

UNITED STATES BANKRUPTCY COURT
DISTRICT OF VERMONT



In re:

**Judy B. & David R. Stevens,
Debtors.**

**Chapter 13 Case
01-10401**

**Judy B. & David R. Stevens,
Plaintiffs,**

v.

**Adversary Proceeding
03-1054**

**Town of Bennington, Vt.,
Defendant.**

Appearances: *Kerry G. Spradlin, Esq.*
 Rutland, VT
 Attorney for the Debtors-Plaintiffs

Jennifer Emens-Butler, Esq.
Obuchowski & Emens-Butler, P.C.
Bethel, VT
Attorney for the Defendant

MEMORANDUM OF DECISION
GRANTING THE DEFENDANT’S MOTION TO DISMISS

Plaintiffs Judy B. Stevens and David R. Stevens have filed an adversary proceeding under 11 U.S.C. § 505 and Rule 3012 of the Federal Rules of Bankruptcy Procedure¹ for an order determining the value of the secured claim held by the Defendant, the Town of Bennington (“the Town”), for delinquent property taxes, interest, and penalties. The gravamen of the Debtors’ Complaint is that the payments they have made under the Plan to date have fully satisfied any unpaid taxes; that the remainder due on the Town’s secured claim in the Plan is attributable to interest, late fees, and penalties that they are not obligated to pay; and therefore, that the Court should reduce the Town’s allowed secured claim accordingly. The Debtors’ second cause of action seeks leave to amend the Chapter 13 Plan to reflect the Town’s reduced secured claim amount and to terminate the Debtors’ payment obligation on the Town’s secured claim. The Debtors’ third cause of action seeks an order directing the Chapter 13 Trustee to escrow payments currently allocated to the Town’s secured claim so that these funds can ultimately be paid to holders of unsecured claims.

¹ All references to statutes are to Title 11 of the United States Code (“the Bankruptcy Code”) and all references to rules are to the Federal Rules of Bankruptcy Procedure (“the Bankruptcy Rules”), unless otherwise indicated.

Presently before the Court is the Town's Motion to Dismiss for failure to state a claim upon which relief can be granted under Bankruptcy Rule 7012 and Federal Rule of Civil Procedure 12(b)(6) See doc. #7. In support of this motion, the Town argues that *res judicata* bars the Debtors from relitigating matters this Court decided in the order confirming the Debtors' Amended Plan.

After considering the parties' papers, the evidence presented, and relevant law, the Court finds it appropriate to grant the Town's Motion to Dismiss. Specifically, it finds that *res judicata* bars the Debtors from challenging the Town's claim when they had the opportunity to do so prior to the entry of the order confirming their Amended Plan and did not do so.

This Court has jurisdiction over this core proceeding under 28 U.S.C. §§ 1334 and 157(b)(2)(K).

I. BACKGROUND²

The Debtors own their home, which is located at 1279 Houghton Lane in Bennington, Vermont ("the Property"). The grand list value of the Property is \$63,800. On March 27, 2001, the Debtors filed for relief under chapter 13 of the Bankruptcy Code, and, on April 11, 2001, the Debtors filed a Chapter 13 Plan. In their Summary of Schedules the Debtors listed the Property as having a value of \$85,200; claimed \$42,800 was exempt; and listed secured claims of \$40,966.15, priority unsecured claims of \$1,801.54, and general unsecured claims of \$21,727.58.

On May 15, 2001, the Trustee objected to the Debtors' proposed plan, asserting that it failed to provide for the full satisfaction of property taxes which encumber the Property, and that the Debtors had improperly listed the property taxes as a general unsecured claim rather than as a secured claim. In response, on May 17, 2001, the Debtors filed an amended plan and amended schedules, but the amended summary of schedules listed \$17,769.32 in tax debt as a priority unsecured claim, rather than a secured claim.³

At the confirmation hearing held on June 12, 2001, the Debtors and the Trustee agreed on the record, *inter alia*, that the Town's tax claim was a secured claim.⁴ This resolved the Trustee's objection to confirmation, and the Debtors' amended plan ("the Amended Plan") was confirmed. Thereafter, the Court entered a Corrected Findings and Order Confirming Amended Chapter 13 Plan, which listed the Town's tax

² The Court gleaned the following history from the record in the Debtors' chapter 13 case, their confirmed Plan, and the facts admitted by both parties in this adversary proceeding.

³ The amended Schedule E itemized property taxes totaling \$1,801.54 for the period of July 1, 2000, through June 30, 2001, and \$15,967.58 for the period of 1996 through 2000.

⁴ The Debtors also made an oral motion to extend the life of their amended plan to 60 months, and that oral motion was granted.

claim of \$17,769.32 under the headings “SECURED CREDITORS” and “TOTAL PAYMENTS TO SECURED CLAIMS.”⁵ Importantly, the Debtors’ attorney approved this “Corrected” Confirmation Order prior to its entry. The confirmed Amended Plan calls for payments of \$400 for two months and \$465.53 per month for the remaining 58 months, for a total payments of \$27,800.74.

In June 2003, the Town notified the Debtors that the delinquent pre-petition property taxes due for 2000 and 2001 were part of the \$17,769.32 secured claim included in the Debtors’ Amended Plan. At the same time, the Town also gave the Debtors notice of delinquent post-confirmation taxes for 2001 and 2003.⁶ The Debtors contend the Town was late in providing such notice and speculates that the reason for the Town’s failure to give timely notice was that the Town erroneously believed the Debtors were still involved in an earlier chapter 13 case (case # 95-10908), in which the Debtors received their discharge on August 30, 2000. The Town concedes that it did not give notice to the Debtors in the usual course, for fear of violating the automatic stay, but insists that this was reasonable conduct on their part and caused no harm to the Debtors.

The Town has not filed a proof of claim in this case. As of January 14, 2004, the Trustee has disbursed \$11,741.58 to the Town pursuant to the confirmed Amended Plan in this case, leaving a balance due of \$6,027.74.

II. ISSUES PRESENTED

The Debtors’ position is that they should not be required to pay any amount of interest, late charges, or penalties on the tax obligation they owe to the Town under their Amended Plan, notwithstanding that the order confirming the Amended Plan identified all components of the tax obligation as a secured claim and provided for it to be paid in full. They contend that they now realize that the payments they have made pursuant to their Amended Plan have satisfied the debt principal, and therefore, that they should be permitted to modify their Amended Plan to reduce the amount of the Town’s secured claim. The Debtors’ Complaint seeks an order allowing them to redetermine the amount and classification of their tax debt to the Town, to modify their Amended Plan, and to direct the Trustee to hold Amended Plan payments in escrow for the benefit of the priority and general unsecured creditors until further order by this Court.

⁵ The labeling of the Confirmation Order as “Corrected” is a misnomer. There was no prior confirmation order entered. Rather, the “correction” captured in the Corrected Confirmation Order appears to have been included by the Trustee to reflect the re-categorization of the Town’s claim as a secured claim.

⁶ Neither party to this proceeding has specified the amounts of the alleged 2001 and 2003 post-confirmation tax delinquencies. However, these alleged delinquencies are not before the Court for consideration and are referenced for informational purposes only.

In response to the Complaint, the Town filed a Motion to Dismiss for failure to state a cause of action upon which relief can be granted, under FED. R. CIV. P. 12(b)(6) and Bankruptcy Rule 7012. The Town argues that *res judicata* bars the Debtors from reopening their confirmed Amended Plan and modifying the treatment of the Town's claim, which the Debtors voluntarily designated as fully secured. The Town also argues that, since it holds a first priority secured lien on the Property, and since the Property's fair market value exceeds the Town's lien against it, the Town is entitled to interest on its claim. In support of this argument, the Town asks the Court to take judicial notice of the Debtors' valuation of the Property in their amended schedules. The Town also argues that the Debtors' allegations regarding notice deficiencies are without merit because the pre-petition delinquent taxes were included in the Debtors' confirmed Amended Plan as a secured claim, and the Town gave the Debtors actual notice of the post-confirmation taxes due.

III. DISCUSSION

A. The Bankruptcy Rule 7012 Standard

Pursuant to Bankruptcy Rule 7012, this Court must view the facts relevant to the Town's Motion to Dismiss in the light most favorable to the Debtors. "In weighing a motion to dismiss, a Court will accept as true the facts as pled by the non-moving party." In re Peterson, 93 B.R. 323, 324 (Bankr. D. Vt. 1988) (citing Fine v. New York, 529 F.2d 70 (2d Cir.1975)). This is especially appropriate here where the Town has admitted the Debtors' factual assertions.⁷ This Court will rely on the facts set forth in the Debtor's schedules, amended schedules and Amended Plan, all of which were filed under penalty of perjury and relied upon at the confirmation hearing. Therefore, the Town's request for judicial notice of the same is denied as moot.

B. Res Judicata and Confirmed Chapter 13 Plans

The first issue before this Court is whether the doctrine of *res judicata*, also known as claim preclusion, bars the Debtors from relitigating the amount, nature, and priority of the Town's tax claim. This Court has previously analyzed the intersection of *res judicata* with chapter 13 plans. The Bankruptcy Code provides the starting point for this analysis: "The provisions of a confirmed plan bind the debtor and each creditor, whether or not the claim of such creditor is provided for by the plan, and whether or not such creditor has objected to, has accepted, or has rejected the plan." § 1327(a). "Under § 1327, a confirmation order is *res judicata* as to all issues which were decided, or could have been decided, at the hearing on confirmation."

⁷ The sole exception being that the Town disputes the Debtors' allegation that the Town's notice regarding delinquent taxes was not sufficient. However, the Court finds this contested point to be immaterial to the issues presented.

In re Whelton, 299 B.R. 306, 314 (Bankr. D. Vt. 2003). This Court has consistently held that *res judicata* bars the reopening of claims that this Court has or could have decided at a chapter 13 confirmation hearing. See id.; In re Crowley, 258 B.R. 587, 591 (Bankr. D. Vt. 2000). The Second Circuit has ruled that “The doctrine of *res judicata*, or claim preclusion, holds that ‘a final judgment on the merits of an action precludes the parties or their privies from relitigating issues that were or could have been raised in that action.’” Monahan v. New York City Dep’t of Corrections, 214 F.3d 275, 284 (2d Cir. 2000) (quoting Allen v. McCurry, 449 U.S. 90, 94 (1980)). The majority of courts will apply *res judicata* to bar subsequent challenges to a plan “as to all provisions in the underlying chapter 13 plan, even if contrary to the Bankruptcy Code.” In re Whelton, 299 B.R. at 313 (citing Andersen v. UNIPAC-NEBHELP, 179 F.3d 1253, 1259 (10th Cir.1999); Great Lakes Higher Educ. Corp. v. Pardee, 193 F.3d 1083, 1086 (9th Cir.1999); In re Szostek, 886 F.2d 1405 (3rd Cir. 1989)).

The Debtors’ argument that they should not pay any amount of interest, penalty, or other costs above and beyond the original amount of their tax liability, is founded on the premise that the Bankruptcy Code does not permit such relief to a creditor. I disagree. There is no question that oversecured creditors are entitled to collect interest as a part of their secured claim. See § 506(a); United States v. Ron Pair Enter., Inc., 489 U.S. 235, 241 (1989) (“Recovery of post-petition interest is unqualified..”). However, a creditor’s right to collect penalties and other costs is not so straightforward. Both the Second Circuit and the Supreme Court have ruled that a creditor holding an oversecured, non-consensual lien may claim interest, but may not claim penalties or other costs as part of its secured claim since the non-consensual lien does not have an underlying agreement that provides for the reimbursement of those expenses. See In re Parr Meadows Racing Ass’n, Inc., 880 F.2d 1540, 1549 (2d Cir. 1989)(“In the absence of such an agreement, fees and costs are not recoverable.”); Ron Pair, 489 U.S. at 241 (“Recovery of fees, costs, and charges, however, is allowed only if they are reasonable *and provided for in the agreement under which the claim arose.*” (emphasis added)). Thus, while the Debtors’ Complaint appears to raise a valid point regarding the appropriateness of allowing the subject penalties and other costs as part of the Town’s tax claim, and while this issue may have been a proper subject for dispute and litigation during the confirmation process, neither factor justifies reopening the confirmation order to redetermine the treatment of the Town’s secured claim at this time. The Debtors’ failure to raise the issue during confirmation bars the Debtors from litigating it at this time. See In re Whelton, 299 B.R. at 313 (citing Andersen, 179 F.3d at 1259; Pardee, 193 F.3d at 1086; In re Szostek, 886 F.2d at 1406).

One of the primary purposes of a chapter 13 plan is to conclusively set forth the treatment of claims. See § 1322(a)–(b); see generally In re Loper, 222 B.R. 431, 435 (D. Vt. 1998) (“In Chapter 13 [cases], the debtor is allowed to adjust the amount and the timing of the repayment of his/her indebtedness to secured and

unsecured creditors in a repayment plan. The repayment plan is subject, however, to confirmation by the Bankruptcy Court.”); KEITH M. LUNDIN, CHAPTER 13 BANKRUPTCY, 3d Ed. § 103.1 Here, the Debtors acknowledge that they relied on information they received from the Town’s attorney in determining the amount of property tax to include in their amended schedules and Amended Plan. See Compl. at ¶ 3. Moreover, they included this claim information in their Amended Plan despite the fact that the Town did not file a proof of claim. See id. at ¶¶ 3–4. The Debtors also accepted the Trustee’s classification of the tax obligation as a secured debt in the proposed order of confirmation. The Debtors could have, and in fact should have, litigated any dispute as to the nature, extent, or validity of the Town’s claim at the time of the confirmation hearing. This is particularly true here, where, there had previously been a dispute regarding the appropriate amount of interest to be paid on the Town’s claim. Instead, the Debtors asked the Court to confirm their Amended Plan which treated the entire tax liability as secured.

It is important to point out that the Debtors are challenging a provision of an otherwise valid Amended Plan, and that this is an amended plan which the Debtors themselves proposed, amended, sought to have confirmed, and paid to the extent of two-thirds of the Town’s secured claim. The Debtors did not challenge the Town’s claim at the appropriate time, namely, at the confirmation hearing. The necessary result of this failure to bring their challenge, in a timely fashion, is a settled matter of law. “When an issue of fact or law is actually litigated and determined by a *valid and final* judgment . . . the determination is conclusive. . . .” RESTATEMENT (SECOND) OF JUDGMENTS § 27 (1982) (emphasis added).

In affirming a decision of this Court on a similar question, the Second Circuit affirmed the importance of parties being able to rely on final orders of a court and held a party may reopen an order entered by a Bankruptcy Court “only upon a showing of exceptional circumstances” because “final judgments should not be lightly reopened.” Cent. Vermont Power Corp. v. Herbert, 341 F.3d 186, 190 (2d Cir. 2003) (citation omitted). Here, the Town should be able to rely on the provisions of the Confirmation Order that set forth the treatment of its claim.

Moreover, the instant decision to preclude post-confirmation litigation of a claim that should have been litigated at the confirmation stage of the case is in accord with modern federal practice, which provides that certain issues may only be raised at specific times.⁸

⁸ For example, if a defendant fails to raise such affirmative defenses as “duress, estoppel . . . fraud, [or] illegality,” these are deemed waived. See FED. R. CIV. P. 8(c); see also Saks v. Franklin Covey Co., 316 F.3d 337, 350 (2d Cir. 2003).

In sum, this Court finds that it is barred from redetermining the value of the Town of Bennington's tax claim, the first cause of action stated in the Debtors' § 505 Complaint, based upon the doctrine of *res judicata*. Hence, the Court grants the Town's Motion to Dismiss the Debtor's first cause of action on that basis.

CONCLUSION

Finding that the principle of *res judicata* bars the redetermination of the value of the Town of Bennington's tax claim, the Court dismisses the Debtors' first cause of action. Since the remaining two causes of action articulated in the Debtors' Complaint – the modifying of their Plan and the escrowing of any further Plan payments allocated to the Town – are dependant on a determination that the Debtors may reopen the Confirmation Order and reduce the Town's secured claim, they too must fail. Accordingly, the Town's Motion to Dismiss is granted and the Debtors' Complaint is dismissed in its entirety.

This Memorandum of Decision constitutes the Court's findings of fact and conclusions of law.

March 5, 2004
Rutland, Vermont



Colleen A. Brown
United States Bankruptcy Judge