

UNITED STATES BANKRUPTCY COURT  
FOR THE WESTERN DISTRICT OF MICHIGAN

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In re:

ROLAND LR MUDGET and  
HIEDI ANN MUDGET,  
  
Debtors.

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Case No. DK 12-10989  
Hon. Scott W. Dales  
Chapter 7

THOMAS C. RICHARDSON, Chapter 7  
Trustee,

Plaintiff,

Adversary Proceeding  
No. 13-80178

v.

YANKEE SPRINGS MHC, LLC, and  
PATTERSON HOME SALES, INC.,

Defendants.

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ORDER DENYING TRUSTEE'S  
MOTION FOR APPROVAL OF SETTLEMENT

PRESENT: HONORABLE SCOTT W. DALES  
United States Bankruptcy Judge

Chapter 7 trustee Thomas C. Richardson (the "Trustee") sued Defendants Yankee Springs MHC, LLC and Patterson Home Sales, Inc. (the "Defendants") to avoid as unperfected a security interest in the 2007 Dutch manufactured home (the "Manufactured Home") that Roland and Hiedi Mudgett (the "Debtors") owned on the petition date and continue to use as their residence. The parties have settled their dispute, and the Trustee filed a Stipulated Motion for Approval of Settlement (the "Stipulated Motion," DN 10). The Trustee served the Stipulated Motion on all creditors, and no one objected. Nevertheless, because the court had questions about the settlement, it set the matter for hearing which took place on December 11, 2013, in

Kalamazoo, Michigan. The Defendants and the Trustee appeared through counsel; the Debtors did not.

The Stipulated Motion is, as its title suggests, a settlement stipulation and the Trustee's motion for the court's approval of the settlement, presumably under Fed. R. Bankr. P. 9019. Because the Manufactured Home is at the center of the Trustee's dispute with the Defendants, and because the Debtors use the Manufactured Home as their residence, the Stipulated Motion endeavors to address all competing claims to the property. As of the petition date, for example, the Debtors had possession of the Manufactured Home, but the property itself was included within their bankruptcy estate, subject to the Trustee's control. *See* 11 U.S.C. §§ 323 and 541(a). As for the Defendants, they claimed a security interest in the Manufactured Home which they failed to perfect.<sup>1</sup> The Trustee, as the hypothetical lien creditor under § 544(a), claimed a right to avoid the Defendants' security interest.

As part of the three-way settlement, the Defendants stipulated that their security interest is unperfected (and therefore avoidable under § 544), and they agreed to surrender the Manufactured Home's original certificate of title to the Trustee. The Debtors and the Trustee, in turn, agreed that they would procure a replacement title certificate naming the Debtors as owners and the Trustee as secured party, and that the Debtors would "continue to make all manufactured home monthly payments to the Trustee" until the \$15,242.53 balance of the original loan was paid in full. The Debtor and the Trustee also agreed to certain default and cure provisions less favorable to the Debtors than terms that would otherwise apply under applicable law.<sup>2</sup>

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<sup>1</sup> The Defendants' security interest is not noted on the certificate of title. *See* M.C.L. § 440.9311(1)(b)(iv) (Uniform Commercial Code provision governing perfection of property subject to certificate of title statutes) *and* M.C.L. § 125.2330-2330i (Mobile Home Commission Act).

<sup>2</sup> The agreement contemplates that in the case of default, after a ten day grace period, the Trustee will send a Notice of Default to the Debtors. If the Debtors do not cure the default in thirty days, the Trustee may "liquidate the Manufactured Home" and file the same Notice of Default with the court, together with a consent judgment for the balance due plus interest, "without a hearing." *See* Stipulated Motion at ¶ 4. The agreement does not clearly state

The court's difficulty with the settlement stems from the fact that the Stipulated Motion conflates several steps into one and appears to be premised on the Trustee's view that when he avoids an unperfected lien, he "steps into the creditor's shoes" with respect to the lender's secured claim. The court infers that the Trustee is relying on § 551 for this proposition.

Section 551, however, states only that "[a]ny transfer avoided under section ... 544 ... of this title ... is preserved for the benefit of the estate but only with respect to property of the estate." 11 U.S.C. § 551. Here, because the Trustee is avoiding the Debtors' transfer of a security interest in the Manufactured Home, that transfer (and nothing more) is "preserved" for the benefit of the estate. This automatic preservation prevents junior liens from stepping up in priority upon avoidance,<sup>3</sup> but it does not mean the claim secured by the Manufactured Home is assigned to the estate under § 544 and 551, *ipso jure*, as Trustee's counsel implicitly argued by contending that his client "stepped into" the Defendant's shoes. The Defendants' prepetition contractual rights against the Debtors are not included within the property of the estate, and these rights are not dependent on any collateral that might be included within the estate. *See Morris v. St. John Nat'l Bank (In re Haberman)*, 516 F.3d 1207, 1212 (10th Cir. 2008) ("the Trustee is mistaken when he asserts that he "becomes" the creditor upon avoidance and ascends to *all* the rights thereof.").

If, as the Trustee argues, his right to payment from the Debtors were the actual claim the Defendants held prepetition, then the settlement terms would be unenforceable against the Debtors given the dictates of the Bankruptcy Code's reaffirmation requirements, as Defendants' counsel suggested during the hearing. Under the Trustee's counsel's theory, the settlement

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whether the Debtors get credit for the proceeds of liquidation. They were, however, represented by counsel who presumably advised them of the settlement terms, which they accepted.

<sup>3</sup> *Gold v. New Century Mortgage Corp. (In re Salinitro)*, 355 B.R. 15, 19 (Bankr. E.D. Mich. 2006).

would be “an agreement between the holder of a claim and the debtor, the consideration for which, in whole or in part, is based on a debt that is dischargeable in a case under this title . . .” 11 U.S.C. § 524(c).

Moreover, the terms of the settlement are unclear with respect to the rights, if any, remaining in the Defendants. Under the applicable rule, the Defendants are left with an unsecured claim as a result of the avoidance and could file a proof of claim within 30 days after the judgment avoiding their security interest becomes final. *See* Fed. R. Bankr. P. 3002(c)(3). But because the Defendants presumably retained their claim against the *estate* for the balance due on account of the Debtor’s purchase of the manufactured home, the court could not accept the Trustee’s theory of claim *and* approve the settlement without, in effect, allowing two factions (the Defendants and the Trustee) to hold the same claim—an unworkable result.

In reality, the Trustee is not asserting the Defendants’ former claim. Instead, he has a newly-created right to payment against the Debtors under the Stipulated Motion because, in effect, the estate is selling the Manufactured Home back to them. This gives rise to a new (and non-dischargeable) debt, payable in installments perhaps on terms comparable to those the Defendants originally extended.

The Stipulated Motion’s misleading characterization of the respective parties’ claims relating to the Manufactured Home, however, explains only part of the court’s hesitation to approve the settlement. The court is also concerned that the transaction involves a disguised sale of estate property under 11 U.S.C. § 363(b) and Fed. R. Bankr. P. 6004, and inadequate notice thereof. To start, although the Trustee served the Stipulated Motion on the creditor matrix, the sale aspect of the motion is at most implicit, at best discernible, but not at all obvious. Consequently, the court is not satisfied that the Stipulated Motion gives adequate notice of the

proposed sale despite service on the matrix. Furthermore, the Trustee, using the adversary proceeding caption, filed the Stipulated Motion in the adversary proceeding docket rather than the base case. This could lead less careful readers to believe the scope of the settlement to be more limited than it actually is. In addition, entities filing electronic appearances in the base case might not have received notice of docket events taking place in the adversary proceeding, further undermining the adequacy of the sale notice under Fed. R. Bankr. P. 2002(a)(2) and 6004. Finally, the current notice also violated the spirit as well as the letter of Fed. R. Bankr. P. 2002(c)(1) because it did not include the terms of the sale or the time fixed for filing objections to the sale.

Finally, the court assumes the Trustee does not intend to keep this case open for several years to collect the installment payments from the Debtors. *See Handbook for Chapter 7 Trustees at 4-17* (U.S. Dep't of Justice, Oct. 1, 2012) ("Generally, the trustee should avoid sales of estate assets involving buyer payments which will extend beyond one year."). Rather, the court assumes the Trustee will eventually seek to sell the receivable under § 363(b). *Id.* As presently documented, however, and given the uncertainties the court has described, the court predicts the receivable would be of questionable marketability. At the very least it seems fair to infer that the Trustee's claim against the Debtors would fetch a higher price if the documentation accurately reflected the entire transaction, including the fact and terms of the private sale, and the source of the Trustee's right to payment from the Debtors.

For the foregoing reasons, the court will deny the Stipulated Motion.

NOW, THEREFORE, IT IS HEREBY ORDERED that the Stipulated Motion (DN 10) is DENIED without prejudice.

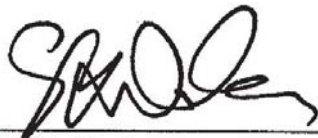
IT IS FURTHER ORDERED that the Clerk shall serve a copy of this Order pursuant to Fed. R. Bankr. P. 9022 and LBR 5005-4 upon Roland LR Mudget and Hiedi Ann Mudget, David A. Trentadue, Esq., Paul F. Davidoff, Esq., and Thomas C. Richardson, Chapter 7 Trustee.

END OF ORDER

**IT IS SO ORDERED.**

Dated December 13, 2013



  
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Scott W. Dales  
United States Bankruptcy Judge