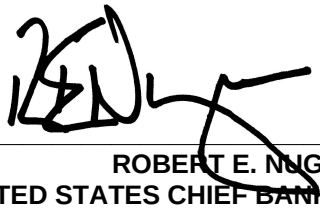
SO ORDERED.

SIGNED this 21 day of June, 2011.



ROBERT E. NUGENT
UNITED STATES CHIEF BANKRUPTCY JUDGE

OPINION DESIGNATED FOR ON - LINE PUBLICATION
BUT NOT PRINT PUBLICATION

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF KANSAS

IN RE:	)	
	)	
PAUL L. CLAY, SR.,	)	**Case No. 09-10618**
DARLA A. CLAY,	)	**Chapter 13**
	)	
Debtors.	)	
	)	

ORDER (1) GRANTING TRUSTEE'S MOTION TO MODIFY CONFIRMED PLAN (Dkt. 65); AND (2) SUSTAINING TRUSTEE'S OBJECTION TO AMENDED CLAIM OF MID AMERICA CREDIT UNION (Dkt. 54)

The debtors Paul and Darla Clay filed this bankruptcy case and their chapter 13 plan on March 13, 2009. In their plan, they proposed to repay a car loan from Mid America Credit Union (MACU) in full. The loan was secured by a purchase money security interest in a vehicle they had acquired within 910 days of the petition date. After the plan was confirmed, the vehicle was totally destroyed in an accident, and its insurance proceeds paid to MACU. The Trustee moved to modify

debtors' confirmed plan to provide for MACU's deficiency claim to be paid as an unsecured claim–pro rata.[1] At or about the same time, MACU moved to amend its secured claim by reducing its amount by the amount of insurance proceeds previously applied.[2] The Trustee objected to the amended proof of claim, asserting that MACU no longer had a secured claim.[3] For the reasons set out below, the Trustee's motion to modify the plan should be GRANTED and her objection to MACU's amended claim SUSTAINED.[4]

Jurisdiction

These matters are core proceedings pursuant to 28 U.S.C. § 157(b)(2)(B), (L), and (O). The Court has subject matter jurisdiction under 28 U.S.C. §§ 1334(b) and 157(b)(1).

Facts

The parties stipulated to an extensive list of facts that govern this controversy.[5] They may be summarized as follows. The Clays bought a vehicle with an enabling loan made by MACU within 910 days of filing their case here. On the petition date, they owed MACU $8,129.30. In their plan, the Clays undertook to pay this amount in full.[6] The Court confirmed their plan on May 13, 2009 and the Trustee began disbursing funds to the creditor. By January 20, 2010, the Trustee had

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[1] Dkt. 65.

[2] *See* Proof of Claim No. 14, filed May 26, 2010 and amending MACU's amended proof of claim no. 1

[3] Dkt. 54.

[4] The Trustee Laurie B. Williams appears by her attorney Christopher Micale. MACU appears by its attorney Eric D. Bruce. Debtors appear by their attorney William H. Zimmerman.

[5] Dkt. 76.

[6] *See* 11 U.S.C. § 1325(a)(9)(*), the so-called hanging paragraph and special treatment of 910-car loans implemented in 2005 by BAPCPA.

distributed enough money to MACU to have reduced the principal balance to $6,353.41. In February of 2010, the Clays were in a wreck that totally destroyed the car. They advised the Trustee of this fact and told her that the insurance proceeds would be paid to MACU. The Trustee ceased distribution to MACU at that time. After MACU received the insurance proceeds, it filed an amended claim for a remaining balance of $4,157.20, but maintained that its claim was still secured.[7] The parties stipulate that the insurance proceeds paid to MACU on account of the totaled vehicle was $3,778.41. The Trustee seeks to modify the debtors' plan to provide that the remaining balance owing to MACU should be treated as an unsecured claim and objects to MACU's amended claim on similar grounds.

Analysis

At issue in this case is whether a confirmed plan may be modified under § 1329(a) to provide for the surrender of the proceeds of the creditor's collateral and the payment of the creditor's remaining claim as an unsecured claim. That there are numerous reported cases on both sides of this issue is somewhat surprising, given the relatively clear meaning of the Bankruptcy Code provisions that bear on it.[8]

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[7] As noted later, this amount cannot be substantiated on the present record.

[8] Cases that permit a post-confirmation modification of plan providing for surrender of collateral and remainder of claim treated as unsecured, include: *In re Zieder,* 263 B.R. 114 (Bankr. D. Ariz. 2001); *In re Lenillen,* 322 B.R. 648 (S. D. Ind. 2005); *In re Marino,* 349 B.R. 922 (Bankr. S.D. Fla. 2006); *In re Bell,* 339 B.R. 309 (Bankr. W.D. N.Y. 2006); *In re Lane,* 374 B.R. 830 (Bankr. D. Kan. 2007); *In re Disney,* 386 B.R. 292 (Bankr. D. Colo. 2008); *In re Boykin,* 428 B.R. 662 (Bankr. D. S.C. 2009); *In re Sellers,* 409 B.R. 820 (Bankr. W. D. La. 2009); *In re Davis,* 404 B.R. 183 (Bankr. S.D. Tex. 2009); *In re Rodriguez,* 430 B.R. 694 (Bankr. M.D. Fla 2010); *In re Hutchinson,* __ B.R. __, 2011 WL 477821 (Bankr. W. D. Mo. Feb. 3, 2011). Cases disallowing such modification are led by *Chrysler Financial Corp. v. Nolan (In re Nolan),* 232 F.3d 528 (6th Cir. 2000) and *Sharpe v. Ford Motor Credit Co. (In re Sharpe),* 122 B.R. 708 (E.D. Tenn. 1991) and include: *In re Overbaugh,* 559 F.3d 125 (2nd Cir.

Debtors who have acquired vehicles with purchase money financing within 910 days of filing are required to pay the claim of their purchase money lender in full as a result of the "hanging paragraph" found in § 1325(a)(9)(*). That paragraph provides that § 506 does not apply to secured claims of this type for purposes of cramdown under § 1325(a)(5). Accordingly, whatever the vehicle may be worth, the loan it secures must be paid in full if it meets the criteria in the hanging paragraph and the debtor retains the vehicle. Put another way, the creditor's secured claim is allowed in the full amount of its claim.

Section 1329(a) allows the Trustee, the debtor, or an unsecured creditor, to seek modification of a confirmed chapter 13 plan for several limited purposes. Subsection (a)(1) permits modification to increase or reduce the amount of payments on "claims of a particular class" and subsection (a)(3) allows the modification to alter distributions to a creditor who has received payments "to the extent necessary to take account of any payment of such claim other than under the plan." Section 1329(b)(1) makes the provisions of §§ 1322(a), 1322(b), 1323(c), and 1325(a) apply to any modification allowed under § 1329(a). While § 1327(a) provides that the provisions of the confirmed plan bind the debtor and the creditors, § 1329(a)'s modification provision makes clear

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2009); *In re Crisp,* 430 B.R. 831 (Bankr. W.D. Tenn. 2010); *In re Jackson,* 280 B.R. 703 (Bankr. S.D. Ala. 2001); *In re Banks,* 161 B.R. 375 (Bankr. S.D. Miss. 1993); *In re Wilcox,* 295 B.R. 155 (Bankr. W.D. Okla. 2003); *In re Coffman,* 271 B.R. 492 (Bankr. N.D. Tex. 2002). The Tenth Circuit has not addressed this issue. An excellent summary of the issue and collection of the case law is found in Lundin's Chapter 13 treatise, Keith M. Lundin & William H. Brown, CHAPTER 13 BANKRUPTCY, 4TH EDITION, § 264.1, SEC. REV. July 14, 2004, www.Ch13online.com. The treatise authors also discuss the impact of BAPCPA's addition of the hanging paragraph and 910-car loans on this issue. *Id.* at § 506.1, ¶s 24-26, SEC. REV. Mar. 29, 2006, www.Ch13online.com. *See In re Bowman,* 2007 WL 1466743 (Bankr. W.D. Tex. May 15, 2007) (confirmed plan could be modified to surrender 910-car and treat deficiency as unsecured claim); *In re Lane, supra; In re Belcher,* 369 B.R. 465 (Bankr. E.D. Ark. 2007) (debtor not permitted to modify plan after confirmation to surrender 910-car loan in full satisfaction of debt when car is destroyed in an accident.)

that a final confirmation order may be altered in limited ways.[9]

As a matter of state law, the insurance proceeds payable to the debtors and the lender upon the "disposition" of the wrecked vehicle were "proceeds" within the meaning of KAN. STAT. ANN. § 84-9-315(a) (2010 Supp.) in which MACU retained a perfected security interest under § 84-9-315(a)(2) and (c).[10] When those proceeds were paid to MACU and applied to its claim, MACU was entitled to recover a deficiency.[11]

The Bankruptcy Code unquestionably permits the modification of a plan to reduce the amount of payments to a particular class of claims. Here, MACU was classified in a single-creditor secured class and there should be no dispute that its payments can be reduced–here, to zero. The Code also permits the alteration of the planned distribution to allow for payments that MACU received outside the plan–here, the insurance proceeds paid directly to the lender after the debtors' car was wrecked.

Likewise, so long as the modified plan contains the mandatory provisions outlined in § 1322(a) and none of its provisions breach the limits contained in (b), it complies with § 1329(b). Nothing in the proposed modification runs afoul of subsection (a). Section 1322(b)(2) expressly provides that the rights of holders of secured claims like MACU may be modified as the Trustee here proposes. Section 1325(a)(5) also applies to modified plans. Paragraph (C) of that subsection provides, as an alternative to periodic payments equal to the amount of the lender's secured claim,

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[9] *In re Hutchison*, ___ B.R. ___, 2011 WL 477821 at *3 (Bankr. W.D. Mo. Feb. 3, 2011) ("Section 1327 states the binding effect of the plan, but § 1329 specifically permits modification of a Chapter 13 plan subsequent to confirmation.").

[10] *See* KAN. STAT. ANN. § 84-9-102(a)(64)(E) (2010 Supp.) (defining proceeds to include insurance payable on loss or damage to collateral)

[11] *See* KAN. STAT. ANN. § 84-9-615(d)(2) (2010 Supp.).

the option to surrender the collateral that secures that claim. Tenth Circuit case law holds that a debtor may surrender a 910 car to his lender, but that the lender retains its state law rights to a deficiency.[12] Here, of course, the collateral was "surrendered" during the administration of the confirmed plan when MACU received payment from a source other than the debtor, the insurer. As noted above, § 1329(b) clearly allows modification of the proposed distribution to a claim-holder who has received funds from a non-plan source. Certainly, MACU is such a claim-holder.

Another judge of this Court has held, on nearly identical facts, that a modification like that proposed here by the Trustee may be confirmed. In *In re Lane*, Judge Somers carefully analyzed the statutes described above to conclude, that a similarly situated debtor could surrender the insurance proceeds of her partially-wrecked vehicle and the vehicle itself while treating the lender's deficiency as an unsecured claim.[13] Judge Somers exhaustively dealt with *In re Nolan*, the leading decision from the Sixth Circuit Court of Appeals outlining the opposing view.[14]

In *Nolan*, decided five years before the passage of BAPCPA's hanging paragraph, the Sixth Circuit concluded that § 1329(a)(1) only authorized the court to modify payments to members of classes of creditors, not their actual classification (*i.e.* "reclassify" from secured to unsecured). There, the court considered whether to confirm a modified plan that provided for a debtor's surrender of her well-used vehicle and payment of the difference between the surrendered vehicle and the lender's claim as an unsecured claim. The *Nolan* panel concluded that the confirmation of the debtor's initial plan "fixed" the secured claim and that the allowance of that claim as secured and

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[12] *See DaimlerChrysler Financial Services Americas LLC v. Ballard (In re Ballard)*, 526 F.3d 634 (10th Cir. 2008).

[13] 374 B.R. 830 (Bankr. D. Kan. 2007).

[14] *Chrysler Financial Corp. v. Nolan (In re Nolan)*, 232 F.3d 528 (6th Cir. 2000).

in an amount certain was final under § 1327(a) and therefore res judicata on subsequent efforts at modification, except in the narrow ways that § 1329(a) permits.[15] *Nolan* concluded that where the proposed modification does not comply with § 1329(a)(1), the surrender provisions of § 1325(a)(5)(c) that are read into § 1329(b) are never reached because subsection (b) plainly makes those sections applicable to "any modification under subsection (a)..."[16] The Sixth Circuit also noted that unfairness or inequity could result when debtors were permitted to rapidly depreciate their cars and then surrender them to their formerly-secured creditors with only an unsecured obligation remaining.[17]

Judge Somers noted in *Lane* that many courts agree with *Nolan* as does Norton's bankruptcy treatise.[18] He also noted that both Collier's and Judge Lundin have roundly criticized the decision in their treatises.[19] Judge Lundin states that the *Nolan* court's analysis "turns the Code on its head" by not only ignoring the plain import of § 1329, but also by operating to penalize the other unsecured creditors so that a secured creditor with no collateral can be paid what is essentially a premium.[20] *Nolan* did not consider extra-plan payments as a basis for post-confirmation modification under § 1329(a)(3), the provision that was plainly implicated here and in *Lane. Nolan* also ignores the presence in the Code of § 502(j) which allows for the reconsideration of an allowed

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[15] *Id.* at 532-33.

[16] *Id.*

[17] *Id.* at 533-34.

[18] 374 B.R. at 836.

[19] *Id.*

[20] Keith M. Lundin & William H. Brown, CHAPTER 13 BANKRUPTCY, 4TH EDITION, § 264.1, ¶ 11, SEC. REV. July 14, 2004, www.Ch13online.com.

claim for cause "according to the equities of the case." In *Lane*, the court held that post-confirmation destruction of collateral through no fault of the debtor is cause for reconsideration of the allowed claim.[21]

In this case, the debtors' car was totally destroyed through no apparent fault of their own.[22] In keeping with their legal obligations, they have permitted the proceeds of the car to be paid to their secured creditor who has, at the time of the motion to modify, no more collateral to support its "secured claim." This is the functional equivalent of a surrender. The Trustee has proposed that the payment of MACU's secured claim be reduced to zero as is plainly permitted by § 1329(a)(1). She proposes this in order to recognize that MACU has received an extra-plan distribution on account of its claim as provided for in § 1329(a)(3). In doing so, she seeks to modify MACU's secured claim as is plainly permitted by § 1322(b)(2) which is applicable to modifications under § 1329(b). Her objection to MACU's amended claim amounts to a request that the allowance of its formerly secured claim be reconsidered under § 502(j). The equities of this case, including the fact that MACU no longer has any collateral, demand that MACU's secured claim be allowed at zero, but

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[21] 374 B.R. at 839-40.

[22] There is no suggestion of bad faith on the debtors' part. And, if there were, § 1325(a)(3) also applies to modifications making bad faith a basis upon which to deny a proposed modification. See *Hutchison*, *supra* at *6 (Recognizing the potential for abuse with some modifications to surrender collateral and treat balance of claim unsecured, but noting that such abuses can be dealt with by the good faith test.); *In re Butler*, 174 B.R. 44 (Bankr. M.D. N.C. 1994) (post-confirmation modification to apply proceeds from salvage of damaged vehicle to secured claim and balance of claim treated as unsecured would not be approved where debtors failed to keep vehicle insured); *In re Cooper*, 167 B.R. 889 (Bankr. E.D. Ark. 1994) (proposed modification to surrender vehicle destroyed in post-confirmation accident was denied for not being filed in good faith where debtor caused accident and let car insurance lapse on vehicle; debtor responsible for loss of value of vehicle).

that it be permitted to make an unsecured deficiency claim.[23]

Allowing the Claim

In connection with determining the extent of MACU's unsecured deficiency claim, the Court notes a significant discrepancy between MACU's amended "secured" claim in the amount of $4,157.20 and the other amounts contained in the stipulations. The parties stipulated that the amount of MACU's initial allowed secured claim was $8,129.30 and that the debtors had made principal payments totaling $1,775.89 before the car was destroyed. Applying those payments to the beginning principal balance leaves a principal balance of $6,353.41. The parties then stipulated that the insurance payments applied to MACU's debt totaled $3,778.41. There was no stipulation concerning how these payments were applied to principal and interest. If all of the payments were applied to principal, the remaining amount due would be $2,575.

A filed proof of claim in proper form is prima facie evidence of its validity.[24] When the Trustee objected to MACU's amended claim, she had the burden to meet its presumed validity with evidence of at least equal weight that demonstrates a true dispute. If she does that, the burden of persuasion shifts to MACU to demonstrate its claim by a preponderance of the evidence. The stipulated amounts of payments, both through the plan and from the insurance proceeds, cannot be reconciled with the amount of MACU's amended claim. The Trustee has successfully demonstrated a true dispute and met the presumption of validity. As there are no calculations in the record that support the amount claimed by MACU, the Court concludes that MACU has failed to demonstrate that it should be allowed an unsecured claim in excess of $2,575, the difference between the

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[23] *Lane, supra*, at 841-42.

[24] See 11 U.S.C. § 502(a).

principal balance remaining after the application of the principal portion of the payments under the plan and the total insurance proceeds.[25] The Court therefore sustains the Trustee's objection and allows MACU's unsecured claim in the amount of $2,575.00.

The Trustee's motion to modify the debtors' confirmed plan is GRANTED and her objection to MACU's amended claim is SUSTAINED as set forth above.

# # #

[25] In other words, the Court lacks sufficient evidence to determine the impact of interest accrual from the time of the plan payments to the time of the insurance payments on the final claim amount. The stipulations are silent on that point.