IN THE UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF ARIZONA

In re:	)	Chapter 13
	)	
FRANCISCO J. ESPINOSA,	)	Case No. 4-92-03819-EWH
	)	
	)	
Debtors.	)	**MEMORANDUM DECISION**
	)	

INTRODUCTION

Are the terms of a confirmed Chapter 13 Plan that provide for discharge of a student loan debt binding if the debtor failed to follow the requirements of the Bankruptcy Code and Bankruptcy Rules of Procedure for obtaining a hardship discharge of the student loan obligation? I find that the holding of In re Pardee, 193 F.3d 1083 (9th Cir. 1999) controls and requires an affirmative answer to the question.

FACTS

The Debtor filed a Chapter 13 Petition ("Petition") and Chapter Plan ("Plan") on December 7, 1992. The Plan which was noticed to all creditors pursuant to Fed. R. Bankr. P. 2002(b), including United States Student Aid Funds ("USA Funds") and the United States Department of Education ("DE") (collectively "Student Loan Creditors"), provided for the payment of $13,250.00 in outstanding student loan debt owed to a number of different student loan creditors. The Plan provided that "any amounts or claims for student loans unpaid by this Plan shall be discharged." Both the Plan and the 341 notice listed April 15, 1993 as the date

of the confirmation hearing. The Plan provided that any objections to the Plan be filed seven (7) days prior to the confirmation hearing.

On January 18, 1993, USA Funds, apparently on behalf of all of the outstanding student loan creditors, filed an unsecured, non-priority claim of $17,832.15. On March 30, 1993, the Chapter 13 Trustee filed an objection to the proposed Plan because the Plan classified the student loan claim as a priority. The Student Loan Creditor did not file a Plan objection. On April 25, 1993, a confirmation hearing was held. There were no objections to the confirmation of the Plan, other than that of the Trustee, which was resolved pursuant to a stipulated order ("Confirmation Order") entered on May 6, 1993.

On June 10, 1993, the Trustee objected to USA Funds' Proof of Claim because the amount of the claim differed from the amount provided for in the Plan. The Trustee served USA Funds with its objection at the address listed on its Proof of Claim. The objection provided that if no response was filed, the claim would be allowed at the Plan amount. There was no response filed. On May 30, 1997, the Debtor received a discharge after completing all Plan payments, including payment of $13,250.00 to USA Funds.

Beginning in 2001, the Student Loan Creditors began collection efforts against the Debtor, asserting the outstanding obligation was in excess of $17,000.00 and that the obligation had not been discharged under the Plan. After various efforts to resolve the matter, the Debtor moved to reopen the case and filed a Motion for Violation of the Discharge, Contempt, Sanctions and Damages ("Motion").

JURISDICTIONAL STATEMENT

Jurisdiction is proper in this case pursuant to 28 U.S.C. § 157(b)(2)(L) and (O).

ISSUES

1. Is the Confirmation Order void?

2. If the Confirmation Order is not void, should sanctions be imposed on the Student Loan Creditors for violation of the discharge injunction?

DISCUSSION

USA Funds and DE have filed two identical briefs opposing the Motion. USA Funds and DE argue that the Confirmation Order is void pursuant to Fed. R. Civ. P. 60(b)(4) (made applicable in bankruptcy cases by Fed. R. Bankr. P. 9023) either because: (1) the Debtor did not give notice of the student loan discharge terms in the Plan in the same manner as if he had filed an adversary proceeding seeking a hardship discharge under 11 U.S.C. § 523(a)(8), thereby purportedly denying the Student Loan Creditors of their constitutional due process rights; or (2) the bankruptcy court lacked subject matter jurisdiction to enter the Confirmation Order because the Plan contained so-called "illegal" terms which were inconsistent with the Bankruptcy Code's requirement that an adversary proceeding be filed in order to obtain a discharge of a student loan.

I address the argument regarding lack of subject matter jurisdiction first. This exact argument was rejected by the Ninth Circuit in In re Pardee, 193 F.3d 1083 (9th Cir. 1999). The facts in Pardee are almost identical to the facts of this case. In Pardee, the Chapter 13 debtors moved to enforce their discharge and to enjoin the student loan creditor's attempt to collect interest on the student loan obligation. The Pardee Plan contained a provision

discharging the post-petition interest on their student loan debt. The student loan creditor had notice of the Plan and its discharge provisions but failed to object to the Plan. In Pardee the student loan creditor asserted, and the Ninth Circuit considered and rejected, the argument that if a Chapter 13 plan contains so-called "illegal provisions," that the Plan is nugatory and res judicata principles cannot prevent post-discharge collection efforts by the student loan creditor: "[t]his court has recognized the finality of confirmation orders even if confirmed bankruptcy plans contain illegal provisions." Id. at 1086, citing Trulis v. Barton, 107 F.3d 685, 691 (9th Cir. 1995); Stratosphere Litig. LLC v. Grand Casinos, Inc., 298 F.3d 1137; 1143 (9th Cir. 2002).

Recently, the Ninth Circuit has issued a decision which casts some doubt on the continued viability of the holding in Pardee. In re Enewally, 368 F.3d 1165 (9th Cir. 2004), addressed the question of whether an order which approved a modification to a confirmed plan had a res judicata effect on the creditor. The Enewally court cited Trulis v. Barton and Pardee for the proposition that "it is beyond cavil that once a bankruptcy plan is confirmed, it is binding on all parties and all questions that could have been raised pertaining to the plan are entitled to res judicata effect." In re Enewally, 368 F.3d at 1173 (internal quotations omitted). However, one paragraph later the court states "although confirmed plans are res judicata to issues therein, the confirmed plan has no preclusive effect on issues that must be brought by an adversary proceeding, or were not sufficiently evidenced in a plan to provide adequate notice to the creditor." Id. Certainly, the above-cited language is broad enough to call the holding of Pardee into question. But the facts in Enewally are significantly different than here, or in

Pardee. In Enewally, the debtor had commenced an adversary proceeding to obtain the "lien-stripping" result noticed in the Plan modification. Even more importantly, the modification which the debtor argued had altered the secured creditor's rights was approved by the bankruptcy court, conditioned upon the debtor prevailing in the adversary. On these facts it is clear that the plan modification could not have a res judicata effect where the validity of the modification was specifically reserved for decision in the adversary. The essence of the Enewally holding on res judicata is that "a Chapter 13 plan confirmed while an adversary proceeding was pending would not have res judicata effect on the adversary proceeding." Id. Regardless of Enewally's broad language, it did not overrule Pardee. Given the different fact pattern in Enewally, the similarity of the facts in this case to those in Pardee, and Enewally's citation to Pardee as "good law," the Student Loan Creditors cannot prevail on their subject matter jurisdiction arguments in this case.

The second argument urged by the Student Loan creditors is that they were denied due process because the notice they received of the Plan was not equivalent to the notice required by Fed. R. Bankr. P. 7001(6), which requires the service of a summons and complaint in order to initiate a complaint to determine if a student loan debt should be discharged under 11 U.S.C. § 523(a)(8). The Student Loan Creditors argue that because Pardee does not directly address whether the student loan creditor's due process rights were violated by receiving notice under Fed. R. Bankr. P. 2002, instead of Fed. R. Bankr. P. 7016, that the holding in Pardee does not control the outcome of the case.

In re Repp, 307 B.R. 144 (9th Cir. BAP 2004), is a recently decided case very similar to this one, in which the majority agreed with the arguments made by the Student Loan Creditors. The majority found that the minimal service requirements for Chapter 13 plan confirmations could not be used to elude the obligations to demonstrate undue hardship in an adversary proceeding. However, as pointed out by Judge Ryan's well-reasoned dissent, by deciding that a student loan creditor, who received notice under Fed. R. Bankr. P. 2002(b) of an adverse plan provision, is bound by that provision, the Ninth Circuit necessarily determined that the notice the creditor received satisfied due process requirements. Id. at 155.

In this case, USA Funds had several months notice of the Plan and its student loan discharge provisions. USA Funds filed a proof a claim before the Plan confirmation hearing. USA Funds received an objection to its claim shortly after the Plan was confirmed when it could have easily moved under Rule 9023 to revoke the discharge on the grounds that the Plan "illegally" discharged the balance of the Debtor's student loan obligations.[1] It did not do so. As Judge Ryan noted in his dissent in Repp, "[t]he idea that a creditor with more than 25 days notice of a plan containing a provision that adversely affects it can ignore the proceeding, sit on its rights, and then raise a due process argument years later, defies common sense." Id.; In re Pardee, 193 F.3d at 1086 (the student loan creditor "failed to take an active role in protecting its own interests" and so cannot, years later, expect the bankruptcy court or trustee

[1]A motion to alter or amend a judgment must be filed no later than 10 days after entry of the judgment. Fed. R. Bankr. P. 9023(3).

to protect its interests.) As Judge Ryan also noted, due process does not place form over substance.[2]

In reaching this decision, I do not condone what the debtor did in this case. I agree with the approach adopted by Judge Haines in In re Webber, 251 B.R. 554 (Bankr. D. Ariz. 2000) and would not confirm a Chapter 13 plan that contained student loan discharge provisions similar to the provisions in this case. However, what is at issue in this case is not whether the Plan should have been confirmed, but the effect of the Plan's confirmation and the Debtor's receipt of a discharge after making all of the required Plan payments. The Repp decision ignores the fact that the holding in Pardee is based on the determination that the student loan creditors' failure to object after receiving notice of the Chapter 13 plan and its terms barred it from later attacking the terms of that order. It follows that if the notice the creditor received did not satisfy due process requirements, then the student loan creditors could not have been bound by the terms of the confirmed Chapter 13 plan; however, the Ninth Circuit held in Pardee that the creditor was bound, and therefore, the notice must have been sufficient to satisfy due process.

CONCLUSION

Because I find that because the Confirmation Order is not void, the Debtor's request that the Student Loan Creditors cease and desist all collection activity against the Debtor will

---

[2]The due process requirement is satisfied with notice that is reasonably calculated, under all the circumstances, to apprise interested parties of pendency of action and to afford them the opportunity to object; it must be of such a nature as to reasonably convey the required information and to afford reasonable time for response. Mullane v. Cent. Hanover Bank & Trust Co., 339 US 306, 314 (1950).

be granted. However, because a number of courts agree with the position taken by the Student Loan Creditors, this is not an appropriate case for imposing sanctions for violation of the discharge injunction.[3] Moreover, the Student Loan Creditors have returned tax refunds previously withheld. Therefore, all remaining requests for relief in the Debtor's motion will be denied. An order consistent with the terms of this Memorandum Decision will be entered this date.

Dated this 12th day of August, 2004.

Eileen W. Hollowell

EILEEN W. HOLLOWELL
UNITED STATES BANKRUPTCY JUDGE

Copy of the foregoing mailed this
12 day of August, 2004, to:

James L. Robinson, Jr.
Robinson & Rylander
4340 North Campbell Ave., Suite 266
Tucson, AZ 85718
Attorneys for Debtor

---

[3] There is a split in the Circuits on the issue. Some courts hold that a confirmed Chapter 13 plan that purports to discharge student loan debt without the filing of an adversary proceeding cannot have res judicata effect on a creditor that did not object to the discharge provision at confirmation. See e.g., In re Banks, 299 F.3d 296 (4th Cir. 2002). However, other courts uphold the discharge even where there is a provision in a confirmed Chapter 13 plan that a student loan will be discharged upon completion of the plan and no adversary proceeding to determine the hardship discharge was filed. See In re Boyer, 305 B.R. 42 (Bankr. D. Kan. 2004); In re Andersen, 179 F.3d 1253 (10th Cir. 1999); In re Patton, 261 B.R. 44 (Bankr. E.D. Wash. 2001).

Madeleine C. Wanslee
Gust Rosenfeld
201 East Washington, Suite 800
Phoenix, AZ 85004-2327
Attorneys for United States Student Aid Funds, Inc.

Elizabeth Wilson
Office of the U.S. Attorney
405 West Congress St. #4800
Tucson, AZ 85701
Attorneys for U.S. Department of Education

Dianne Kerns, Chapter 13 Trustee
7320 North La Cholla Blvd. #154-413
Tucson, AZ 85741

By _____
Judicial Assistant