

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF INDIANA
SOUTH BEND DIVISION

IN THE MATTER OF)	
)	
JAMES RAY DALTON and)	CASE NO. 02-36393 HCD
LINDA D. DALTON,)	CHAPTER 13
)	
DEBTORS.)	
)	
)	
JAMES RAY DALTON and)	
LINDA D. DALTON,)	
PLAINTIFFS.)	
vs.)	PROC. NO. 02-3137
)	
FIVE STAR CREDIT UNION,)	
DEFENDANT.)	

Appearances:

Debra Voltz-Miller, Esq., attorney for debtors, 108 North Main Street, Suite 328, South Bend, Indiana 46601;
William C. Elliott, Esq., attorney for defendant, 556 South Perry Street, Montgomery, Alabama 36104; and
Debra L. Miller, Esq., Standing Chapter 13 Trustee, P.O. Box 11550, South Bend, Indiana 46634-0550.

MEMORANDUM OF DECISION

At South Bend, Indiana, on November 6, 2003.

Before the court are the complaint of the plaintiffs, debtors James Ray Dalton and Linda D. Dalton (“plaintiffs” or “debtors”), and the motion to dismiss of the defendant Five Star Credit Union (“defendant” or “credit union”). At issue in this adversary proceeding is the status of a 1998 Mazda 626 automobile. Six days before the plaintiffs filed their chapter 13 bankruptcy petition in this court, the defendant repossessed the Mazda. The debtors filed a Complaint for Turnover of Automobile soon after filing bankruptcy. Almost five months thereafter, the defendant returned the vehicle to them. It then filed a Motion to Dismiss Adversary Proceeding. The debtors objected to dismissal and demanded damages. The court took the matters under advisement.

Jurisdiction

Pursuant to 28 U.S.C. § 157(a) and Northern District of Indiana Local Rule 200.1, the United States District Court for the Northern District of Indiana has referred this case to this court for hearing and determination. After reviewing the record, the court determines that the matter before it is a core proceeding within the meaning of § 157(b)(2)(E) over which the court has jurisdiction pursuant to 28 U.S.C. §§ 157(b)(1) and 1334. This entry shall serve as findings of fact and conclusions of law as required by Federal Rule of Civil Procedure 52, made applicable in this proceeding by Federal Rules of Bankruptcy Procedure 7052 and 9014. Any conclusion of law more properly classified as a factual finding shall be deemed a fact, and any finding of fact more properly classified as a legal conclusion shall be deemed a conclusion of law.

Background

A. Procedural History

The plaintiffs filed their chapter 13 bankruptcy petition on November 5, 2002, and their Complaint for Turnover of Automobile on November 21, 2002. After the defendant answered the complaint and the court conducted a pre-trial hearing, the parties expressed their willingness to attempt resolution. On April 13, 2003, less than a month after the pre-trial, the defendant returned the vehicle to the plaintiffs. The Mazda has remained in the debtors' possession. Ten days later, the defendant filed a Motion to Dismiss Adversary Proceeding, asserting two grounds for dismissal: first, that the proceeding was moot because the defendant had turned over the automobile to the plaintiffs; and second, that the automobile was not property of the debtors' estate. The debtors filed their Objection to Motion to Dismiss Adversary Proceeding on May 2, 2003, insisting that the proceeding was not moot because damages were due and owing to them.

Following the pre-trial conference held June 4, 2003, the court directed the parties to file an agreed stipulation of facts and briefs on the issues. *See* R. 24, Order of June 11, 2003. The parties did not file stipulated facts; however, they filed briefs. The defendant filed its brief in the form of a Motion for Summary Judgment

and a memorandum in support of the motion. Once the briefing schedule had expired, the court took the complaint and motion under advisement.

B. Factual Background

Although the parties failed to file the agreed stipulation of facts ordered by this court, the court finds that the relevant facts in this proceeding are not in contention. The Daltons entered into a loan agreement with the credit union in Alabama on April 6, 1999. They signed a promissory note, secured by a parcel of real property and a 1998 Mazda, and received \$20,957.36, to be repaid in 71 installments commencing May 1999.

The debtors are not strangers to bankruptcy proceedings. On June 25, 1999, they filed a chapter 13 bankruptcy petition in Alabama, listing the credit union as a secured creditor. The case was dismissed on May 12, 2000. In the meantime, the debtors had moved to Indiana. They filed a chapter 7 bankruptcy petition on June 28, 2000, in this court, again listing the credit union as a secured creditor. Although they stated their intention to reaffirm their loan from the defendant, they never executed a reaffirmation agreement. They received a discharge on or about September 25, 2000.

The debtors, having retained the Mazda, entered into a new loan agreement with the defendant on March 30, 2001. That agreement, financing \$23,938.04, stated that the debtors would pay \$200.00 per month for a year, beginning April 30, 2001, with a balloon payment at the end. The collateral securing the agreement was the same Mazda and parcel of property. At the end of that year, the debtors did not make a balloon payment. The credit union offered them another loan agreement on May 21, 2002, requiring payments of \$225 monthly for one year. The Daltons did not sign that 2002 agreement and did not pay the increased monthly amounts. In fact, the record indicates that the debtors made no payments to the credit union between May 2, 2002, and September 5, 2002; moreover, the payments of September 5 and October 3, 2002, were for \$200, not \$225. On October 30, 2002, the credit union repossessed the debtors' 1998 Mazda.¹

¹ The parcel of real property securing the promissory note was sold in October 2002. On
(continued...)

The plaintiffs filed the present chapter 13 bankruptcy case on November 5, 2002. On November 6, 2002, by letter, they requested the return of the automobile. On November 21, 2002, the debtors filed their Complaint for Turnover, seeking the immediate return of the vehicle and damages, based upon the vehicle's depreciation, lost wages, costs and attorney fees.² On April 13, 2003, the credit union returned the vehicle to the debtors. Nevertheless, the debtors continued to demand damages, claiming that the defendant violated the automatic stay. The credit union challenged the debtors' valuation of the Mazda and asserted that the vehicle was never property of the debtors' estate.

Discussion

The key facts before the court are that the defendant, a secured creditor, repossessed the debtors' 1998 Mazda six days before the debtors filed their chapter 13 petition and returned it five months after the filing. The debtors' claims are threefold: (1) The Mazda was property of the debtors' chapter 13 estate, and the secured creditor was required to turn over possession of the vehicle to them. (2) The creditor willfully violated the automatic stay by not turning over the property after the debtors filed their bankruptcy petition, knowing that the automatic stay was in effect, that the vehicle was insured, that it had entered into a loan agreement with the debtors after the chapter 7 discharge, and that the debtors and Trustee were willing to provide adequate protection payments. (3) The creditor's continued possession and control over the vehicle from November 5, 2002 through April 13, 2003, was a continuing violation of the automatic stay and was egregious conduct sufficient to warrant the imposition of actual and punitive damages under § 362(h).

¹(...continued)

November 4, 2002, the defendant received the net proceeds from the sale, \$4,601.30, and released the mortgage to the purchasers.

² The debtors' chapter 13 plan lists the credit union as a secured creditor and places a value on the 1998 Mazda of \$6,870. The plaintiffs state that they have made timely payments to the chapter 13 trustee during the course of the bankruptcy.

The creditor denies each of those allegations. It points out that, at the time the debtors received a chapter 7 discharge on September 25, 2000, the creditor had a properly perfected security interest in the Mazda.³ Therefore, it was not in violation of the automatic stay when it repossessed the vehicle prior to the debtors' chapter 13 bankruptcy. Moreover, it asserts, once it repossessed the vehicle, the debtors had neither the right of redemption nor of possession of the car when they filed their chapter 13 petition. It insists that its return of the vehicle post-petition is not a waiver of its legal position. It asks for summary judgment in its favor.

The debtors are authorized, pursuant to 11 U.S.C. § 542, to seek the turnover of the vehicle in the creditor's possession if it is "property of the estate." "Property of the estate" includes "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a)(1). This broad, inclusive definition includes "property of the debtor that has been seized by a creditor prior to the filing of a petition." *United States v. Whiting Pools, Inc.*, 462 U.S. 198, 103 S. Ct. 2309, 2315, 76 L.Ed.2d 515 (1983). To determine whether these debtors have sufficient interest in their repossessed Mazda to constitute "property of the estate," the court turns to Indiana law. *See Butner v. United States*, 440 U.S. 48, 55, 99 S. Ct. 914, 918, 59 L.Ed.2d 136 (1979) ("Property interests are created and defined by state law."). A bankruptcy court determines the nature of a debtor's interest in property by looking to state law, but determines whether that interest counts as property of the estate by looking to federal bankruptcy law. *See In re Krueger*, 192 F.3d 733, 737 (7th Cir. 1999).

³ In reviewing this record, the court finds that the Mazda was estate property during the debtors' chapter 7 proceeding and that the debtors intended but failed to reaffirm the credit union loan secured by the Mazda. It is clear law in this circuit that the debtors had the options of choosing to reaffirm, redeem, or surrender the property. *See* 11 U.S.C. § 521(2); *In re Edwards*, 901 F.2d 1383, 1385 (7th Cir. 1990). Because they wished to retain the vehicle, they were required under the Bankruptcy Code to redeem or reaffirm. *See id.* at 1386 (stating that "[n]o debtor would reaffirm personal liability unless required to do so"). *Edwards* makes clear that debtors may not choose to retain possession of the collateral simply by continuing to make regularly scheduled payments. These debtors did just that, however. After their discharge, they were no longer personally liable upon default. "The creditor's only recourse in such a case would be to seek repossession of the collateral." *Id.* at 1384 n.3. Nevertheless, the credit union continued its business relationship with the debtors. It offered them new loan agreements in March 2001 and May 2002. It was not until the debtors failed to sign the 2002 agreement and stopped making monthly payments that the credit union repossessed the vehicle.

Most bankruptcy and district courts have concluded that “a Chapter 13 debtor retains sufficient interest in a vehicle that was repossessed pre-bankruptcy to maintain an action or motion for turnover.” *In re Coleman*, 229 B.R. 428, 430 (Bankr. N.D. Ill. 1999) (citing cases). The *Coleman* court found that, under Illinois law, although legal title passes to a secured creditor after it takes possession following default, the debtor retains significant rights and responsibilities in the collateral. *See id.* at 431 (citing *Kouba v. East Joliet Bank*, 481 N.E.2d 325, 329 (Ill. Ct. App. 1985)). Our sister bankruptcy courts in Illinois are in agreement:

This court believes that the situation presented in this case [a demand for turnover of a vehicle repossessed prepetition] falls squarely within *Whiting Pools*' conclusion that until a sale has taken place, property seized prepetition pursuant to a creditor's provisional remedy remains property of the estate, and as such, is subject to the turnover requirements of § 542(a).

Spears v. Ford Motor Credit Co. (In re Spears), 223 B.R. 159, 165 (Bankr. N.D. Ill. 1998) (citing *Whiting Pools*, 462 U.S. at 211, 103 S. Ct. at 2316-17). *Accord, In re Coleman*, 229 B.R. 431; *In re Nash*, 228 B.R. 669, 673 (Bankr. N.D. Ill. 1999).

Some courts have found that, under Article 9 of the revised Uniform Commercial Code, a debtor retains an interest in a repossessed vehicle, subject to the creditor's lien, and that the debtor's interest was property of the estate. *See, e.g., In re Robinson*, 285 B.R. 732, 737-39 (Bankr. W.D. Okla. 2002) (pointing to a debtor's state law right of redemption and federal bankruptcy law right to cure the default under § 1322). Other courts have concluded that, until a creditor disposes of the property, the debtor remains the legal and equitable owner, subject only to the creditor's debt collection remedies, and the vehicle is an asset in which the debtor still has a property interest even after default. *See, e.g., In re Sanders*, 291 B.R. 97, 101-02 (Bankr. E.D. Mich 2003) (finding that “repossession is merely a device to collect on the creditor's claim, and that therefore repossession does not transfer ownership to the creditor”); *In re Coleman*, 229 B.R. at 431 (finding that, until property seized prepetition is sold, it remains property of the estate and is subject to turnover); *In re Spears*, 223 B.R. at 165 (same). Courts also have determined that the debtor's statutory right of redemption is sufficient to bring the repossessed property into the estate. *See, e.g., National City Bank v. Elliott (In re Elliott)*, 214 B.R. 148, 151-52 (6th Cir. B.A.P. 1997).

The Eleventh Circuit, however, has concluded that a debtor's interest in a repossessed vehicle does not constitute "property of the estate," under the statutes of Florida and Alabama, and that the ownership of the collateral passes to the creditors upon repossession. See *Bell-Tel Federal Credit Union v. Kalter (In re Kalter)*, 292 F.3d 1350, 1360 (11th Cir. 2002) (holding that a vehicle repossessed prepetition does not qualify as property of the debtor's estate under Florida law); *Lewis v. Charles R. Hall Motors, Inc. (In re Lewis)*, 137 F.3d 1280, 1285 (11th Cir. 1998) (holding that, under Alabama law, when a debtor defaults, title and right of possession pass to the creditor, and the debtor's "bare right of redemption" did not qualify the automobile as property of the debtor's estate). But see *Greene v. The Associates (In re Greene)*, 248 B.R. 583 (Bankr. N.D. Ala 2000) (finding that the *Lewis* decision was improperly decided and that the vehicle repossessed prepetition but not sold when bankruptcy was filed was property of the debtor's estate); *In re Coleman*, 229 B.R. at 431 (declining to follow *Lewis*).

The Indiana bankruptcy courts have not previously considered whether a motor vehicle repossessed prepetition qualifies as estate property when a debtor later files bankruptcy. However, the court has determined that, in Indiana, an Internal Revenue Service levy notice issued prepetition constituted property of the debtor's estate. See *Gouveia v. Internal Revenue Service (In re Quality Health Care)*, 215 B.R. 543, 568 (Bankr. N.D. Ind. 1997) (finding that "a prepetition Notice of Levy by the IRS of a debtor's bank account is analogous to a prepetition repossession of tangible property, and that the bank account remains property of the debtor's estate subject to turnover"). It is only a small step from that determination to our finding that the Mazda, seized prepetition, remains property of the debtor's estate subject to turnover.

This court finds that the Illinois bankruptcy decisions present a reasoned approach to this issue by interpreting the language of the Supreme Court in *Whiting Pools*. In addition, *Spears* and other courts analyzing the revised U.C.C. soundly determined that there is sufficient interest in the repossessed property to allow the debtor to claim it as property of the estate. Under the revised UCC adopted in most states, a debtor's interest in a repossessed vehicle is the right to redeem the vehicle. Although, on default, a secured party has the right to

take possession of the collateral and to dispose of it, at any time before the collateral is sold the debtor may redeem it by tendering fulfillment of all the obligations to the secured party, including its expenses. *See Automotive Finance Corp. v. Smart Auto Center, Inc.*, 334 F.3d 685, 689 (7th Cir. 2003) (finding that the debtor never tendered payment in full in order to redeem the collateral, under Ind. Code § 26-1-9.1-623, and thus that the creditor was not required to release the vehicles); *Spears*, 223 B.R. at 163 n.3. This court therefore determines that a vehicle repossessed prepetition is analogous to a prepetition Notice of Levy by the IRS and qualifies as property of the estate under the laws of Indiana.⁴

The court next considers whether the creditor violated the automatic stay by refusing to turn over possession of the Mazda immediately upon the filing of the bankruptcy petition or upon the debtors' informal demand. The Illinois bankruptcy courts in the Northern District of Illinois surveyed the two lines of authority on the question and concluded that "a creditor need not turn over its collateral until adequate protection has been provided." *See In re Spears*, 223 B.R. at 166.

Thus, a creditor that repossesses estate property pre-petition is under no obligation to return the property post-petition until and unless adequate protection is provided. "Since the purpose of the automatic stay is to maintain the status quo that existed on the date of a debtor's bankruptcy filing, the creditor should not have to turnover the vehicle absent assurance that its pre-petition position will be protected." *Spears*, 223 B.R. at 166.

⁴ The court also finds that the repossession prior to the bankruptcy filing was lawful. The contract between the debtors and the credit union contains repossession and non-waiver clauses. *See* R. 13, Ex. B. Under Indiana law, a secured party has the right to demand strict compliance and to repossess the collateral without notice when the debtors fail to comply with the terms of the contract. *See Van Bibber v. Norris*, 419 N.E.2d 115, 122 (Ind. 1981). Under Indiana's Uniform Commercial Code ("UCC"), when a vehicle is collateral for a loan that is in default, the secured party lawfully may exercise its right to take possession of the collateral without judicial process as long as there is no breach of the peace. *See* Ind. Code § 26-1-9.1-609 (which follows former section 9-503); *see also Van Bibber*, 419 N.E.2d at 122 (stating that the purpose of Indiana Code § 26-1-9-503 is best served when creditors require strict compliance with the contract). The debtors do not dispute that they were in default on the loans; indeed, they do not challenge the repossession. They do not suggest that the defendant breached the peace when it took the vehicle. Nor have they invoked their right to redeem the collateral. Under Indiana law, they could redeem their vehicle by tendering the full amount due. *See* Ind. Code § 26-1-9.1-623; *Automotive Finance Corp.*, 334 F.3d at 689. Offering to enter into a new loan agreement or to promise to perform an existing promise falls short of "tendering payment." *See id.* Since the debtors in this case were in default on the loan and did not reaffirm the debt or tender full payment, the defendant credit union had the right under Indiana law to repossess the vehicle.

In re Coleman, 229 B.R. at 432. Moreover, the *Spears* ruling noted that the courts have found that the automatic stay, specifically § 362(a)(3),⁵ “reaches only postpetition affirmative actions to take control of a debtor’s property” and that the “passive act of continuing to possess property does not fall within the prohibition under § 362(h).” *In re Spears*, 223 B.R. at 166.

Judge Lindquist, then Chief Judge of the United States Bankruptcy Court for the Northern District of Indiana, definitively found that a creditor had no duty to turn over the collateral simply upon the demand of the debtors. See *Gouveia v. Internal Revenue Service (In re Quality Health Care)*, 215 B.R. 543, 573-80 (Bankr. N.D. Ind. 1997) (rejecting the holding of *Knaus v. Concordia Lumber Company, Inc. (In re Knaus)*, 889 F.2d 773 (8th Cir. 1989), which held that the duty to turn over property of the estate arises upon the filing of the bankruptcy petition). Although the creditor “had a duty to not commit any affirmative, postpetition act that would disturb the *status quo* as of the petition date,” there was no stay violation in not volunteering to relinquish possession or to waive any of its rights. Once property is found to be property of the estate pursuant to § 541(a), then the turnover provision of § 542, by its express reference to § 363, requires that the Trustee or debtor first must provide adequate protection “before a secured creditor is required to turn over property of the Debtor’s estate.” *Id.* at 581.

This court follows the sound reasoning in *Quality Health Care*, which determined that the automatic stay, precisely § 362(a)(3), does not require that creditors immediately turn over possession of property seized prepetition and thus waive their right to assert defenses to turnover under § 542 until after the turnover. See 215 B.R. at 573-79 (concluding that the IRS’s refusal to turn over to the Trustee bank account proceeds does not necessarily constitute a violation of the automatic stay). In the case before this court, the creditor repossessed the Mazda and held it, without disposing of it, for five months before returning it to the debtors. See *In Re Richardson*, 135 B.R. 256, 259 (Bankr. E.D. Tex. 1992) (finding that, “[i]n maintaining the seized property in

⁵ 11 U.S.C. § 362(a)(3) operates as a stay of “any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate.”

the status it enjoyed just before the filing of the debtor's petition, a creditor is merely complying with the spirit of the § 362 freeze"). The court therefore finds that the creditor did not violate the automatic stay by refusing to surrender the plaintiffs' vehicle to them at the commencement of the case. In the view of this court, the creditor was entitled to hold onto the property during the pendency of the § 542 turnover action until the adequate protection question was resolved.

Having found that the creditor's conduct did not violate the automatic stay, the court further finds that no damages are warranted in this matter. *See, e.g., In re Spears*, 223 B.R. at 167 (concluding that the stay was not violated and thus the motion for sanctions was denied); *see also In re Young*, 193 B.R. 620 (Bankr. D.C. 1996) (concluding that no sanction should be placed on creditor for retaining possession of debtor's vehicle pending resolution of adequate protection).

Conclusion

For the reasons set forth in this Memorandum of Decision, the court finds that the 1998 Mazda 626 automobile repossessed by the defendant Five Star Credit Union six days before the plaintiffs, James Ray Dalton and Linda D. Dalton, filed their chapter 13 bankruptcy petition, qualifies as property of the debtors' estate pursuant to 11 U.S.C. § 541(a). However, the court also finds that the defendant was not required to turn over possession of the vehicle to the plaintiffs under 11 U.S.C. § 542 until adequate protection was provided. The defendant having turned over the vehicle to the plaintiffs, the court further determines that the creditor's conduct did not violate the automatic stay and did not warrant the imposition of damages under 11 U.S.C. § 362(h).

The plaintiffs' Complaint for Turnover of Automobile is granted in part and denied in part. The defendant's Motion to Dismiss Adversary Proceeding is denied. The defendant's Motion for Summary Judgment is denied.

SO ORDERED.

Handwritten signature of Harry C. Dees, Jr. in black ink, with the initials JS01 written in the bottom right corner of the signature.

HARRY C. DEES, JR., CHIEF JUDGE
UNITED STATES BANKRUPTCY COURT