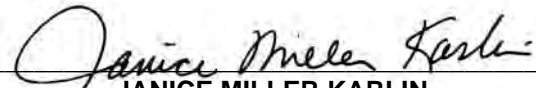




SO ORDERED.

SIGNED this 06 day of April, 2006.


JANICE MILLER KARLIN
UNITED STATES BANKRUPTCY JUDGE

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF KANSAS**

In re:)
)
CLARENCE EDWARD ELLIS)
ERIN ELLIS,) **Case No. 05-41505**
) **Chapter 13**
Debtors.)
)

**MEMORANDUM ORDER AND OPINION SUSTAINING DEBTORS' OBJECTION TO
CLAIM OF WELLS FARGO BANK AND OVERRULING, IN PART, WELLS FARGO
BANK'S OBJECTION TO CONFIRMATION OF DEBTORS' CHAPTER 13 PLAN**

This matter is before the Court on the objection of Debtors, Clarence Edward Ellis and Erin Ellis ("Debtors"), to that portion of the claim filed by Wells Fargo Bank ("Wells Fargo")¹ seeking a specified arrearage on Debtor's home mortgage, and on Wells Fargo's objection to confirmation of Debtors' Chapter 13 plan.² The latter objection is on the basis that the plan does not propose to pay the arrearage in the amount that Wells Fargo asserts is due. Thus, the core issue in both matters

¹Doc. 21.

²Doc. 16. Wells Fargo's objection to confirmation also asserts that Debtors' Chapter 13 plan cannot be confirmed because it lacks feasibility. That matter will be dealt with, below.

is the amount of the arrearage Debtors owed to Wells Fargo on their home mortgage on the date of filing. The Court has now heard evidence on this matter and is prepared to rule. This matter constitutes a core proceeding, and the Court has jurisdiction to hear it.³

I. FINDINGS OF FACT

On March 25, 1994, Debtors signed a note and mortgage with Kansas Home Mortgage of Junction City, Inc. These instruments were eventually transferred to Wells Fargo. On July 30, 2003, Wells Fargo filed a state court foreclosure action against Debtors as a result of Debtors' failure to timely make the required monthly payments. Debtors filed a counterclaim against Wells Fargo, claiming that it had mismanaged the escrow account associated with the mortgage. After a year of litigation, on March 1, 2005, the parties entered into a Settlement Agreement that was intended to resolve all issues associated with that foreclosure action. The terms of that Settlement Agreement are at the center of this dispute.

The basic terms of the settlement, contained in paragraph 6 of the agreement, required Debtors to pay Wells Fargo the sum of \$21,720.85—which represented the agreed (or settled) amount of the arrearage---in two installments. The first installment, in the amount of \$8,000.00, was due by February 25, 2005. The second installment, in the amount of \$13,720.85, was due by April 15, 2005. If Debtors complied with the terms of the Settlement Agreement, the foreclosure action was to be dismissed, and the parties would thereafter resume their contractual relationship as if there had not been a default. The dismissal was stayed, according to Paragraph 9 of the agreement, until April 16, 2005, the day after the second payment was due, to make sure Debtors made both payments. The Settlement Agreement then established the remedy if Debtors failed to “pay any of

³28 U.S.C. §§ 157(b)(2)(B) and 1334.

the payments as set forth in paragraph 6.” The agreed remedy was that “ judgment for foreclosure ‘in rem’ shall be granted to [Wells Fargo].”

The agreement unambiguously stated that it was intended to resolve all disputes between the parties. Paragraph 4 of the agreement provides:

That except as expressly provided in paragraph 9 herein, subsequent to February 18, 2005, neither [Wells Fargo] nor any other person or entity acting on their behalf, shall make any claim or cause any action to be filed against Clarence E. Ellis and Erin Ellis in connection with the following account:

Loan No. 11796531/472, 131 Robin Hood Dr., Geary County, KS 66441 or the note and mortgage executed on or about March 25, 1994 and filed with the Geary County Register of Deeds on or about March 25, 1994 at Book 114, page 1899.

This prohibition includes but is not necessarily limited to any matter or claim of any kind raised in District Court case no. 03CV198 or any claim of any kind which may have been raised in said action, regardless of whether said claim was actually made.

Paragraph 8 of the agreement states:

Upon reinstatement of loan no. 11796531/472 as set forth in this Agreement, neither the [Debtors] nor [Wells Fargo] shall have any liabilities, duties, obligations or other responsibilities beyond those contained in the aforementioned Note and Mortgage, which shall continue unaffected by, this Agreement or any other action or act by any of the parties which may have occurred on or prior to the date of execution of this Release.

Paragraph 10 of the agreement also indicates that:

This agreement does constitute and by execution of this agreement is acknowledged by all parties to be a full and complete compromise of District Court case no. 03CV198, all claims of any kind presently pending, all claims of any kind which may have been raised in said action and any claim or cause of action arising out of or related to the accounts set forth in paragraphs [sic] 4 herein.

Contemporaneously with the execution of the Settlement Agreement, the parties also filed an Agreed Journal Entry of Settlement and Dismissal with the state court. That document similarly provided that if Debtors failed to pay the two required payments, “judgment for foreclosure ‘in rem’

shall be granted to Wells Fargo.” Nothing in the Settlement Agreement contemplates what would happen if Debtors made one payment, but not the second, then filed a bankruptcy petition where they would attempt to pay the second payment over the life of the Chapter 13 plan.

Although Debtors timely made the first required payment, they failed to make the second payment due April 15, 2005. Wells Fargo then presented an Order of Sale to the state court, which was executed on April 24, 2005, reciting that “plaintiff recovered judgment for the sum of \$84,951.91, said judgment to earn interest at the rate of 8 percent per annum from December 1, 2002, on the unpaid principal balance of \$80,645.16, and said judgment to earn interest at the statutory rate from the date of judgment, until paid, costs of \$121.00, and costs accruing....”⁴

On May 12, 2005, before the Sheriff’s sale could be conducted, Debtors filed this Chapter 13 bankruptcy petition. Debtors listed Wells Fargo as a secured creditor on Schedules A and D, and indicated the amount of its secured claim was \$94,000.⁵ Their Chapter 13 plan indicated they owed an arrearage of \$13,721—a few pennies in excess of the amount of the April 15, 2005 payment they were required to pay by the terms of the Settlement Agreement.

Wells Fargo timely filed its Proof of Claim⁶ on August 20, 2005 in the amount of \$121,927.92, which set forth an arrearage of \$27,652.94—an amount more than double the amount

⁴The Court has calculated the amount of the judgment based upon the state court judgment, and it appears that as of March 18, 2005 the amount due on the judgment was \$109,763.49 (plus \$121 in costs, plus “costs accruing” and interest on the entire judgment at the statutory rate until paid). The statutory rate, pursuant to K.S.A. 16-204, was 6.25% on the date this judgment was entered, and thus, another \$1,033.78 in interest accrued through May 12, 2005, the date this bankruptcy was filed. Accordingly, on the date this bankruptcy was filed, the total amount owed on this mortgage, at least according to the state court judgment, was \$110,797.27, plus \$121 in costs “plus costs accruing,” whatever they might have been. The Court does not know if this figure accounts for the \$8,000 payment made pursuant to the Settlement Agreement on or about February 25, 2005.

⁵After hearing the evidence, the Court is unable to figure out precisely where Debtors derived that number. As noted, above, the parties apparently stipulated to the judgment amount, which appears to be in the \$102,797 range, plus or minus the \$8,000 payment. If one subtracts \$8,000 from the \$102,797, it approaches the \$94,000 figure.

⁶Claim No. 6.

of the second and final payment required under the Settlement Agreement. According to Wells Fargo, this difference is attributable to an escrow shortfall on Debtors' account that it claims was not addressed by the Settlement Agreement. Wells Fargo also claims that the figures contained in the Settlement Agreement are not now binding on it—and that it can assert whatever deficiency or arrearage its calculations now support, because Debtors breached that agreement by failing to make the second payment. Conversely, Debtors contend that if there ever was an escrow shortfall, that issue was resolved by the Settlement Agreement, and that their admitted breach of the Settlement Agreement only operated to award judgment in rem in the foreclosure action, in the amount contained in the judgment.

Additional facts will be discussed below, when necessary.

II. ANALYSIS

Wells Fargo timely filed its Proof of Claim in this case. Because Debtors objected to this Proof of Claim, however, the claim is not deemed allowed under 11 U.S.C. § 502(a),⁷ and the Court is required to conduct a hearing to determine the amount of the claim and to allow the claim in the amount it determines is proper, subject to certain exceptions not present in this case.⁸ Wells Fargo's Proof of Claim is prima facie evidence of the validity and amount of its claim, since it was executed and filed in accordance with Bankruptcy Rules and the Bankruptcy Code.⁹

⁷This case was filed before October 17, 2005, when most provisions of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) became effective. All statutory references are thus to 11 U.S.C.A. §§ 101 - 1330 (2004), unless otherwise specified. All references to the Federal Rules of Bankruptcy Procedure are likewise to Fed. R. Bankr. P. (2004), unless otherwise specified.

⁸See *In re Broadband Wireless Intern. Corp.*, 295 B.R. 140, 145 (10th Cir. BAP 2003) (citing 11 U.S.C. §§ 502(a) and 502(b)).

⁹*Id.* (citing Fed. R. Bankr. P. 3001(f)).

Because Wells Fargo's Proof of Claim is prima facie evidence of its claim, Debtors bear the burden of going forward with evidence to support their objection.¹⁰ Such evidence must be of probative force equal to that of the allegations contained in the proof of claim.¹¹ Once Debtors have reached this threshold, Wells Fargo has the ultimate burden of persuasion as to the validity and amount of its claim.¹²

The two issues the Court must resolve in this matter are (1) whether the Settlement Agreement reached in the foreclosure action was meant to include the alleged escrow shortfall on the account, and (2) what effect Debtors' admitted failure to make the second payment under the Settlement Agreement had on the amount of the claim that Wells Fargo can assert in this bankruptcy proceeding. As part of this second issue, the Court must decide what arrearage Debtors must now pay in order to obtain confirmation of their Chapter 13 plan.¹³

A. The Settlement Agreement bars Wells Fargo from now seeking to recover the alleged deficiency in the escrow account.

The Court finds that the Settlement Agreement clearly, and unambiguously, intended to—and did—resolve all issues between the parties, including any purported deficiency in any escrow account. The Settlement Agreement repeatedly stated that the parties intended to resolve any and all claims involving the Debtors' account - whether brought in the foreclosure proceeding or not. Paragraph 4 of the agreement states that “neither [Wells Fargo] nor any other person or entity acting on their behalf, shall make any claim or cause any action to be filed against Clarence

¹⁰*Id.* (citing *In re Geneva Steel Co.*, 260 B.R. 517, 524 (10th Cir. BAP 2001)).

¹¹*Id.*

¹²*Id.*

¹³Wells Fargo does not make the argument that Debtors are barred from curing the arrearage in this Chapter 13 Plan, as a result of the status of the foreclosure proceeding, it only disagrees with the amount of that arrearage.

E. Ellis and Erin Ellis in connection with the [Debtors'] account.” Paragraph 10 stated that “this agreement is acknowledged by all parties to be a full and complete compromise of District Court Case No. 03CV198, all claims of any kind presently pending, all claims of any kind which may have been raised in said action and any claim or cause of action arising out of or related to the [Debtors' account].” The Settlement Agreement at no time indicates that Wells Fargo was reserving its right to bring a later claim for any deficiency in the escrow account.

It is also important to remember the context in which the Settlement Agreement arose. Debtors had been so unhappy with Wells Fargo's handling of the escrow account that they had filed a counterclaim against Wells Fargo in the foreclosure proceeding specifically challenging how Wells Fargo had handled that account. Even if the Court had not already found that the agreement is clear and unambiguous in preventing Wells Fargo from now trying to assert the existence of a delinquency based on some purported escrow account balance owed by these Debtors in excess of the \$21,720.85 expressly agreed to, the Court finds it would be incredible to conclude that Debtors intended to settle the entire case without also resolving the very issue that had precipitated their counterclaim.

Debtors have met their burden of going forward with evidence to support their objection to Wells Fargo's Proof of Claim by introducing the Settlement Agreement into evidence, and thus the burden shifts to Wells Fargo, which bears the ultimate burden of persuasion on its claim. In light of the unambiguous, and classic, integration clause¹⁴ contained in Paragraph 10 of the Settlement

¹⁴*Cf.*, K.S.A. 84-2-202, which declares that when a writing is intended by the parties “as a final expression of their agreement,” its terms may not be contradicted by evidence of any prior agreement or contemporaneous oral agreement, and if the parties intended the contract to be the “complete and exclusive” statement of their agreement, it may not be supplemented even by noncontradictory terms. *Ray Martin Painting, Inc. v. Ameron, Inc.*, 638 F. Supp. 768, 773 (D. Kan. 1986).

Agreement, the Court finds it has not met that burden. It is clear that the Settlement Agreement was intended to resolve any and all claims concerning Debtors' account with Wells Fargo, including any potential deficiency in the escrow account.

Debtors gave up potential rights by entering into the Settlement Agreement, just as Wells Fargo did. That is the typical nature of settlements. Debtors agreed to dismiss their counterclaim against Wells Fargo arising out of its purported mishandling of the escrow agreement. In exchange, Wells Fargo agreed to a concrete figure representing the amount owed to get the account current. The Settlement Agreement clearly showed a mutual intent to settle the past problems on the account, so the parties could start fresh on what Debtors would have to pay to keep the account current, and hopefully some day pay off the mortgage.

B. The Debtors' breach of the Settlement Agreement does not entitle Wells Fargo to now double the amount of its deficiency through the medium of the escrow account.

Having determined that the parties fully intended to settle all issues relating to Debtors' mortgage arrearage with Wells Fargo by executing the Settlement Agreement, including any deficiency in Debtors' escrow account, the Court now turns to the issue of what effect Debtors' failure to fully comply with the terms of the agreement has on the parties' rights in this bankruptcy case. The Court finds that the Settlement Agreement between the parties also controls this issue. The remedy available to Wells Fargo, in the event Debtors failed to make either of the payments required by the agreement, was expressly agreed to by the parties.

Paragraph 9 of the Settlement Agreement provides that "[i]n the event [the Debtors] fail to pay any of the payments as set forth in paragraph 6, judgment for foreclosure 'in rem' shall be granted to [Wells Fargo]." It is important to note that it does not say that the Settlement Agreement

then becomes null and void, or that the parties would revert back to the litigation at the posture it was in at the time of the settlement. It also does not provide that Debtors could resume their counterclaim against Wells Fargo.

And Wells Fargo chose to avail itself of the agreed remedy, when Debtors failed to make the required payment. Wells Fargo prepared and submitted to the state court judge an Order of Sale, which was entered by the state court on April 29, 2005. The sale would have occurred but for the filing of the instant bankruptcy. Wells Fargo thus cannot have it both ways. It cannot be permitted to seek the benefit of the agreed remedy provisions contained in the Settlement Agreement - which included automatic entry of judgment in rem without any further judicial proceedings, including a potential trial on Debtors' counterclaims against it - while simultaneously attempting to repudiate those portions of the Settlement Agreement establishing that the claims between the parties had been settled within the four corners of that document.

Both Debtors and Wells Fargo bargained for, and agreed upon, the remedy available to Wells Fargo in the event Debtors failed to make the required payments under the Settlement Agreement. There is nothing in the agreement that suggests that the agreed settlement amount could be altered in the event Debtors failed to make the required payments. Likewise, there is nothing in the agreement allowing Debtors to revert back to pressing a counterclaim against Wells Fargo for its handling of the escrow account. Instead, the agreement clearly states that Wells Fargo is entitled to a judgment of foreclosure, in rem, against the property in the event of a default.

That said, Debtors' breach of the Settlement Agreement does change the bargain for Wells Fargo in one way. Instead of receiving \$13,720.85 in a lump sum on April 15, 2005, Debtors, by filing this Chapter 13 proceeding, are able to spread the repayment of that sum over the life of the

plan. This does not provide Wells Fargo the equivalent of the bargain reached. For that reason, the Court believes in this instance, in order to give effect to all terms of the Settlement Agreement, Debtors must be required to pay interest on the \$13,720.85¹⁵ so that Wells Fargo will receive the agreed sum, accounting for the time value of money.

The Settlement Agreement called for the parties to in essence continue their relationship if Debtors made the agreed payments. The note between the parties calls for repayment at 8%. It would simply not be fair to require Wells Fargo to accept the \$13,720 over 36 or more months, without interest, when it bargained for the immediate lump sum payment of that amount. Accordingly, this Court finds that to effectuate the agreement between the parties, Debtors are required to repay the \$13,720.85 at 8% interest from date of filing until that sum is paid.¹⁶

III. CONCLUSION

For the above reasons, the Court finds that Debtors' objection to that part of Wells Fargo's claim stating an arrearage of \$27,652.94 is sustained. Debtors and Wells Fargo entered into an agreement that settled their respective claims against each other concerning what amount was needed to bring the account totally current. That amount was \$21,720.85, and Debtors have paid

¹⁵The Settlement Agreement also called for Debtors to make their March and April 2005 payments of \$899.33 each on top of the settled amount, and then continue sending their regular monthly payments starting May 1, 2005. *See* ¶¶ 6 and 7. Evidence at trial was that Debtors had made each post-petition payment. Although counsel for Wells Fargo argued, in her opening statement, that the evidence would show that Debtors had paid their March payment late, that the May payment had been received, but that the April payment of \$899.33 had never been made, the Court's notes indicate neither side presented evidence on this matter. Instead, both parties were focused on the bigger picture—what overall arrearage would be allowed. If Wells Fargo claims that it is entitled to the payments due March, April and May 2005, or late or other fees associated therewith, it should seek a limited reconsideration of this order, after first consulting with Debtors' counsel to determine if an agreement on those limited additional amounts can be mutually reached before the filing of such a Motion. Clearly, under the terms of the Settlement Agreement, which this Court is enforcing herein, Wells Fargo could include in its pre-petition arrearage claim, any missed payments and associated fees for the March, April and May payments, since they were required by the original note and discussed in the Agreement.

¹⁶The Court takes judicial notice that the Chapter 13 Trustee's discount rate for cases filed in May 2005 is 7.5%, but because of the Settlement Agreement between the parties, believes that adopting the contract rate is more appropriate.

\$8,000 of that amount. Assuming Debtors paid the regular payments under the subject mortgage as they came due after the agreement, the different between those two numbers—\$13,720.85, is the arrearage that Wells Fargo can seek in this bankruptcy, with interest. If Debtors can demonstrate that they have the financial ability to make that payment, as well as all other payments required by the terms of their proposed Chapter 13 plan, this plan may well be subject to confirmation.

The Court thus finds that Wells Fargo's objection to the Debtors' Chapter 13 plan, to the extent the objection relates to the amount of arrearage provided for in the plan, is overruled. The Court directs Wells Fargo to inform the Court and opposing counsel **within 10 days** from the date of this order whether it intends to prosecute the feasibility portion of its objection, in light of this decision establishing the arrearage at \$13,720.85, plus interest at 8%. If it desires to proceed with that objection, the Court will set that remaining part of Wells Fargo's objection to confirmation to this Court's May 17-18, 2006 stacked evidentiary docket for evidence and argument.

IT IS, THEREFORE, BY THE COURT ORDERED that Debtors' objection to the arrearage claim of Wells Fargo is sustained, and that portion of Wells Fargo's objection to Debtors' plan based on the plan's failure to pay more than \$13,720.85, plus interest at 8% from the date of filing until paid, is overruled. Wells Fargo's arrearage claim shall be limited to \$13,720.85, plus 8% interest.

IT IS FURTHER ORDERED that Wells Fargo inform the Court and opposing counsel **within 10 days** from the date of this order whether it intends to proceed on the remaining portion of its objection, which relates to the feasibility of the Debtors' Chapter 13 plan. If it elects to prosecute that remaining objection, that hearing will be held on the Court's **May 17-18, 2006**, stacked evidentiary docket. If it does not elect to prosecute that remaining objection, it should file a

withdrawal of that portion of its objection within the same 10-day period so the parties can plan accordingly.

IT IS SO ORDERED.

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