The fact that creditors regularly bypass renewed personal liability suggests that ride-through and reaffirmation are relatively equivalent.[167] A recurrent problem of mootness in ride-through cases further buttresses the assertion that most debtors successfully ride-through assets: many circuits have not yet considered whether BAPCPA eliminated ride-through because the original parties no longer have standing on appeal. Consumer debt is repaid over a short loan term, and by the time the case reaches an appellate court debtors have typically repaid the outstanding loan.[168]

Third, and most importantly, a creditor may in any case alter the terms of the initial lending contract to address concerns that a debtor might damage ride-through assets. Many lending contracts contain "insecurity clauses" that allow a creditor to repossess if the asset value is threatened. For high-value collateral, particularly vehicles, creditors might further specify that

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[165] Out of 1,129,955 Chapter 7 bankruptcy petitions, there were only 2,801 approved reaffirmation agreements. *See supra* notes 7, 83.

[166] *See supra* notes 95-97 and accompanying text.

[167] When a debtor successfully rides-through, a creditor would prefer ride-through to reaffirmation because it eliminates the costs associated with negotiating and filing a reaffirmation agreement. *See* Ehrlich, *supra* note 85, at 697 ("The cost to the creditor of processing the reaffirmation agreement and the nominal increase in value received by establishing the debtor's post-discharge personal liability rarely justify the effort."). *See also supra* note 85.

[168] This circumstance occurs so frequently that parties have argued that ride-through should fall under an exception to the mootness doctrine for issues "capable of repetition, yet evading review." *See, e.g.*, *In re* Price, 370 F. 3d at 365 (considering arguments by both the Prices and Credit Union that ride-through should be heard under the "capable of repetition" exception to mootness, even though the Prices paid the full outstanding loan before the case reached the Third Circuit). Creditors have argued a mootness exception in order to continue litigation against a fully-paid debtor. *E.g.*, Reply Br. At 6, BankBoston, N.A., v. Sokolowski (*In re* Sokolowski), 205 F.3d 532, 534 (2d. Cir. 2000) (Nos. 99-5048, 99-5054). Although they stand nothing to gain against the debtor-litigant, creditors still wish to retain reaffirmation rights, which allow them to press reaffirmation agreements when personal liability would add value, and otherwise simply forbear on repossession rights.

failing to maintain submit regular proof of insurance constitutes an act of default.[169] In this way, creditors may ensure that the value of the collateral is protected post-bankruptcy, while shifting the monitoring costs to the debtor. In either case, a creditor may then repossess immediately following debtor default, virtually guaranteeing that the creditor would collect V_C in any case.[170]

From a practical perspective, comparing statutory ride-through to backdoor ride-through gives post-BAPCPA Congress reason to consider adopting the statutory version. As discussed in Part III(B), backdoor ride-through under BAPCPA presents a serious dilemma for secured creditors by introducing a gambling aspect to reaffirmation agreements. Backdoor ride-through continues the automatic stay under section 362, and so enforces a binding nonrecourse debt agreement. Statutory ride-through, on the other hand, terminates the automatic stay but allows the debtor to retain collateral. Because the terms of statutory ride-through adhere to the original lending agreement, creditors shape the terms of default and repossession. It is almost certain that the creditors' groups who shaped the BAPCPA amendments did not intend to allow backdoor ride-through, and its emergence gives ever more reason to adopt statutory ride-through in its place.

In sum, under proposed section 521, surrender and redemption yield the same payoffs as under the post-BAPCPA Code, and ride-through will generally be equivalent to reaffirmation from a creditor's perspective. In any case, through ex ante contracting, creditors may ensure that they collect at least V_C, their non-bankruptcy payoff, and so their interests are adequately

[169] "Default" is not defined by the U.C.C., but rather by the terms of the lending agreement.
[170] *See supra* note 140 and accompanying text. If a debtor must maintain insurance or surrender, a debtor cannot destroy collateral and prevent the creditor from collecting V_C. Moreover, if the debtor bears the burden of proving insurance, the creditor need not incur the transaction costs of monitoring the debtor.

protected. Given the drawbacks associated with backdoor ride-through, creditor-friendly Congress has more reason than ever to consider statutory ride-through as a viable option.

Finally, as to the third goal of bankruptcy policy, statutory ride-through enhances uniformity by unambiguously resolving the pre-BAPCPA circuit split on common-law ride-through. It further resolves two points of judicial confusion related to interpreting reaffirmation agreements under BAPCPA: whether backdoor ride-through should be imposed, and how undue hardship should be measured.[171]

C. Effect on Terms of Subprime Lending

Market analysis assumes that creditors who expect lower payment in bankruptcy will charge a higher ex ante interest rate.[172] On this basis, the Eleventh Circuit once worried that eliminating reaffirmation agreements would have the secondary effect of raising interest rates on consumer debt.[173] This section first challenges the basis for that assertion, and then argues that any small effect on credit rates due to replacing reaffirmation with ride-through would in any case reflect a shift into a fairer equilibrium.

As a threshold matter, it is unclear that the increased risk would translate into higher interest rates. First, consumer credit markets imperfectly account for risk.[174] In addition, most states impose interest rate caps on loans to subprime borrowers. The respondent's brief in *Till v. SCS Credit Corp.* provides a list of states with interest rate caps, compared with those with rates

[171] *See* discussion *supra* Part III(C).

[172] An ex ante perspective shifts the focus from Chapter 7 debtors and creditors to third parties who have not filed bankruptcy petitions. *Cf.* Adler et al, *supra* note 78, at 586-87 (advocating for and applying an ex ante approach to considering efficiency in consumer bankruptcy).

[173] *In re* Taylor, 3 F.3d at 1516.

[174] *See generally* Oren Bar-Gill, *The Behavioral Economics of Consumer Contracts*, 92 MINN. L. REV. 749 (2008) (discussing systemic mistakes that permeate the consumer credit market).

set freely by contract.[175] When the brief was filed in 2003, sixteen states had a flat interest rate cap on consumer loans, and thirteen had some other form of cap.[176] When high-risk consumers take out loans in those jurisdictions, secured creditors already charge the maximum interest rate. In that case, the increased risk would likely translate into decreased availability of high-risk loans, rather than higher credit rates, in many jurisdictions.

Yet because ride-through and reaffirmation are relatively equivalent from a creditors' perspective, the proposed revision should not adversely affect the availability of secured credit to risky consumers, either. The only loss to a creditor under the proposed system occurs in the narrow set of high-risk cases in which creditors would have benefited from personal liability through a reaffirmation agreement. In those cases, the creditor must accept a nonrecourse ride-through arrangement. The magnitude of that loss should be minimal, for the reasons described in Part IV(C)(ii): reaffirmation agreements infrequently succeed, creditors may protect themselves through altering ex ante contract terms, and backdoor ride-through already exposes creditors to a similar risk.[177]

Finally, there is a compelling normative argument that any change in lending practices under the revised Code would represent a shift into a fairer equilibrium, because the proposed changes better align the bankruptcy and nonbankruptcy states of affair. Outside of bankruptcy, creditors have the right to repossess an asset, but debtors may discharge a repayment deficiency

[175] Brief for Respondent at 3, Till v. SCS Credit Corp, 541 U.S. 465 (2004) (No. 02-1016), 2003 WL 22466039, at *17-19.

[176] *Id.*

[177] Compare this outcome to bifurcation, as in Chapter 13, which required the debtor to reaffirm only the value of the underlying collateral. In that case, creditors are limited to collect V_C in all cases, whereas statutory ride-through generally results in a repayment closer to L. It is no surprise the bifurcation proposal was "[p]erhaps the biggest concern of the automobile financing interests." Whitford, *supra* note 49, at 172.

through a bankruptcy filing.[178] With statutory ride-through, then, a secured creditor "is no more vulnerable than any lender under a consumer installment sales contract."[179] In comparison, reaffirmation allows creditors to renew personal liability for the full value of the asset – both secured and unsecured portions of the loan – effectively allowing secured the creditor to profit from the debtor's bankruptcy petition. If replacing reaffirmation with statutory ride-through caused interest rates to increase, the shift would reflect the elimination of a subsidy to subprime borrowers under the current Code.[180]

CONCLUSION

In 1977, the National Bankruptcy Review Commission advocated ride-through as a replacement for reaffirmation, but then abandoned its position.[181] Despite compelling arguments favoring statutory ride-through as a pro-debtor policy, Congress has never been swayed to implement it. This Note shows that following BAPCPA, there is more reason than ever to support statutory ride-through. Not only have the pro-debtor arguments strengthened, but the post-BAPCPA Code has evolved in a way that secured creditors – and Congress – almost certainly did not intend. By creating a holistic picture of post-BAPCPA asset retention and measuring each outcome in a simple valuation framework, this Note shows how Chapter 7

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[178] *Supra* note 20.

[179] *In re* Belanger, 962 F.2d at 348-49 (reasoning that "[a] purchaser who cannot satisfy a deficiency judgment can generally file a bankruptcy petition and obtain a discharge. This is a risk the creditor takes on any installment loan.").

[180] We could, for example, mandate that the government recompense secured lenders up to the value of their loan, which would have the effect of drastically lowering interest rates to risky credit classes. In general, bankruptcy law requires only adequate protection of secured creditors' interests, and allows the market to dictate lending rates that appropriately reflect risk. Allowing reaffirmation is in tension with that policy.

[181] In a 1977 report, the National Bankruptcy Review Commission recommended a "complete ban on reaffirmations" and explicit recognition of ride-through. 1 NATIONAL BANKRUPTCY REVIEW COMMISSION, *supra* note 101, at 166. After entertaining concerns from interested parties, the Commission revised its recommendation to endorse "limited reaffirmation rights for certain secured debts." *Id*. If limited reaffirmation rights were available, the Commission reasoned, the Code need not "provide an independent right to retain property." *Id*.

bankruptcy has developed in a way that frustrates the fresh start, exposes creditors to unforeseen risks, and evolves through disordered, idiosyncratic judicial interpretation.[182]

Compared with the fractured post-BAPCPA outcome, statutory ride-through would protect debtors by ensuring a fresh start, simplifying the available options, and lowering the price of collateral retention. More importantly, protects creditors by allowing them to potentially collect both secured and unsecured portions of their loan, while eliminating the downsides of backdoor ride-through. Finally, by making ride-through a statutory option, the proposed Code implements a uniform, predictable treatment of secured debt under section 521 for the first time in decades. The text of section 521 affects billions of dollars of secured debt and hundreds of thousands of Americans each year. Codifying statutory ride-through would ensure a more equitable and efficient treatment of that debt.

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[182] *Cf.* Braucher, *Rash and Ride-Through Redux*, *supra* note 37, at 482 (hoping that "[w]hen Congress again turns its attention to the Bankruptcy Code . . . it will have learned the lesson that personal bankruptcy law needs to be simplified to have predictable and sensible consequences").