UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
WINSTON-SALEM DIVISION

IN RE:	)	
	)	
WALTER GRAY MILLER and	)	**Case No. 99-81339**
DONNA APPLE MILLER,	)	
	)	
Debtors.	)	
	)	

ORDER

THIS MATTER came on before the undersigned bankruptcy judge in Durham, North Carolina on March 26, 2002 upon motion by the Debtors to modify their plan, to surrender any interest in a 1998 Chevrolet 1500 Van and 1999 Freightliner, have the balance of the claims reclassified as unsecured claims, and to sell real property located at 915 Split Rail Lane, Hillsborough, N.C. and 3033 Cucumber Branch, Snow Camp, N.C. Counsel for the creditors holding liens on the 1998 Chevrolet 1500 Van and 1999 Freightliner objected to the proposed modifications. Having reviewed the file and considered the arguments of counsel and the testimony of witnesses, the Court makes the following findings of fact and conclusions of law:

FACTS

Walter Gray Miller and Donna Apple Miller (the "Debtors") filed this case under Chapter 13 of the Bankruptcy Code on June 18, 1999. The Debtors operate a small trucking business as a sole proprietorship. In December 1998, the Debtors entered into a security agreement with Associates Commercial Corp. ("Associates") to purchase a 1999 Freightliner FL 70. At the time the petition was filed, Associates was owed $69,320.79 plus costs and attorney fees. The Debtors' plan proposed that Associates have a secured claim in the amount of $44,000.00 with the balance of the claim treated as unsecured. Associates filed an objection to confirmation contending

that the vehicle had a value of $75,950.00 and that the plan should not be confirmed under 11 U.S.C. § 1325. Associates argued that the plan would not adequately protect its rights since the vehicle would depreciate more quickly than payments were being made. Subsequently, a consent agreement was reached fixing the value of the 1999 Freightliner at $68,500.00.

The plan was confirmed on October 19, 1999. The plan provided Associates with a secured claim in the amount of $68,500.00 based upon the value of its collateral, the 1999 Freightliner. The plan also provided for payment of a secured claim of GMAC Collection Service Center ("GMAC") in the amount of $12,735.00 based upon the value of its collateral, a 1998 Chevrolet Van 1500. No fixed payment was set forth in the plan to Associates or GMAC but the plan required the Debtors to pay the sum of $6,635.00 to the Trustee for a total of 36 monthly payments or until such time as the Debtors had paid into the Chapter 13 Trustee enough money to pay unsecured creditors a dividend of 25%.

In May 2001, the Debtors filed a motion to modify the plan to reduce the plan payments from $6,635.00 per month to $5,541.00 per month and to reduce the dividend to unsecured creditors from 25% to 10%. To facilitate the proposed modification, the Debtors requested to surrender a 1998 Freightliner upon which Mercedes-Benz Credit Corp. ("Mercedes-Benz") held a valid lien. At the time of the filing of the petition, the 1998 Freightliner had a fair market value of $42,000.00. At the time of the Debtors' motion to modify, the Freightliner had a value of $30,938.00, having depreciated in the amount of $11,062.00. Since the filing of the Debtors' petition, the creditor had been paid through the Chapter 13 plan approximately $18,828.54, exceeding depreciation in the amount of $7,766.54. No creditor objected to the proposed modification and the modification was based upon the inability to keep drivers and routes for all the trucks due to the unexpected and dramatic increase in gasoline and other expenses. The plan

modification was allowed and Mercedes Benz was granted 120 days to file a deficiency claim.

On January 18, 2002, the Debtors filed a second motion to modify the plan and requested that the plan payments be reduced and that the dividend to unsecured creditors be reduced from 10% to 1%. The Honorable James B. Wolfe, Jr. entered an order denying the second modification on March 4, 2002. On February 27, 2002, the Debtors filed a third motion to modify, which is the motion presently before the Court. The Debtors request that their plan payments be reduced from $5,534.00 per month to $3,346.00 per month. They do not request that the dividend to unsecured creditors be reduced.

Since confirmation of the plan, the Debtors have paid the sum of approximately $185,000.00 into their Chapter 13 plan. Recently, they have experienced a number of difficulties. The Debtors had employed their son to drive a second tractor trailer, but he has been required to stop driving by the Department of Transportation due to health problems. The Debtors have been unable to find a replacement driver and, as a result, have lost the income produced by that second truck. Ms. Miller testified that they spent approximately $16,000.00 in the last six months to replace both the engine and the transmission in the 1999 Freightliner. Finally, the Debtors have become responsible for three grandchildren, who were recently placed in their care. These recent events constitute substantial and unanticipated changes in circumstances.

The Debtors propose to modify their plan such that their payments are reduced to $3,346.00 per month for the remaining life of the plan. To facilitate the proposed modification, the Debtors propose to sell both pieces of real property, and in the event that they have not filed a motion to sell within six months, those properties will be surrendered. The Debtors also request to move their plan payment delinquency in the amount of $11,683.00 to the end of their Chapter 13 plan for payment. Finally, the Debtors wish to surrender any interest that they may have in the vehicles securing the claims of GMAC and Associates. Since the filing of the Debtors' bankruptcy, the value of the 1998 Chevrolet Van has depreciated in the amount of $4,072.50.

During this same time period, the Debtors' plan has paid GMAC approximately $7,443.77. The 1999 Freightliner has depreciated in the amount of $46,550.00, while Associates has been paid approximately $38,785.13. The Debtors wish to reclassify any balances owed on the debts to GMAC and Associates as unsecured.

DISCUSSION

The Court will first consider the issue presented by the requested release of the 1999 Freightliner. This issue is whether the Debtors are entitled to modification of their confirmed plan to surrender collateral that has diminished in value to the secured creditor and to have the balance of the secured claim after liquidation treated as an unsecured claim.

An order confirming a Chapter 13 plan is a final order. Once a plan is confirmed, it is binding on the debtor and creditors. See 11 U.S.C. § 1327. Principles of res judicata bar modification based upon issues that were known and could have been raised prior to confirmation of the debtor's plan. See In re Arnold, 869 F.2d 240 (4th Cir. 1989). Section 1329 permits modification of a confirmed plan for one of the limited purposes enumerated within that section. 11 U.S.C. § 1329 provides as follows:

> (a) At any time after confirmation of the plan but before the completion of payments under such plan, the plan may be modified, upon request of the debtor, the trustee, or the holder of an allowed unsecured claim, to
> (1) increase or reduce the amount of payments on claims of a particular class provided for by the plan;
> (2) extend or reduce the time for such payments; or
> (3) alter the amount of the distribution to a creditor whose claim is provided for by the plan, to the extent necessary to take account of any payment of such claim other than under the plan.
> (b)(1) Sections 1322(a), 1322(b), and 1323(c) of this title and the requirements of section 1325(a) of this title apply to any modification under subsection (a) of this section.
> (2) The plan as modified becomes the plan unless, after notice and a hearing, such modification is disapproved.

11 U.S.C. § 1329(a)-(b). A plan modification permitted under § 1329 may be allowed upon a showing by the debtor of a substantial and unanticipated change in circumstances. See, e.g., In re

James, 260 B.R. 368 (Bankr. E.D.N.C. 2001); In re Butler, 174 B.R. 44 (Bankr. M.D.N.C. 1994). In the Arnold case, the court concluded that "the doctrine of res judicata bars an increase in the amount of monthly payments only where there have been no unanticipated, substantial changes in the debtor's financial situation." Arnold, 869 F.2d at 243. Pursuant to § 1329, a modified plan must have been proposed in good faith as required by § 1325. 11 U.S.C. § 1329(b).

Courts differ on what constitutes an allowable modification under § 1329. While § 1329(a) clearly permits the debtor to modify the timing of payments, or to increase or reduce payments to a particular class, it does not expressly authorize a modification that reclassifies a claim. This type of modification does not fit within the plain meaning of § 1329. A number of courts have held that a debtor cannot modify a plan by surrendering collateral to a secured creditor, having the creditor liquidate the collateral and apply proceeds toward the claim, and having any deficiency reclassified as an unsecured claim. See, e.g., In re Nolan, 232 F.3d 528 (6th Cir. 2000); In re Smith, 259 B.R. 323 (Bankr. S.D. Ill. 2001); In re Coleman, 231 B.R. 397 (Bankr. S.D. Ga. 1999). In Nolan, the Sixth Circuit reasoned that "Section 1329(a)(1) should not be read so broadly as to authorize the reclassification of claims." Id. at 533. The court found that § 1329(a) allowed for a reduction in the payment of claims, but not for a reduction or modification of the claim itself. Id. at 535.

Other courts have held that a plan modification which reclassifies a deficiency as unsecured is permitted under § 1329(a). See, e.g., In re Townley, 256 B.R. 697 (Bankr. D. N.J. 2000); In re Day, 247 B.R. 898 (Bankr. M.D. Ga. 2000); In re Frost, 123 B.R. 254 (S.D. Ohio 1990); In re Conley, 2000 WL 1805324 (Bankr. E.D. Va. 2000). In In re Day, the court reasoned that, "[t]he requirements for postconfirmation modifications, which include a good faith requirement, have the needed protection to ensure that secured claimants are adequately protected." In re Day, 247 B.R. at 903. Furthermore, a creditor may be protected in the event of subsequent modification by objecting to a plan in which the timing and amount of payments do not at least equal the rate of depreciation of the collateral. In re Townley, 256 B.R. at 700.

Some courts have held that while § 1329 standing alone might not authorize reclassification of a secured claim, § 502(j) provides the necessary authorization to reconsider a claim and allow the type of plan modification requested in this case. Section 502(j) provides:

> (j) A claim that has been allowed or disallowed may be reconsidered for cause. A reconsidered claim may be allowed or disallowed according to the equities of the case. Reconsideration of a claim under this subsection does not affect the validity of any payment or transfer from the estate made to a holder of an allowed claim on account of such allowed claim that is not reconsidered, but if a reconsidered claim is allowed and is of the same class as such holder's claim, such holder may not receive any additional payment or transfer from the estate on account of such holder's allowed claim until the holder of such reconsidered and allowed claim receives payment on account of such claim proportionate in value to that already received by such other holder. This subsection does not alter or modify the trustee's right to recover from a creditor any excess payment or transfer made to such creditor.

11 U.S.C. § 502(j). In In re Johnson, 247 B.R. 904 (Bankr. S.D. Ga. 1999), the court reasoned that an analysis which focuses solely on § 1329 is misplaced inasmuch as § 502(j) controls the allowance or disallowance of claims and stated that "[a]fter surrender of collateral, the deficiency portion of the claim is no longer actually secured. A claim simply cannot be secured when nothing secures it." Id. at 908. The fact that a debtor has surrendered collateral securing a claim constitutes cause to reconsider the classification of claim. In re Zeider, 263 B.R. 114 (Bankr. D. Ariz. 2001). According to In re Zeider and In re Johnson, a court may consider the equities of the case pursuant to § 502(j) and modify a plan such that the balance of a secured claim following the liquidation of collateral may be reclassified as unsecured. In re Zeider, 263 B.R. at 117; In re Johnson, 247 B.R. at 909.[1]

This Court finds that modifying a plan in order to reclassify a secured claim does not fall within the scope of § 1329(a) standing alone; however, a claim may be reconsidered pursuant to Section § 502(j) for cause. Section 1327 provides the general rule that the plan is binding upon

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[1] In In re Johnson, the court allowed the reclassification of a deficiency as unsecured claim, however it recognized that the very existence of that deficiency was evidence that the secured creditor was not adequately protected by the plan. The court held that the secured creditor was entitled to an administrative claim based on this failure of adequate protection. In re Johnson, 247 B.R. at 910.

confirmation, while Section § 1329(a) provides limited exceptions to this rule. Section 1329(a) specifically enumerates the three purposes for which a plan may be modified, but does not include among those the type of modification requested in this case. Given the binding nature of confirmation, a secured creditor cannot move to modify the plan if the value of the collateral appreciates. The Court is not persuaded that Congress intended to allow a debtor to use § 1329 to essentially revalue collateral that has depreciated while the debtor had the benefit of possession of that collateral, leaving the creditor with an unsecured claim. Furthermore, a debtor in this situation has other options, if necessary. A debtor can convert to Chapter 7, or dismiss the case and refile after the collateral has been repossessed by the creditor. The Court is unwilling to stretch the plain meaning of § 1329(a) under these circumstances.

Nevertheless, the secured claim of Associates may be reconsidered pursuant to Section § 502(j) for cause. "Cause" is not a defined term within the Bankruptcy Code. Courts have used a variety of standards and have considerable discretion in deciding what constitutes cause; however, "this does not provide for automatic reconsideration of every claim, nor does it make confirmation of a plan 'nonfinal' for res judicata purposes." In re Snow, 270 B.R. 38, 41 (D. Md. 2001). Some bankruptcy courts use the standard of Fed. R. Civ. P. 60(b). Id.; See also In re Coffman, 271 B.R. 492,498 (Bankr. N.D. Texas 2002); In re A.H. Robbins Co., 1998 W.L. 480744 (4th Cir. 1998). Rule 60(b) lists the following reasons for reconsideration: (1) mistake, inadvertence, surprise, or excusable neglect; (2) newly discovered evidence; (3) fraud, misrepresentation, or other misconduct of an adverse party; (4) the judgment is void; (5) the judgment has been satisfied, released, or discharged, or it is no longer equitable that the judgment should have prospective application; or (6) any other reason justifying relief from the operation of the judgment. Fed. R. Civ. P. 60(b). In addition to a finding of cause, Section 502(j) further requires that the equities of this case support reconsideration of the claim at issue. Thus, in order to accomplish both the modification of the plan and the reclassification of Associates claim, the Debtors' circumstances

must satisfy both the good faith requirement of § 1329 and the equitable requirement of § 502(j).

In cases in which a debtor has requested modification pursuant to § 1329, it is clear that a debtor who had abused or neglected collateral causing excessive depreciation between confirmation and the proposed modification is not entitled to shift the burden of that depreciation to the creditor. In re Butler, 174 B.R. at 48. The Court is unable to discern from the record before it why this vehicle depreciated as rapidly as it did, but as the movants, the Debtors "have the burden of proving that the proposed modification meets all of these requirements, including the good faith requirement of § 1325(a)." Id. At the hearing on this matter, Ms. Miller testified that the 1999 Freightliner was in excellent condition and had been well maintained. Within the past year, the Debtors have replaced both the engine and the transmission, at a cost of approximately $16,000.00. The Court does not find that the depreciation of the 1999 Freightliner was a result of abuse or neglect by the Debtors. The Court finds that the Debtors have proposed the modifications in good faith and the equities of the case justify reconsideration of the claim. Associates will be permitted to liquidate the collateral. After Associates forecloses, it has no collateral and the balance of the claim will be allowed as a general unsecured claim.

To modify a confirmed plan such that a secured claim is reclassified as an unsecured claim subsequent to the surrender of the collateral shifts the burden of depreciation to the creditor. Despite the Debtors' efforts to maintain the vehicle, the 1999 Freightliner has suffered a huge loss in its value. It has depreciated in the amount of $46,550.00 during a time period when Associates has been paid only $38,785.13. Almost as if in anticipation of the Debtors' requested modification, Associates made every effort to ensure that it was adequately protected by objecting to confirmation of the plan on the basis that the proposed plan did not adequately protect its interest in the vehicle because the vehicle would depreciate more quickly than payments were being made. The value of the 1999 Freightliner was ultimately set below the amount requested by Associates in their objection.

At the time the Debtors filed their bankruptcy petition, Associates' claim was secured by a vehicle with a value of $68,500.00. The Debtors made the conscious decision to retain the vehicle as provided under § 1325(a)(5) and, in return, Associates received a secured claim in the amount of the value of the vehicle at that time. During the course of the plan, Associates was paid $38,785.13 and the parties agree that the vehicle depreciated in the amount of $46,550.00 ($68,500.00 - $21,950.00). The plan did not adequately protect Associates, therefore, it is entitled to an administrative expense claim caused by this failure of adequate protection in the amount of $7,764.87 ($46,550.00 - $38,785.13) pursuant to §507(b).

In the Fourth Circuit a debtor is permitted to modify the order confirming the plan if the debtor has acted in good faith and the circumstances warranting a modification were the result of substantial unanticipated changes. When both tests are met, the plan is not res judicata as to the rights of creditors. Courts are split as to whether a past confirmation plan modification may provide for the release of collateral and the reclassification of any deficiency as an unsecured claim. The one circuit decision is In re Nolan, in which the Sixth Circuit did not permit the reclassification of the claim after confirmation. However, in Nolan the court did not address § 502(j), which permits a claim that has been allowed or disallowed to be reconsidered for cause. A reconsidered claim may be allowed or disallowed according to the equities of the case.

In the matter before the court, the Debtors have acted in good faith and have experienced substantial unanticipated changes in their circumstances. Their son can no longer drive one of the trucks due to unforeseen health reasons. Despite good faith efforts, they have been unable to locate another driver and they now have the responsibility for three grandchildren. These events constitute cause to reconsider the Associate's claim. The Associates claim will be reconsidered according to the equities of the case. Associates objected to confirmation by objecting to the proposed valuation of its collateral and contending that the vehicle would depreciate at a faster rate than the proposed payments. The parties agreed upon a value for the collateral, but

Associates was correct in that the vehicle has depreciated faster than the monthly payments proposed under the plan. The Debtors are also behind by more than $11,000.00 in plan payments.

The payments proposed under the Chapter 13 Plan did not adequately protect the interest of Associates. The Debtors proposed a stream of payments under the Chapter 13 plan that proved to be inadequate. "Section 11 U.S.C. 507(b) provides that to the extent adequate protection of the interest of a holder of a claim proves to be inadequate, then the creditor's claim is given priority over allowable claims entitled to distribution under § 507(a)." Grundy National Bank v. Rife, 896 F.2d 361, 363 (4th Cir. 1989); See also, In re Cheatham, 91 B.R. 382 (E.D.N.C. 1988); In re Johnson, 247 B.R. at 904 (administrative expenses allowed for depreciation).

A specific monthly payment was not set forth in the plan for Associates. Associates has been paid $38,785.13 and the vehicle has depreciated at a faster rate. Other creditors, specifically Mercedes Benz and GMAC, were paid at a rate faster than the depreciation of their collateral. While the 1999 Freightliner was depreciating, the Debtors were using it to produce income for their business which funded the Chapter 13 plan. The Debtors' allocation of payments under this plan failed to adequately protect Associates for the continued use of the vehicle.

Therefore, based on the equities of the case the claim of Associates will be reconsidered and Associates will be allowed an administrative claim under 11 U.S.C. § 507 in the amount of $7,764.87 for the failure of adequate protection. The Debtors are authorized to release the vehicle and after the application of the sales proceeds, the balance of the claim shall be allowed as a general unsecured claim.

Finally, as to the Debtors' request to modify their plan to release the 1998 Chevrolet Van, the Court finds that this proposal is not in the best interest of the estate. The van has an approximate value of $8,662.50 and there remains a principal balance due to GMAC of $6,814.21

on its secured claim. Thus, there appears to be equity in the vehicle which will be entirely lost if it is released to the creditor. Furthermore, it is possible that if the creditor were to sell the vehicle at auction, the proceeds would not even be sufficient to satisfy the secured claim, resulting in another deficiency claim. In order to maximize the equity in the property, the Court will permit the Debtors to privately sell the vehicle and remit the proceeds to the Office of Chapter 13 Trustee. In the event that the sale does not generate sufficient monies to pay the creditor in full, then the balance of the claim will be allowed as a general unsecured claim. GMAC has consented to this proposed modification.

CONCLUSION

For the foregoing reasons, IT IS ORDERED, ADJUDGED AND DECREED that the Debtors' motion to modify the Chapter 13 plan is allowed and the Debtors are authorized to sell the 1998 Chevrolet Van and may surrender the 1999 Freightliner and reclassify the deficiency of Associates' claim as unsecured. Associates will be allowed an administrative claim in the amount of $7,764.87.

This the 19 day of April 2002.

CATHARINE R. CARRUTHERS

Catharine R. Carruthers
United States Bankruptcy Judge