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Unredeemed Pawned Property and Chapter 13 Plan Confirmation: Must a Pawnbroker Object?

Consider the following fact pattern: a consumer borrower enters into a short term loan agreement with a pawnbroker. In exchange for a relatively small amount of money, the borrower pledges the title to his car and gives his certificate of title to the pawnbroker. Under the loan agreement, the borrower remains in possession of his car, but he must repay the loan plus a predetermined charge by a specific date in order to reclaim his title. The borrower fails to timely repay the loan and the associated charge. However, under applicable state law, he is afforded a short redemption period of 30 days during which he may repay the loan and the associated charge to avoid forfeiting the car title. Despite the extra time, the borrower fails to submit funds sufficient to redeem within the 30 day period.

A few days after the expiration of the redemption period, the borrower files a Chapter 13 petition and plan—a plan which proposes to treat (and cure defaults as to) the pawnbroker's debt pursuant to § 1322(b) (2). The pawnbroker receives notice of the borrower's bankruptcy filing and proposed plan. However, the pawnbroker, confident in his belief that he now owns the car, fails to file an objection to the plan which is subsequently confirmed. Shortly thereafter, the pawnbroker files a motion with the bankruptcy court seeking leave to take possession of the car from the borrower.

At the risk of invoking bad memories from law school: what issues do you see? Is the pawned vehicle property of the bankruptcy estate? Would the answer be different if the borrower's right of redemption did not expire prepetition? After failing to redeem the vehicle prepetition, can the borrower utilize § 1322(b) to keep his car and cure his pre-petition default? Also, what is the effect of the pawnbroker receiving notice of the proposed plan and failing to object? Does plan confirmation preclude the pawnbroker's objection? The goal of this article is to address those questions.

Pledged Property and Property of the Estate

"Section 541(a) describes property of the estate as 'all legal or equitable interests of the debtor in property

as of the commencement of the case.'"¹ "As used in § 541(a)(1), the term 'commencement' means the date on which the debtor filed his bankruptcy petition."² Bankruptcy courts look to applicable state law to determine a bankruptcy estate's interest in property.³ Accordingly, whether the borrower's car in our fact pattern is property of the estate depends on which state's personal property and pledged property rules apply.

In many states, a borrower's failure to timely redeem pawned property results in a forfeiture of all right, title, and interest in the pledged property. For instance, under the Alabama Code, "[p]ledged goods not redeemed within 30 days following the originally fixed maturity date shall be forfeited to the pawnbroker and absolute right, title, and interest in and to the goods shall vest in the pawnbroker."⁴ Similarly, under Georgia's pawn statute, "[p]ledged goods not redeemed within the grace period shall be automatically forfeited to the pawnbroker ... and any ownership interest of the pledgor or seller shall automatically be extinguished as regards the pledged item."⁵ In those states,⁶ pledged property which is not redeemed before a borrower files a bankruptcy petition does not become property of the bankruptcy estate.⁷ In other states, a pawnbroker may need to take additional steps in order to take title to pledged property.⁸

Regardless of the state law at issue, most courts agree that once title to pawned property is divested from a borrower under applicable state law, it does not become estate property in a subsequently filed bankruptcy case.⁹

Pledged Property May Drop Out of the Estate

"[I]f redemption rights still exist as of the bankruptcy filing, the Bankruptcy Code extends the redemption period 60 days from the petition date."¹⁰ Thus, if our borrower's right of redemption was still intact when he filed his Chapter 13 case, he would have additional time to redeem his car title. However, under the Eleventh Circuit's decision in *In re Northington*, pledged property may "drop out" of the bankrupt estate if a debtor does not complete the redemption during the allotted (and extended) time period.¹¹

Unredeemed Pledged Property and Section 1322(b)

“Section 1322(b)(2) of the Code allows a debtor to ‘modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor’s principal residence.’”¹² However, once a debtor loses all right, title, and interest in pledged property, nothing remains for a debtor to modify under § 1322(b)(2).¹³ As stated by the bankruptcy court in *In re Thompson*: “It is well established that ‘a Chapter 13 plan cannot be used to revive a debtor’s right to redeem pawned property once the statutory redemption period has expired.’”¹⁴ In accordance, our borrower’s attempt to utilize § 1322(b)(2) to retain his car and to cure his default after failing to redeem the vehicle on a prepetition basis should fail. However, a timely objection by the pawnbroker might be necessary to avoid confirmation of the borrower’s proposed plan.

The Impact of a Pawnbroker’s Failure to Object

Section 1327(a) of the Code provides that “[t]he 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.”¹⁵ “Thus, § 1327 gives *res judicata* effect to a confirmed Chapter 13 plan.”¹⁶ Indeed, “[c]onfirmation of a chapter 13 plan by a bankruptcy court of competent jurisdiction, in accordance with the procedural requirements of notice and hearing of confirmation, ‘is given the same effect as any district court’s final judgment on the merits.’”¹⁷ Clearly, Congress and the courts place a high value on finality and enforceability of confirmation orders. In fact, the United States Supreme Court in *United Student Aid Funds, Inc. v. Espinosa* went as far as to hold that even legally suspect plans will bind properly noticed parties once confirmed.¹⁸

In the case of our borrower, the pawnbroker failed to object to the borrower’s plan which purported to treat the pawnbroker’s debt pursuant to 11 U.S.C. § 1322(b)(2). In doing so, the pawnbroker risked being stuck with the proposed treatment even where he could have asserted a meritorious objection—i.e., that the borrower no longer held an interest in the pledged vehicle. The Eleventh Circuit’s opinion in *Northington* seems to indicate that “some action” should be taken prior to confirmation to preserve one’s rights.¹⁹ However, the majority in *Northington* side-stepped the necessity of a formal objection to confirmation by construing a motion for relief from stay filed by the pawnbroker prior to confirmation as sufficiently asserting the issues with the plan’s proposed treatment.²⁰ But, what happens if no action is taken prior to confirmation, as in the fact pattern detailed above?

Several courts have addressed that question, but a consensus approach has not yet emerged. Very recently, the Bankruptcy Court for the Northern District of Alabama in *In re Tommy and Julie Barnett*²¹ considered essentially the same fact pattern detailed at the beginning of this article. There, pawn-lender TitleMax filed a postconfirmation *Motion to Confirm the Absence of the Automatic Stay*.²² Like in our fact pattern, the prepetition debtor (Mr. Barnett) pawned his car title to TitleMax and failed to timely repay the loan or satisfy the redemption price. Even so, when the Barnetts subsequently filed their Chapter 13 case and plan, they proposed to keep the vehicle and to cure the default pursuant to § 1322(b)(2). TitleMax received notice of the proposed plan, but did not file a response. The bankruptcy court subsequently confirmed the proposed plan and TitleMax’s *Motion* followed. In an oral ruling, the bankruptcy court denied TitleMax’s *Motion* and explained that the pawnbroker improperly “slept on its rights” by failing to object preconfirmation.²³ The court also specifically cited the equitable doctrine of laches in support of its decision.²⁴ Laches is a defense sounding in equity that serves to bar suit by a plaintiff “whose unexcused delay, if the suit were allowed, would be prejudicial to the defendant.”²⁵

In contrast, other bankruptcy courts facing similar fact patterns, albeit under different state law, have concluded that *res judicata* does not bind a pawnbroker to a confirmed plan where the debtor lost all right, title, and interest in the pledged property prepetition.²⁶ Those courts reason that a bankruptcy court lacks jurisdiction to confirm a plan which proposes modified treatment as to property which does not qualify as property of the estate.²⁷ As stated by the bankruptcy court in *In re Thorpe*²⁸:

[T]here are limits to the preclusive effect of a confirmed plan that is not perfectly legal. Under 11 U.S.C. § 1322(b)(2), debtors may modify the rights of certain secured creditors in their chapter 13 plan, but debtors “succeed[] to no greater interest in an asset than that held by the debtor at the time the bankruptcy petition was filed.” *Dunlap v. Cash Am. Pawn of Nashville (In re Dunlap)*, 158 B.R. 724, 727 (M.D. Tenn. 1993). Importantly, debtors may not “restructure the claims of a pawnbroker after the expiration of the redemption period.” *USA Title Pawn v. Askeew (In re Howard)*, 507 B.R. 394, 399 (Bankr. N.D. Ga. 2014) (citing *In re Dunlap*, 158 B.R. at 727). Where the redemption period on a pawned vehicle expires prior to the petition date, the pawned vehicle does not become

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part of the debtor's bankruptcy estate, the Court has no jurisdiction over it, and the plan cannot include it. *In re Howard*, 507 B.R. at 398-99; see also *Barnette v. Bankers Fin. Servs. (In re Barnette)*, Ch. 13 Case No. 07-12986, Adv. No. 07-1068, 2008 WL 7842071, at *2 (Bankr. N.D. Ga. 2008) (holding if the redemption period on a pawned vehicle expires prior to the filing of debtor's bankruptcy petition, the debtor's ownership interest has been forfeited and does not become part of the bankruptcy estate); *Bell v. Instant Car Title Loans (In re Bell)*, 279 B.R. 890, 896-97 (Bankr. N.D. Ga. 2002) (same).

Final Thoughts

It is largely undisputed that pawned property does not enter a subsequently filed bankruptcy estate where the debtor lost all right, title, and interest as to the property under applicable state law. However, it makes good sense for a pawnbroker to take "some action" prior to confirmation if a debtor attempts to include unredeemed property in a proposed Chapter 13 plan. Though jurisdictional concerns abound as to a bankruptcy court's treatment of non-estate property, finality rules provide an interesting counterpoint if a creditor chooses to sleep on its rights. 🏠

Endnotes

- ¹ *In re Thompson*, 609 B.R. 443, 452 (M.D. Ala. 2019).
- ² *In re Northington*, 876 F.3d 1302, 1309 (11th Cir. 2017).
- ³ *Butner v. United States*, 440 U.S. 48, 55 (1979); *Thompson*, 609 B.R. at 452 ("Whether a debtor's interest constitutes property of the estate is a federal question, but bankruptcy courts look to state law to decide whether the debtor had a legal or equitable interest in the property as of the petition date.").
- ⁴ Ala. Code 5-19A-6; *In re Jones*, 304 B.R. 462, 468 (Bankr. N.D. Ala. 2003).
- ⁵ *Northington*, 876 F.3d at 1311 (citing Ga. Code § 44-14-403(b)(3)).
- ⁶ In Alabama, there is an argument to be made that a debtor remaining in possession of a pawned vehicle precludes the automatic operation of Ala. Code § 5-19A-6 since that statute references "pledged goods" and "pledged goods" are defined under Ala. Code § 5-19A-2 as property "deposited with, or otherwise actually delivered into the possession of a pawnbroker in connection with a pawn transaction." The bankruptcy court in *In re Thompson*, 609 B.R. 443, 449 (Bankr. M.D. Ala. 2019), provides a

detailed analysis of a version of that argument and concludes that a creditor's possession of a certificate of title is sufficient under Alabama law for a vehicle to be "pledged goods" even where the debtor retains possession of the vehicle.

- ⁷ *Thompson*, 609 B.R. at 453 ("In circumstances where a default occurs and the redemption period expires pre-petition, the pawned vehicle does not become property of the estate."); *In re Howard*, 507 B.R. 394 (Bankr. N.D. Ga. 2014) ("Because the Debtor did not pay the outstanding principal, interest, or other charges due on the maturity dates of the contracts and because the Debtor did not redeem the vehicles prior to filing for bankruptcy protection, the vehicles are not included in 'property of the estate.'").
- ⁸ See, e.g., *In re Sorensen*, 586 B.R. 327, 335 (B.A.P. 9th Cir. 2018) (explaining that, unlike Georgia's pawnshop law, California's law requires a pawnbroker to send written notice to a borrower before obtaining legal title to pawned property).
- ⁹ See *In re Thorpe*, No. 18-20082, 2019 WL 1785303, at *3-*4 (Bankr. S.D. Ga., Mar. 29, 2019) (explaining that when a debtor failed to redeem her vehicle under applicable Georgia law prior to the filing of her current bankruptcy case she "had no interest in the [v]ehicle whatsoever that could have become property of the estate in the [p]resent [c]ase"); *Thompson*, 609 B.R. at 453 ("In circumstances where a default occurs and the redemption period expires pre-petition, the pawned vehicle does not become property of the estate."); *In re Bell*, 279 B.R. 890, 896-97 (Bankr. N.D. Ga. 2002) (debtor no longer held an interest in pawned property once the redemption period expired prepetition and pawned property was not property of the estate); *In re Walker*, 204 B.R. 812, 816 (Bankr.M.D.Fla.1997) ("This Court has also held that if a debtor fails to redeem the property within the redemption period, debtor's right to redeem is terminated, and debtor's interest in the property is permanently extinguished. In this case, Debtor failed to redeem the truck prior to the expiration of the redemption period, and the Court finds that his interest in the property was terminated by law on May 14, 1996.").
- ¹⁰ *Thompson*, 609 B.R. at 453 (citing 11 U.S.C. § 108(b)(2)); *In re Bramlett*, 483 B.R. 244, 246, (Bankr. N.D. Ala. 2012); *Thorpe*, No. 18-20082, 2019 WL 1785303, at *2 ("[W]hatever a debtor's interest in a pawned vehicle is on the petition date, if any, will enter the bankruptcy estate; this also includes any right of redemption a debtor may have in the pawned vehicle.").

- ¹¹ *Northington*, 876 F.3d at 1306 and 1314 (explaining that “an estate is not necessarily ‘frozen in time,’ but rather can, in certain circumstances, expand or contract in accordance with the operation of underlying state-law property rules”).
- ¹² *In re Jones*, 304 B.R. 462, 466 (Bankr. N.D. Ala. 2003); *Northington*, 876 F.3d at 1315 (“It is axiomatic, though, that a plan can ‘modify ... rights’ arising under a ‘claim’ only if the claim exists at the time the plan would purport to modify the rights associated with it—namely, at confirmation.”).
- ¹³ (*Id.*); *In re Dunlap*, 158 B.R. 724, 728 (M.D. Tenn. 1993) (“Accordingly, after the redemption period has run, a debtor may not seek to cure or modify the pawn contract under § 1322, because this remedy only applies to goods in which the estate retains an interest.”); *In re Howard*, 507 B.R. 394, 399–400 (Bankr. N.D. Ga. 2014) (“Cases dealing with this issue have held that § 1322(b)(2)—which authorizes a debtor to modify the rights of certain holders of secured claims in a Chapter 13 plan—cannot be used to restructure the claims of a pawnbroker after the expiration of the redemption period.”).
- ¹⁴ *Thompson*, 609 B.R. 443, 452–53; *see also In re Young*, 281 B.R. 74, 77 (Bankr. S.D. Ala. 2001) (“If a redemption period has expired prior to the filing of bankruptcy, then the contract may not be modified because this remedy applies only to property in which the estate retains an interest.”); *In re Dunlap*, 158 B.R. 724, 727–28 (M.D. Tenn. 1993) (holding that a debtor cannot modify a pawn contract under 11 U.S.C. § 1322 where the debtor lost all right title and interest in the pawned goods prepetition); *In re Howard*, 507 B.R. 394, 399–400 (Bankr. N.D. Ga. 2014) (“Here, the Debtor’s obligation fully matured and she defaulted on payment and failed to redeem the Suzuki and the Chevrolet within the Georgia Code’s grace period, so USA Title became the effective owner of the vehicles prior to the filing of this case as a result of the statutory automatic forfeiture provision, and they ceased to be the Debtor’s property. Had the debtor filed bankruptcy before her right to redeem expired, she would have been permitted to cure her default and keep the vehicles; but her right of redemption expired pre-petition, so at that point she no longer had a right to cure her default under the Bankruptcy Code.”).
- ¹⁵ *Universal Am. Mortg. Co. v. Bateman (In re Bateman)*, 331 F.3d 821, 830 (11th Cir. 2003).
- ¹⁶ (*Id.*).
- ¹⁷ (*Id.*) (citing *In re Justice Oaks II, Ltd.*, 898 F.2d 1544, 1550 (11th Cir. 1990)).
- ¹⁸ *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260, 269 (2010).
- ¹⁹ *Northington*, 876 F.3d at 1308.
- ²⁰ (*Id.* at 1307–08).
- ²¹ *Tommy Barnett, Jr. and Julie Barnett*, No. 19-81656-CRJ-13 (Bankr. N.D. Ala.).
- ²² (*Id.* at Doc. 66).
- ²³ (*Id.* at Doc. 78 (attaching the hearing audio) and Doc. 77 (denying the *Motion* and incorporating the hearing record)).
- ²⁴ (*Id.*).
- ²⁵ *Black Warrior Riverkeeper, Inc. v. U.S. Army Corps of Engineers*, 781 F.3d 1271, 1283 (11th Cir. 2015). “The elements of laches are (1) lack of diligence by the plaintiff(s), and (2) prejudice to the defendant(s) as a result of the delay.” *In re Beeghley*, 529 B.R. 98, 104 (Bkrtcy.E.D. Pa. 2015).
- ²⁶ *In re Howard*, 507 B.R. 394, 400 (Bankr. N.D. Ga. 2014) (“True enough, the confirmed Chapter 13 plan treats the two vehicles as property of the Debtor and the obligation related thereto as a debt that can be restructured, but this fact is irrelevant when, as here, the vehicles did not become property of the estate upon the filing of Debtor’s petition, and therefore they were not property within the Court’s vested jurisdiction.”) and (“[T]he Debtor’s Chapter 13 plan cannot bring property into her bankruptcy estate that was not her property as of the petition date.”); *In re Thorpe*, No. 18-20082, 2019 WL 1785303, at *3–*4 (Bankr. S.D. Ga., Mar. 29, 2019).
- ²⁷ (*Id.*).
- ²⁸ *Thorpe*, No. 18-20082, 2019 WL 1785303, at *4. *See also In re Danley*, 552 B.R. 871, 883 (Bankr. M.D. Ala. 2016) (“The Court had in rem jurisdiction over the Residence when the Danleys filed bankruptcy. However, a bankruptcy court’s in rem jurisdiction over property only lasts so long as that property remains in the estate; if the property leaves the estate, in rem jurisdiction lapses.”).