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SOUTHERN DISTRICT OF CALIFORNIA
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FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF CALIFORNIA

In re

OSCAR MUNOZ and
DIANA MUNOZ,

Debtors.

Bankruptcy No. 09-07087-JM13

OPINION

I

The Chapter 13 Trustee objected to confirmation of the Debtors' plan and sought dismissal of the case on the grounds that the unsecured debt included on the schedules exceeded the limits for eligibility imposed by 11 U.S.C. § 109(e)¹. After oral argument on December 11, 2009, the Court ruled that these Debtors are eligible to proceed under Chapter 13. The Court submits this Opinion to address a legal issue that has become more prevalent in the wake of the

¹ Unless otherwise stated, all references to Section or § are to the Bankruptcy Code, 11 U.S.C. §§ 101 - 1532 (2009).

1 significant decline in real property values in many areas of the
2 country in the last few years.

3
4 II

5 FACTS

6 The Debtors' schedules contain the following information about
7 their assets and liabilities. They own a residence in Chula Vista,
8 California, which they value at \$412,000. The Debtors pledged the
9 house as collateral for two consensual obligations. The senior of
10 these obligations has an outstanding balance of \$707,452.25, secured
11 by a trust deed. The Debtors reported \$295,452.25 of this debt as
12 undersecured on Schedule D.

13 The debt secured by the junior second deed of trust is
14 \$161,382.93. The Debtors indicated this debt was fully unsecured and
15 they intended to "strip" the lien from the residence, through what has
16 become a common practice based on authority such as In re Zimmer, 313
17 F.3d 1220 (9th Cir. 2002), and In re Lam, 211 B.R. 36 (9th Cir. BAP
18 1997).

19 On Schedule F, they listed unsecured debts totaling \$300,969.48.
20 This figure includes the amount of the claim associated with the
21 wholly unsecured second trust deed. The amount of unsecured debts
22 leaps to \$596,421.73, if the undersecured portion of the first trust
23 deed is included. The Debtors filed a motion to determine the value
24 of their real property and to extinguish the lien secured by the
25 second trust deed. That uncontested motion was granted by an order
26 entered on December 11, 2009.

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III

ISSUE PRESENTED

Whether the undersecured portion of the debt secured by a consensual first priority trust deed on the Debtors' home should be included in the amount of unsecured debt for eligibility under § 109(e), when that claim is entitled to the protections afforded by the anti-modification provision found in § 1322(b)(2).

IV

DISCUSSION

Section 109(e)² limits Chapter 13 eligibility to individuals that owe noncontingent, liquidated, unsecured debts which total less than \$336,900 on the date of the filing of the petition, and secured debt of less than \$1,010,650. Eligibility is normally determined based on the figures included in the debtor's original schedules, checking only to see that the schedules were prepared in good faith. In re Scovis, 249 F.3d 975, 982 (9th Cir. 2001).

While adhering to the rule stated above, the Scovis decision applied a "principle of certainty", that a judgment lien which impaired a homestead exemption could be avoided under § 522(f). The Court of Appeals held that even though the lien would not be avoided until after the Chapter 13 petition was filed, the fact that the debtors listed the homestead exemption and the lien on the schedules provides the bankruptcy court with a sufficient degree of certainty to regard the judgment lien as unsecured as of the petition date for

² These amounts reflect the limits in effect on May 22, 2009, the date the Debtors filed their bankruptcy petition. The amounts are subject to periodic adjustment as provided in § 104.

1 eligibility purposes. Scovis, 249 F.3d at 984. Based on the
2 analysis and holding in Scovis, the amount of the debt associated with
3 the junior trust deed should be included as unsecured debt in
4 determining eligibility for Chapter 13. In re Groh, 405 B.R. 674
5 (S.Cal. 2009), In re Smith, __ B.R. __, 2009 WL 4048015 (C.Cal. 2009).
6 However, that conclusion does not end the inquiry in this case.
7 Including the debt associated with the junior lien, results in total
8 unsecured debts on the petition date of \$300,969.48, which falls
9 within the limit imposed by § 109(e).

10 Eligibility in this case hinges on a decision of whether the
11 portion of the senior debt which exceeds the value of the real
12 property is counted as secured debt or unsecured debt as of the
13 petition date for the purpose of § 109(e). The Supreme Court ruled
14 that § 1322(b)(2) prevents a bankruptcy court from modifying a lien
15 secured only by the debtor's principal residence through a Chapter 13
16 plan. In re Nobleman, 508 U.S. 324 (1993). This antimodification
17 protection applies to the entire claim even if the debt is
18 undersecured, that is, if the amount of the claim exceeds the value of
19 the property. Nobelman, 508 U.S. at 331.

20 Since the Debtors may not modify the terms of the partially
21 secured senior lien through their Chapter 13 plan, this case is
22 distinguishable from cases such as Scovis, 249 F.3d at 983-84 and In
23 re Soderlund, 236 B.R. 271 (9th Cir. BAP 1999). The Chapter 13 debtors
24 in Soderlund and Scovis could bifurcate the claims at issues between
25 a secured claim and an unsecured claim, and reduce the amount of the
26 lien against their property to the amount of the secured claim. Given
27 the holding of Nobleman, bifurcation of the debt secured by the first
28 lien on the Debtors' residence into partially secured and partially

1 unsecured claims is a legal impossibility.

2 This distinction is significant, as expressly mentioned by the
3 Panel:

4 We note that a different question might be presented if the
5 debts in question were entitled to the protection afforded
6 by § 1322(b)(2), i.e., claims secured only by a security
7 interest in real property that is the debtor's principal
8 residence. See Nobelman v. American Savings Bank, 508 U.S.
324, 113 S.Ct. 2106, 124 L.Ed.2d 228 (1993) and Dewsnup v.
Timm, 502 U.S. 410, 112 S.Ct. 773, 116 L.Ed.2d 903 (1992).
Here, the debts are not entitled to such protection,
accordingly, we do not attempt to resolve that issue.

9 Soderlund, 236 B.R. at n. 5.

10 The scenario referred to in the quote above is central to this
11 case. Some bankruptcy courts grappling with this issue have
12 determined that if the schedules reflect the claim of a secured
13 creditor as greater than the value of the collateral, then the
14 undersecured portion should be included as an unsecured debt for
15 eligibility purposes, relying on the determination of secured status
16 found in § 506(a)(1). Groh, 405 B.R. at 678; In re Werts, 410 B.R.
17 677 (Kan. 2009); In re Brammer, __ B.R. __, 2009 WL 5067632 (Dist.Col.
18 2009).

19 However, the final sentence of § 506(a)(1) mandates that the
20 "value shall be determined in light of the purpose of the valuation
21 and of the proposed disposition or use of such property, and in
22 conjunction with any hearing on such disposition or use or on a plan
23 affecting such creditor's interest." The Court of Appeals also
24 instructs us to apply a principle of certainty to consider the effect
25 of other statutes upon the secured status of a claim in determining
26 eligibility. Scovis, 249 F.3d at 984. In Scovis, the Court applied
27 this principle to treat a secured judgment claim as unsecured for
28 eligibility purposes because the Code allows the debtor to avoid the

1 judicial lien to the extent it impairs the homestead exemption. In
2 this case, we have the opposite scenario. The creditor has a
3 partially unsecured claim, but in the Chapter 13 plan, that claim must
4 be treated as fully secured under § 1322(b)(2) and Nobelman.

5 The Court agrees with the statement contained in the conclusion
6 of Groh that "In re Scovis . . . makes very clear that events like
7 obvious lien avoidance should be considered in determining a debtor's
8 eligibility. There is no reason why the same rationale would not apply
9 to a lien strip-off under 11 U.S.C. § 506(a) and § 1322(b) as it did
10 to a lien avoidance under § 522." This analysis squarely supports a
11 decision that the junior lien should be counted as unsecured debt for
12 eligibility purposes. The difference between the wholly unsecured
13 second lien and the partially unsecured first lien is that the latter
14 is not subject to "obvious lien avoidance" because it may not be
15 modified under § 1322(b) and Nobelman.

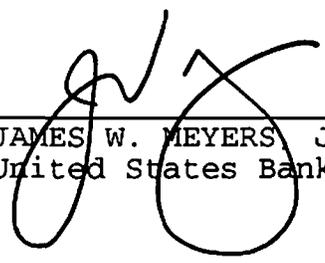
16 It is at this point the Court must diverge from the decision in
17 Groh. Instead, this Court concludes that it is more consistent to
18 consider the certainty of the effect of § 1322(b) and Nobelman in
19 classifying a debt as secured or unsecured for eligibility purposes.
20 The Court agrees with a conclusion in the Smith decision, that it is
21 more appropriate to treat the debt secured by a lien in the same
22 manner for confirmation and eligibility purposes. The wholly
23 unsecured junior lien should be treated as unsecured for both
24 confirmation and eligibility, while the partially secured senior lien
25 should be treated as secured for both purposes.

26
27 V.

28 CONCLUSION

1 The "undersecured" portion of a lien that cannot be modified in
2 Chapter 13 should not be included in the amount of unsecured debts for
3 purposes of determining eligibility under 11 U.S.C. § 109(e), but as
4 part of the amount of secured debts. The Debtors are eligible to
5 proceed under Chapter 13 and the Trustee's motion to dismiss the case
6 is denied. Counsel for the Debtors is instructed to file an order
7 confirming the Chapter 13 plan within 14 days of entry of this
8 Opinion.

9 DATED: JAN 12 2010



JAMES W. MEYERS JUDGE
United States Bankruptcy Court

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