

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
ROANOKE DIVISION

IN RE: JASON ROBERT ROSE)
SALLY ELIZABETH ROSE,)
Debtors.) CHAPTER 7
)
) CASE NO. 7-04-03490-WSA-7
)

JASON ROBERT ROSE)
SALLY ELIZABETH ROSE,)
Plaintiffs)
)
v.) Adversary Proceeding No. 04-7123
)
PEOPLES LOAN COMPANY,)
Defendant)
)

MEMORANDUM DECISION

This adversary proceeding has been brought by the Debtors to determine the nature and extent of the lien, if any, of Peoples Loan Company in a certain 1994 Geo Tracker automobile which they acquired by means of financing provided by Peoples. This vehicle was purchased on July 16, 2004 but no security interest was ever noted on the certificate of title prior to the bankruptcy case filing on August 24, 2004. According to the account given by counsel to the Court when this adversary proceeding came on to be heard at a pre-trial conference on December 22, 2004, Peoples entrusted the lien documentation to the Roses to take to the Virginia Division of Motor Vehicles to note the security interest of the certificate of title but they did not get around to fulfilling this responsibility before they filed their petition. Neither the vehicle nor the debt to Peoples was listed in the original schedules to the Debtors' petition. The meeting of

creditors pursuant to section 341 of the Bankruptcy Code was held on September 28, 2004 and the Chapter 7 Trustee immediately filed a “no asset” report. The Debtors then filed amended schedules listing the Geo Tracker in Schedule B and claiming it as exempt in Schedule C and adding Peoples as a creditor in their case. Peoples has not responded to the notification that it was added as a creditor in the case and has not responded to the complaint in this adversary proceeding. No party in interest has filed any objection to the Debtors’ claim of exemption of the Tracker. The Debtors seek here entry of a default order directing Peoples “to void or extinguish any lien claimed” by it in the vehicle. The amended schedules do not list Peoples as having any security interest in the Tracker or show any connection between the ownership of the vehicle and the debt to Peoples. A review of the case file does not disclose whether the Trustee was advised of the apparent pre-petition grant by the Debtors of a security interest in the Tracker to Peoples in connection with the purchase money financing it provided.

CONCLUSIONS OF LAW

This Court has jurisdiction of the Debtors’ bankruptcy case by virtue of the provisions of 28 U.S.C. §§ 1334(a) and 157(a) and the delegation made to this Court by Order from the District Court on July 24, 1984. 28 U.S.C. § 157(b)(1) provides that bankruptcy judges, when the District Court has referred bankruptcy cases to them pursuant to 28 U.S.C. § 157(a), which the District Court for this District has done as referenced in the preceding sentence, “may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11, and may enter appropriate orders and judgments, subject to review under section 158 of this title.” The jurisdiction of a bankruptcy court to hear and determine any particular matter involving a bankruptcy debtor is of course derivative of the

jurisdiction accorded to the district courts by 28 U.S.C. § 1334(a) and (b) of “all cases under title 11” and “all civil proceedings arising under title 11, or arising in or related to cases under title 11.”

The fact that a bankruptcy debtor has some type of legal dispute with a third party does not automatically mean that the bankruptcy court has jurisdiction to determine that particular dispute. The status of Peoples’s security interest in the Tracker vis-a-vis the Debtors’ claim of exemption of such vehicle does not involve a claim against property which the bankruptcy trustee seeks to administer for the benefit of the Debtor’s creditors. Neither does it involve any issue as to the dischargeability of the Roses’ debt to Peoples. The latter has filed a complaint initiating a separate adversary proceeding (No. 04-07133) seeking to determine the dischargeability of such debt. Under section 522(a) and (l) of title 11, the Debtor’s unobjected to claim of exemption results in the claimed property being “exempt” from the bankruptcy estate.

There is a question whether an adversary proceeding to determine the nature and extent of liens against exempt property which does not involve rights created under the Bankruptcy Code is within the Court’s jurisdiction of the bankruptcy case. Collier on Bankruptcy includes the sub-category of core bankruptcy proceedings to determine the “validity, extent or priority of liens”, see 28 U.S.C. §157(b)(2)(K), within the broader category of core proceedings involving “property of the estate”. See 1 Collier on Bankruptcy §3.02[3][c] at pp. 3-44 through 3-45 (15th ed. rev.). The Bankruptcy Court for the District of Minnesota held that it had jurisdiction to determine the nature and extent of liens against admittedly exempt property in the case of In re Gibbs, 44 B.R. 475, 477 (Bankr. D. Minn. 1984). That holding is not definitive on the situation presented to this Court in this case because it dealt with rights arising under a

specific provision of the Bankruptcy Code, specifically 11 U.S.C. §506(d), which, as this opinion will point out below, is not true in this case. Nevertheless, even if jurisdiction of this adversary proceeding under the grant of jurisdiction over the underlying bankruptcy case is uncertain, the Court concludes that it has “related to” jurisdiction under 28 U.S.C. §1334(b) because whether or not Peoples has any security rights affects the nature and extent of any creditor claim it has against the bankruptcy estate. See In re Toledo, 170 F.3d 1340, 1344-46 (11th Cir. 1999).

This effort by the Debtors to challenge any claim of entitlement by Peoples to a security interest in the Geo Tracker is not a motion to avoid a creditor’s lien pursuant to Bankruptcy Rule 4003(d) and 11 U.S.C. §522(f) on the ground that it impairs the Debtors’ exemption rights. That the Debtors have not attempted to proceed under 11 U.S.C. §522(f) is for the very good reason that Peoples’s security interest, if any, is neither a “judicial lien” under §522(f)(1) nor a “nonpurchase-money security interest” under §522(f)(2). Accordingly, the Debtors have no right to avoid the security interest claimed by Peoples on the ground that it impairs their exemption rights. While it is true that the Chapter 7 bankruptcy trustee may have a right to exercise his “strong arm” powers under 11 U.S.C. §544(a) to avoid People’s security interest for the benefit of the bankruptcy estate, such power is not exercisable by a debtor for his own benefit where the grant of the security interest sought to be avoided was a “voluntary transfer” on such debtor’s part. 11 U.S.C. §522(g), (h) and (i).

The fact that a creditor’s security interest in some part of a bankruptcy debtor’s property in unperfected on the filing date and thus susceptible to attack by the bankruptcy trustee does not invalidate that security interest by operation of law as against the debtor. While the debtor’s personal obligation to repay the creditor may have been discharged or not, either

eventuality does not affect the creditor's rights, if any, in the collateral. Unless expressly avoided pursuant to applicable provisions of the Bankruptcy Code, such rights remain the same as they were immediately prior to the filing of the bankruptcy petition. When a debtor obtains a loan to acquire property and grants a security interest in that property to secure the repayment of that loan, there is no basis under either Virginia law or federal bankruptcy law for that *debtor* to keep such property free and clear of the creditor's interest. See Virginia Code §34-3 (1996 Repl. Vol.); 11 U.S.C. §522(f), (g), (h) and (i).

The Court concludes that the Bankruptcy Code does not accord to it any power to invalidate for a bankruptcy debtor's benefit a voluntary pre-bankruptcy grant of a security interest by that debtor to secure a purchase-money loan. Accordingly, even in the situation presented here where the affected creditor has not appeared in the case to protest such treatment, it will decline to enter a default order requiring that creditor to release its lien rights in property which the bankruptcy debtor seeks to hold exempt.¹ A different situation would be presented if the creditor appeared and expressly consented to such treatment. By separate order the Court will dismiss this adversary proceeding with prejudice as to the Debtors.

This 6th day of January, 2005.

William F. Atone, Jr.
UNITED STATES BANKRUPTCY JUDGE

¹ While the Debtors or their counsel may take issue with the Court's raising these issues *sua sponte*, the Court notes for their benefit that it makes a distinction between raising a possible affirmative defense for a non-appearing party, such as the statute of limitations, which it would not do, and declining to grant relief which according to its understanding of the law is unwarranted on its face, which it is this Court's accustomed practice not to do. A default by one party does not create any legal entitlement on the part of the other party to whatever relief the latter may have been seeking to obtain. Because it concludes that the Roses simply are not entitled to that which they seek, the Court will leave the parties as it finds them.