IN THE UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF UTAH

CENTRAL DIVISION

In re:	:	
Richard Eugene Northington and Linda Sue Northington,	:	Bankruptcy Number 00-34258
	:	Chapter 13
Debtors.	:	

MEMORANDUM DECISION AND ORDER

David T. Berry, Berry & Tripp, Salt Lake City, Utah, for Richard Eugene Northington and Linda Sue Northington, Debtors.

This matter came before the Court on Richard Eugene Northington and Linda Sue Northington's (the "Debtors") Amended Objection to Proof of Claim 4 of Household Finance Corp. and Amended Motion to Avoid Security Interest. At a duly noticed and scheduled hearing held November 28, 2001 (the "hearing"), where the Debtors were represented by counsel, the Court took the matter under advisement in order to conduct more thorough research into the issue. No other parties appeared, and no parties have responded to the Debtors' objection.

FACTS

The facts of this matter are straightforward. The Debtors filed for bankruptcy protection under Chapter 13 on December 8, 2000. Shortly thereafter, the Debtors filed statements and schedules detailing debts and assets, including their primary residence valued at $20,000.00. In addition, the Debtors claimed a homestead exemption of $40,000.00 relating to that residence.

No objections were filed to the listed exemption, and the Debtors' plan was confirmed, by consent, July 12, 2001. Listed on the schedule of debts, is a first mortgage holder on the Debtors' residence, Utah Housing Trust Fund, whose claim, according to the proof of claim it filed, is $24,678.94. A second lien holder, Household Finance Corporation ("HFC"), also filed a proof of claim asserting a secured claim in the amount of $24,838.55 and a prepetition arrearage amount of $2,455.60. This debt is listed on the Debtors' schedule of unsecured nonpriority claims, and it is noted on the Debtors' schedules that the Debtors intend the lien to be avoided because of its entirely unsecured status.

After HFC filed its proof of claim, and after confirmation of their plan of reorganization, the Debtors filed an objection to the claim, arguing that HFC's trust deed is completely unsecured and should be avoided pursuant to 11 U.S.C. §§ 506(a) and (b), 502, and Bankruptcy Rules 4003(d) and 9014. The Debtors argue that because the value of the collateral is only $20,000.00 and the first mortgage holder's claim exceeds that value, any remaining claim holder must be entirely unsecured and, therefore, the lien on the property held by HFC may be avoided or "stripped."

DISCUSSION

A. JURISDICTION

The Court has jurisdiction over the parties and subject matter of this contested matter under 28 U.S.C. § 1334. This is a core proceeding under 28 U.S.C. § 157(b)(2)(B) and (b)(2)(K), and the Court has authority to enter a final order. Venue is proper in the Central Division of the District of Utah under 28 U.S.C. § 1409.

B. PROCEDURAL HISTORY

The Debtors brought the matter before the Court by filing an Objection to Claim as contemplated by Federal Rule of Bankruptcy Procedure 3007. The Debtors plan has previously been confirmed and the Debtors now seek to avoid the lien. In the Debtors statements and schedules, filed with the Debtors initial petition, the Debtors list the HFC debt and lien, but also state that it is the Debtors' intention to avoid the lien. More importantly, the Debtors state explicitly in their Chapter 13 plan that "[p]ursuant to 11 U.S.C. § 1322(b)(2), the wholly unsecured junior mortgage lien of Household Finance shall be avoided (qualifies for avoidance as it is wholly unsecured claim under 11 U.S.C. § 506(a)) and shall be deemed a general unsecured claim." Pursuant to this specific intention, Debtors filed their objection to claim.

Rule 3007, in relevant part, provides that "[a]n objection to the allowance of a claim shall be in writing and filed. . . . If an objection to a claim is joined with a demand for relief of the kind specified in Rule 7001, it becomes an adversary proceeding." Although Debtors specifically listed their intention to avoid the lien in their confirmed plan, arguably giving notice to HFC through notice and circulation of the plan and the Motion to Confirm Amended Plan by Consent, the Debtors did not comply with Rule 3007 and institute an adversary proceeding to specifically avoid the lien but instead filed and noticed an objection to claim. Federal Rule of Bankruptcy Procedure 7001(2) provides that "a proceeding to determine the validity, priority, or extent of a lien or other interest in property" is an adversary proceeding. Clearly, the objection filed by the Debtors is an attempt to determine the extent of HFC's lien. As such, an adversary proceeding should have commenced to "strip" HFC's lien from the Debtor's primary residence and it cannot

occur through an objection to claim.

An adversary proceeding provides specific protection to creditors with liens on property. As one court noted, "notice is to be taken particularly seriously when liens are being affected in bankruptcy. Holders of liens that may be adversely affected are entitled to unambiguous notice and an adequate opportunity to reflect and to respond." GMAC Mortgage Corp. v. Salisbury (In re Loloee), 241 B.R. 655, 662 (B.A.P. 9th Cir. 1999). By requiring an adversary proceeding to avoid a lien, debtors must comply with Rule 7004 by filing a complaint and serving a copy of the summons and complaint on the creditor. The complaint must articulate the intent to avoid a lien.

The Debtors may argue that by serving a copy of an objection to claim, along with notice of a hearing on the matter, that they are sufficiently complying with the rules.[1] However, without

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[1] The Court is aware of several cases whereby liens and security interests have been determined via means other than an adversary proceeding, whether by motion, objection, or plan confirmation. See e.g., Halverson v. Cameron (In re Mathiason), 16 F.3d 234, 237-38 (8th Cir. 1994) ("The fact that the parties did not invoke procedures ordinarily available in an adversary proceeding is not fatal."); Trust Corp. of Mont. v. Patterson (In re Copper King Inn, Inc.), 918 F.2d 1404, 1407 (9th Cir. 1990) (finding that because the validity of secured claims was debated at the hearing objecting to the reorganization plan and extensive briefs were filed that "for all practical purposes an adversarial proceeding was held"); Jones v. Progressive-Home Fed. Sav. and Loan Ass'n (In re Jones), 122 B.R. 246, 250 (W.D. Pa. 1990) ("If the objection to the proof of claim is joined with a demand for relief challenging the validity, priority, or extent of an interest in property, the objection is considered a complaint in an adversary proceeding."); In re Zobenica, 109 B.R. 814, 816 (Bankr. W.D. Tenn. 1990) (recognizing that an adversary proceeding should have been filed, but finding that upon a motion for relief by the creditor where the debtors, in objection, sought a determination of the creditor's lien that was "vigorously opposed" by the debtors, the court was not precluded from determining the extent of the lien because of a "procedural defect"); In re Nat'l Oil Co., 112 B.R. 1019, 1020 (Bankr. D. Colo. 1990) ("Pursuant to Bankruptcy Rule 3007, when an objection to claim is joined with a demand for relief of the kind specified in Rule 7001, the matter becomes an adversary proceeding. Hence, there is no need for the trustee to commence a separate adversary proceeding."). However, in each of these proceedings, the matter was actually litigated, with creditors and/or the trustee being present to appropriately argue the merits of the lien. In the case before the Court, the creditor did not appear at the objection to claim's hearing nor did HFC have the opportunity to appear at a confirmation hearing because the plan was confirmed by consent. In addition,

a copy of the complaint and summons, a creditor familiar with the rules may believe that the hearing on the objection will not effect the lien, regardless of the objection language, because the rules specifically provide that a lien may not be affected without an adversary proceeding. "Initiation of an adversary proceeding is a prerequisite to challenging 'the validity or existence' of a lien against property of the estate in a Chapter 13 proceeding . . . . Where such a proceeding 'is required to resolve the disputed rights of third parties, the potential defendant has the right to expect that the proper procedures will be followed.'" CEN-PEN Corp. v. Hanson, 58 F.3d 89, 93 (4th Cir. 1995). By allowing a lien to be avoided through the claims objection process in a non-adversary proceeding, creditors may only get notice of the plan with the lien avoidance language, but without a specific focus on their lien. Of course, in the instant case, Debtors not only provided for the lien avoidance through the plan, but have also instituted a motion to hear this specific objection to claim and have provided notice to the creditor, HFC. The creditor did not respond in any way. While HFC may have received notice of the Debtors' intention, the plain language of Rule 7001 still does not allow a lien of this type to be avoided without the instigation of an adversary proceeding.

The Court is aware of a few courts that have held that a debtor may avoid a lien without an adversary proceeding because the intent to avoid the lien was specifically stated in the confirmed plan, but these courts are in the minority.[2] The Court believes the better, and more

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HFC filed no objection or response. Therefore the court is unable to say the matter has been fully briefed or that a "de facto" adversary proceeding has been held.

[2] See e.g., Lee Servicing Co. v. Wolf (In re Wolf), 162 B.R. 98, 107-08 (Bankr. D.N.J. 1993) ("This court holds that a debtor may modify a secured creditor's claim and cancel its lien to the extent permitted under Code section 506(a) and 1325 by so providing in a chapter 13 plan without an adversary proceeding, objection to claim or motion under Bankruptcy Rule

appropriate practice is to file a complaint and instigate an adversary proceeding as the rules provide as the strong majority of cases suggests.[3] This affords the maximum protection to the creditor whose lien is subject to avoidance and grants to it the benefits of protecting that lien through the adversarial process and not through an otherwise properly noticed hearing.

CONCLUSION

Because the Court finds the objection procedurally incorrect, the Court declines to comment on the appropriateness of the relief actually requested. The Court therefore

ORDERS that Debtors' Amended Objection to Proof of Claim 4 of Household Finance Corp. and Amended Motion to Avoid Security Interest of Richard and Linda Northington is hereby denied without prejudice to being presented in a manner consistent with this Order.

DATED this _____ day of January, 2002.

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William T. Thurman
United States Bankruptcy Judge

3012."); In re Williams, 166 B.R. 615, 620 (Banrk. E.D. Va. 1994) (finding that a debtor can provide in the plan for lien avoidance without instituting an adversary proceeding).

[3] See e.g., CEN-PEN Corp. v. Hanson, 58 F.3d 89 (4th Cir. 1995); Sun Finance Co., Inc. v. Howard (In re Howard), 972 F.2d 639 (5th Cir. 1992); Foremost Fin'l Serv. Corp. v. White (In re White), 908 F.2d 691 (11th Cir. 1990); Wright v. Commercial Credit Corp., 178 B.R. 703 (E.D. Va. 1995); Simmons v. Savell (In re Simmons), 765 F.2d 547 (5th Cir. 1985); In re Vincente, 257 B.R. 168 (Bankr. E.D. Pa. 2001).

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I, the undersigned, hereby certify that I served a true and correct copy of the foregoing **Memorandum Decision and Order** by mailing the same, postage prepaid, to the following, on the ____ day of February, 2002.

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Amy K. Smedley
Law Clerk

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