

**IN THE UNITED STATES BANKRUPTCY COURT  
WESTERN DISTRICT OF ARKANSAS  
FAYETTEVILLE DIVISION**

**IN RE: TIMOTHY and REBECCA WALTERS, Debtors**

**No. 5:07-bk-72025  
Ch. 13**

**ORDER**

Before the Court is the Objection to Confirmation of Modified Plan Dated 11-15-2007 filed on November 21, 2007, by creditor Wells Fargo Auto Finance, Inc. [Wells Fargo]. Wells Fargo argues that it has an allowed claim against the debtors that is secured by a purchase money security interest [PMSI] in a motor vehicle acquired for the personal use of the debtors within the 910 days preceding the filing of the debtors' petition. The creditor believes that because it holds what is known as a 910 car claim, the claim is not subject to valuation under 11 U.S.C. § 506 of the bankruptcy code, which allows bifurcation of a claim (secured/unsecured) based on the value of the collateral. The debtors argue that the security interest includes "negative equity," and is not a PMSI, and that bifurcation is appropriate. The chapter 13 trustee also appeared at the hearing and asked the Court to apply the transformation rule to negate the creditor's security interest in the alleged negative equity. The Court heard the objection to confirmation on April 29, 2008, and allowed the parties 25 days to file post-trial briefs in support of their respective positions. For the reasons stated below, the Court sustains Wells Fargo's objection.

This Court has jurisdiction over this matter under 28 U.S.C. § 1334 and 28 U.S.C. § 157, and it is a core proceeding under 28 U.S.C. § 157(b)(2)(K) and (L). The following opinion constitutes findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052, made applicable to this proceeding under Federal Rule of Bankruptcy Procedure 9014.

## Stipulations

After opening statements, the parties read into the record the following stipulations:

1. On or about August 18, 2006, the debtors purchased from Hendren Chevrolet-Pontiac, Inc., in Pineville, Missouri pursuant to a Retail Installment Contract and Security Agreement (“contract”) a 2006 Chevrolet Malibu, bearing VIN # 1G1ZT51846F183479 (“vehicle”). For valuable consideration and in the ordinary course of business, Wells Fargo purchased the contract in good faith from the dealership without notice of any claim or defense to it, and by proper assignment, became the holder thereof. A true and correct copy of the contract is attached hereto, made a part hereof, and marked as Exhibit “A”.
2. Wells Fargo claims a purchase money security interest in the vehicle, and the security interest was perfected under Arkansas law. A true and correct copy of the Arkansas Certificate of Title to the vehicle noting Wells Fargo’s lien thereon is attached hereto, made a part hereof, and marked as Exhibit “B”.
3. The specific material terms of the contract secured by the vehicle provided the cash price of the vehicle was \$28,954.15; a manufacturer’s rebate of \$1,500.00; a trade-in allowance of \$10,500.00 on a 2003 Chevrolet Cavalier; a payoff amount of \$10,400.00 to Nuvel on the Cavalier; a \$100.00 net trade-in credit; a \$1600.00 net cash/trade-in down payment on the vehicle. The resulting unpaid balance cash price was \$27,354.15, plus a \$1.00 filing fee, a \$149.00 document fee, and a \$500.00 Express Autogap policy fee. The resulting amount which debtors financed equaled \$28,004.15, at an annual percentage rate of 17.19%, over 72 months, with monthly installment payments of \$630.37 commencing on October 3, 2006.
4. On or about June 29, 2007, Debtor’s filed their voluntary petition under Chapter 13 of the United States Bankruptcy Code.
5. On or about August 1, 2007, Wells Fargo filed its Proof of Claim asserting a secured claim in the amount of \$27,703.98. A true and correct copy of said claim is attached hereto, made a part hereof and marked as Exhibit

“C”.

6. The debtors purchased the vehicle for their personal use within 910 days of the filing of their bankruptcy petition.
7. On November 15, 2007, debtors filed a second amended plan, which proposed to pay Wells Fargo’s claim applying 11 U.S.C. § 506, valued the vehicle at \$13,700.00, and proposed to pay that amount at 9.25% interest at \$286.05 per month. The parties stipulate that the current retail value of the vehicle is \$13,700.00. A true and correct copy of the amended plan is attached hereto, made a part hereof, and marked as Exhibit “D”. Wells Fargo objected to confirmation of the amended plan on November 21, 2007. The objection is based in part on the debtor’s classification of creditor as a claim where § 506 is applicable.
8. Solely for the purposes of this case, the parties stipulate that the rate of interest under *Till vs. SCS Credit Corp.*, 541 U.S. 465 (2004) proposed by Debtors’ in their plan is 9.25%.

After reading the stipulations into the record, the parties provided the Court with a written copy of the stipulations with the following exhibits attached:

- Ex. A: Retail Installment Contract and Security Agreement
- Ex. B: Certificate of Title
- Ex. C: Proof of Claim of Wells Fargo Bank, N.A.,
- Ex. D: Modification of Chapter 13 Plan

### **Findings of Fact and Conclusions of Law**

According to the bankruptcy code, the court shall confirm a plan if the requirements of 11 U.S.C. § 1325(a) are met. In their current chapter 13 plan, the debtors state that Wells Fargo “is to receive the value of the vehicle \$13,700, payable at 9.25%.” Wells Fargo objected to their plan and argues that the debtors should be paying the full amount of their claim, \$27,703.98. The hanging paragraph located in § 1325(a) states,

For purposes of paragraph (5),<sup>1</sup> *section 506 shall not apply to a claim*

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<sup>1</sup> The reference to paragraph (5) refers to § 1325(a)(5), which describes how allowed secured claims are treated in a confirmable plan.

*described in that paragraph if the creditor has a purchase money security interest* securing the debt that is the subject of the claim, the debt was incurred within the 910-day preceding the date of the filing of the petition, and the collateral for that debt consists of a motor vehicle (as defined in section 30102 of title 49) acquired for the personal use of the debtor, or if collateral for that debt consists of any other thing of value, if the debt was incurred during the 1-year period preceding that filing.

11 U.S.C. § 1325(a)(last paragraph) (emphasis added). If § 506 applies to Wells Fargo's claim then the debtors may bifurcate the claim into secured and unsecured portions based on the value of the collateral. If, instead, Wells Fargo has a PMSI of the kind described in the hanging paragraph and § 506 does not apply to its claim, the debtors must provide for payment of the full amount of Wells Fargo's claim in their plan. The parties do not dispute that the debt that is the subject of Well's Fargo claim was incurred within 910 days preceding the bankruptcy filing or that the vehicle involved was acquired for the debtor's personal use. Rather, the application of § 506 depends on whether Wells Fargo's interest is a PMSI within the purview of the hanging paragraph located in § 1325(a).

The definition of PMSI in this case is a question of Missouri state law. *In re Weiser*, 381 B.R. 263, 266 (Bankr. W.D. Mo. 2007).<sup>2</sup> Under Missouri statute, a security interest in goods is a PMSI "[t]o the extent that the goods are purchase-money collateral with respect to that security interest." Mo. Ann. Stat. § 400.9-103(b)(1) (West, WESTLAW through 2008 Second Reg. Sess.). Wells Fargo has a PMSI only to the extent that its collateral is purchase-money collateral. "Purchase-money collateral" is defined as

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<sup>2</sup> The bankruptcy code does not define PMSI, and, therefore, courts turn to applicable state law. *In re Townsend*, 2008 WL 920610, \*6-7 (Bankr. D. Kan. 2008); *In re Weiser*, 381 B.R. at 266. In this case, the parties' contract states that "[t]he law of Missouri shall govern this transaction," and neither party contested that provision. When courts have construed PMSIs under the hanging paragraph, they have looked to the definitions in Article 9 of the Uniform Commercial Code [UCC]. *Townsend*, 2008 WL 920610, at \*7. The Missouri Bankruptcy Court has found the definitions regarding PMSIs in Missouri's version of the UCC to be "a useful guide to Missouri's use of the term 'purchase money security interest.'" *Id.* (quoting *Weiser*, 381 B.R. at 266).

“goods or software that secures a purchase-money obligation incurred with respect to that collateral.” § 400.9-103(a)(1). Wells Fargo’s collateral is purchase-money collateral if it secures a purchase money obligation. *See In re Townsend*, 2008 WL 920610, \*4 (Bankr. D. Kan. 2008). A "purchase-money obligation" is "an obligation of an obligor incurred as all or part of the price of the collateral or for value given to enable the debtor to acquire rights in or the use of the collateral if the value is in fact so used."

§ 400.9-103(a)(2). Therefore, Wells Fargo has a PMSI in the total amount financed if the debtors’ obligation was incurred as all or part of the price of the Malibu or if the debtors’ obligation was for value given to enable them to acquire rights in or use of the Malibu. The debtors assert that part of their obligation was incurred because of the debtors’ negative equity<sup>3</sup> in the trade-in.

In this case, the debtors financed their purchase of a new 2006 Chevrolet Malibu pursuant to a retail installment contract and security agreement. The contract reflects the debtors traded in a 2003 Chevrolet Cavalier. According to the contract, the collateral in which the debtors gave the creditor a security interest included,

the Vehicle, all accessions, attachments, accessories, and equipment placed in or on the Vehicle, together called Property, and proceeds of the Property. You also assign to us and give us a security interest in proceeds and premium refunds of any insurance and service contracts purchased with this Contract.

The contract also itemizes the amounts the debtors financed as follows:

Vehicle Price (incl. sales tax of \$1109.15): \$29,954.15

Service Contract: N/A

Cash Price: \$28,954.15

Manufacturer’s Rebate: \$1500.00

Cash Down Payment: N/A

Deferred Down Payment: N/A

Total Cash/Rebate Down: \$1500.00

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<sup>3</sup> Negative equity in this case refers to the amount by which the outstanding balance on the Cavalier exceeded the value of the Cavalier.

Trade-In Allowance: \$10,500.00  
Less: Amount Owing: \$10,400.00  
Net Trade-In: \$100.00  
Net Cash/Trade-In: \$1600.00

Down Payment: \$1600.00  
Unpaid Balance of Cash Price: \$27,354.15

After a filing fee, document fee, and a \$500.00 express auto gap policy fee,<sup>4</sup> the contract shows that the Amount Financed totaled \$28,004.15. The debtors presented testimony that the Cavalier was worth less than the Trade-In Allowance, that it is common in the industry to include negative equity in the selling price of the vehicle in the contract, and that the Malibu's sticker price reflected a total vehicle price less than that reflected in the contract for sale. The debtors argue that this evidence proves that a portion of the amount financed is attributable to negative equity.

However, on its face, the contract fails to show that the total amount financed included any negative equity in the trade-in; in fact, the contract shows that the debtors were allowed \$10,500 for their trade-in, which is \$100 more than the contract reflects was owed on the Cavalier. The evidence presented by the debtors does not indicate that negative equity was included in the final agreement between the parties. The Court would have to engage in speculation to hold that any amount of negative equity was included in the parties' final agreement, which is evidenced by the contract.

The Court acknowledges the discrepancy between the Malibu sticker price and the final contract price. But even if this court found that there was negative equity from the trade-in that accounted for the discrepancy, Wells Fargo would still have a PMSI in the total amount of the debtors' obligation for purposes of the hanging paragraph. Comment 3 to

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<sup>4</sup> Though the chapter 13 trustee mentioned in her opening statement the issue of whether gap insurance is "included in a purchase money security interest," the trustee presented no evidence on this point at hearing, the parties did not pursue the issue in their briefs, and the debtors did not assert that anything other than the financing of negative equity would prevent Wells Fargo from holding a PMSI in the total obligation.

the Missouri statute elaborates on the definitions of "purchase-money collateral" and "purchase-money obligation" under the statute:

As used in subsection (a)(2), the definition of "purchase-money obligation," the "price" of collateral or the "value given to enable" *includes* obligations for expenses incurred in connection with acquiring rights in the collateral, sales taxes, duties, finance charges, interest, freight charges, costs of storage in transit, demurrage, administrative charges, expenses of collection and enforcement, attorney's fees, and other similar obligations.

The concept of "purchase-money security interest" *requires a close nexus between the acquisition of collateral and the secured obligation*. Thus, a security interest does not qualify as a purchase-money security interest if a debtor acquires property on unsecured credit and subsequently creates the security interest to secure the purchase price.

Mo. Ann. Stat. § 400.9-103, cmt. 3 (emphasis added).

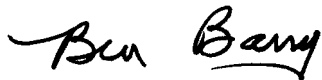
Mr. Walters admitted at the hearing that the contract was a negotiated, package deal and that he would not have been able to purchase the Malibu without trading in the Cavalier. In the light of the comment above, this Court agrees with the line of cases that hold that if a portion of the purchase money obligation is attributable to negative equity on a trade-in, this portion is part of the price of the collateral or value given to enable the debtor to acquire rights in the vehicle when there is a close nexus between the acquisition of the collateral and the secured obligation. *In re Weiser*, 381 B.R. at 267-68 (finding that because the debtor could not have acquired rights in the vehicle without rolling in the negative equity, there is a "close nexus" between the purchasing of the new vehicle and the portion of the obligation used to pay off the trade-in). Where the transaction is a package deal, as would be the case here, any negative equity would have been part of that deal and "inextricably intertwined with the sales transaction and the financing of the purchase." *Graupner v. Nuvell Credit Corp.*, 2007 WL 1858291, at \*2 (M.D. Ga. 2007) (holding that the "close nexus between the negative equity and [the] package transaction supports the conclusion that the negative equity must be considered as part of the price of the collateral").

Therefore, because the contract reflects that the debtors' original obligation was a purchase money obligation and the obligation was secured by purchase money collateral, the Court finds that Wells Fargo's claim is a PMSI of the kind described in the hanging paragraph, and the bifurcation provisions of § 506 are not applicable. Because this Court does not find negative equity, it is unnecessary to discuss the transformation rule raised by the trustee in this case. Hence, the creditor's objection to the debtors' plan is sustained. The debtors shall have 20 days from the entry of this order to amend their plan to provide for the entire amount of Wells Fargo's claim.

IT IS SO ORDERED.

June 19, 2008

DATE



BEN T. BARRY

UNITED STATES BANKRUPTCY JUDGE

cc: Jack L. Martin, attorney for the debtors  
Louis Whitaker Light, attorney for creditor Wells Fargo Auto Finance, Inc.  
Patt Pine, attorney for the chapter 13 trustee  
Joyce Bradley Babin, chapter 13 trustee