

IN THE UNITED STATES BANKRUPTCY COURT  
EASTERN DISTRICT OF ARKANSAS  
WESTERN DIVISION

IN RE:           FREDERICK L. STARKS,  
                          Debtor.

NO. 4:05-bk-10728  
CHAPTER 13

ORDER

This case is before the Court upon a motion for relief from stay filed by Castle Investments, LLC (“Castle”). The issues in this case arise from the pre-bankruptcy foreclosure sale to Castle of 6205 Meadowbrook Lane, the home of Frederick Starks (“Debtor”). The Court is asked to decide two questions: (1) whether Castle is bound by the Debtor’s confirmed chapter 13 plan that proposes to pay his monthly mortgage payments and arrearage on the home even though the home had been sold to Castle prior to bankruptcy and (2) whether the foreclosure sale can be set aside because of alleged irregularities in the sale.

A hearing on the motion for relief was held on July 22, 2005, in Little Rock, Arkansas, and the matter was taken under advisement. Briefs have been filed by both parties.

The matter before the Court is a core proceeding pursuant to 28 U.S.C. § 157 (b)(2)(G), and the Court has jurisdiction to enter a final order in this case. For the reasons stated below, the Court finds that Castle is not bound by the plan and that the Court should abstain from deciding whether sale irregularities occurred.

FACTS

The material facts in this case are not in dispute. A non-judicial foreclosure sale of the home occurred on January 18, 2005, at 11:00 a.m., and Castle was the successful bidder for the sum of \$85,000.00. (Petitioner’s Ex. 6.) The Trustee’s Deed conveying the property to Castle

was recorded by the Circuit Clerk of Pulaski County, Arkansas on January 21, 2005. Id.

Two days after the foreclosure sale, the Debtor's petition for relief under the provisions of Chapter 13 of the United States Bankruptcy Code was filed on January 20, 2005. On his Schedule A. Real Property, the Debtor listed the residence located at 6205 Meadowbrook Lane in which he claimed a one-half ownership interest valued at \$50,000.00. The Debtor's Schedule D listed Wells Fargo as a secured creditor with a claim for \$75,000.00 secured by a lien in the home. He claimed the home as an exempt homestead pursuant to 11 U.S.C § 522(d)(1).

On February 22, 2005, the Debtor amended his schedules to increase the value of his interest in the home to \$100,000.00 and the amount of the secured claim to \$89,000.00.

The proposed plan, which was filed January 28, 2005, was for a period of 60 months. The plan treated Wells Fargo as a secured creditor holding a lien in the home and proposed to pay the regular mortgage payment to Wells Fargo of \$730.00 per month. The plan also proposed to pay Wells Fargo an arrearage on the mortgage debt in the sum of \$12,000.00 at the rate of \$200.00 per month.

Castle was never scheduled as a creditor and never received any notice, formal or informal, that its interest in the home was being adjudicated by the terms of the Chapter 13 plan. However, by February 3, 2005, Castle was aware that the Debtor had filed for bankruptcy. (Tr. at 11-12; Debtor's Ex. 2.)

On February 4, 2005, Bruce Cook, an owner of Castle, wrote the Debtor's attorney, enclosed a copy of the trustee's deed to Castle, and offered to lease the home to the Debtor for \$1000.00 per month. (Debtor's Ex. 3.) The letter proceeded to demand that the Debtor vacate the premises on or before March 4, 2005, if the lease terms were not acceptable. Id. The record

does not reflect that the Debtor responded in any manner to the demand letter.

Subsequent to the events described above, the Debtor's plan of reorganization under the provisions of Chapter 13 proceeded as if the foreclosure sale had not occurred. The plan to retain ownership of the home, pay the regular note payment, and pay the arrearage to Wells Fargo was confirmed without objection on March 22, 2005. (Debtor's Ex. 7.)

On April 19, 2005, Castle filed a motion for relief from the automatic stay, alleging that it was the owner of the home and that it became the owner prior to the date the Debtor's bankruptcy petition was filed.

### ARGUMENT

The Debtor argues that Castle is bound by the terms of the confirmed plan because Castle had actual notice of the pending bankruptcy case in time to file an objection to confirmation and failed to object. The Debtor also argues that the statutory foreclosure sale is invalid because notice of the sale was published in The Daily Record, a newspaper that does not meet the requirements for publication of a foreclosure pursuant to Arkansas Code Annotated 16-3-105 (Michie 2003).

Castle argues that it is not bound by the confirmed plan because it is not a creditor, and it did not have sufficient notice of its treatment in the plan to satisfy due process. Castle also argues that the statutory foreclosure sale was valid under Arkansas law, and, therefore, the property in question is not property of the estate.

### DISCUSSION

The provisions of subsections 1322(b)(2), (3) and (5) of Title 11 permit a debtor to cure a default in a mortgage secured by a lien in the Debtor's principal residence. However, the

Bankruptcy Code also provides that:

(c) Notwithstanding subsection (b)(2) and applicable nonbankruptcy law —

(1) a default with respect to, or that gave rise to, a lien on the debtor's principal residence may be cured under paragraph (3) or (5) of subsection (b) until such residence is sold at a foreclosure sale that is conducted in accordance with applicable nonbankruptcy law; . . .

11 U.S.C. § 1322(c)(1) (2000).

This Court has previously determined in In re Tomlin that section 1322(c)(1) refers to the point at which a foreclosure sale is final under state law. In Tomlin, the Court held that under state law existing at that time, a sale did not become final until the trustee's deed or mortgagee's deed was recorded. In re Tomlin, 228 B.R. 916, 921 (Bankr. E.D. Ark. 1999).

Since Tomlin, the Statutory Foreclosure Act of 1987 has been amended, and Arkansas law now provides that "(8)'Sale' means the public auction conducted pursuant to § 18-50-107 and shall be deemed concluded when the highest bid is accepted by the person conducting the sale." Ark. Code Ann. § 18-50-101(8) (Michie 2003). Neither party to this proceeding argues that the sale was not final in this case for purposes of 11 U.S.C. § 1322(c)(1).<sup>1</sup>

The Debtor argues that because the confirmed plan listed Wells Fargo as the secured creditor holding a first lien on the home and proposed to cure the arrearage and pay the

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<sup>1</sup> Although the definition of sale contained in Title 18 of Chapter 50 of section 101 is unambiguous, it conflicts with other provisions of the Statutory Foreclosure Act. For instance, section 107(e)(1) of the Act provides that the purchaser at the sale shall be entitled to immediate possession of the property and further provides for a cause of action to obtain a writ of assistance ex parte under section 107(e)(2)(A). However, the section also requires the purchaser to attach a copy of the recorded Trustee deed or Mortgagee deed as a predicate to maintaining the cause of action for possession. Also, section 116(e)(1) of the Act authorizes the trustee to set aside a sale and return the purchase price "[a]t any time prior to delivery of the trustee's or mortgagee's deed. . . ." These two provisions strongly imply that a sale is in substance not actually concluded, as stated in the definition of "sale", until the deed is recorded.

indebtedness, the principle of res judicata applies and binds Castle to the terms of the plan. As authority, the Debtor cites this Court's opinions in In re Ramey, 301 B.R. 534 (Bankr. E.D. Ark. 2003) and In re Smith, 142 B.R. 862 (Bankr. E.D. Ark. 1992), as well as other case law.

However, the Debtor's argument fails to take into account that Castle is not and never has been a creditor of the Debtor. All of the cases cited by the Debtor concern creditors of the Debtor. The Chapter 13 cases cited by the Debtor involve creditors who failed to object to confirmation of a plan and, thus, became bound by the principle of res judicata even though their treatment in the plan was contrary to the provisions of Title 11. See, e.g., In re Ramey, 301 B.R. 534, 545 (Bankr. E.D. Ark. 2003) (holding that secured creditor's treatment in the plan as unsecured was res judicata where creditor had notice of its treatment and failed to object). See, generally, 3 Keith M. Lundin, Chapter 13 Bankruptcy § 233.1 (3<sup>rd</sup> ed. 2000 & Supp. 2004) (footnotes omitted).

Castle did learn that the Debtor had filed a Chapter 13 petition after the auction of the home, but was never listed as a creditor and had no notice of any kind, formal or informal, that its interest in the home was being challenged. Therefore, any attempt by the plan to divest title to the home is void for lack of due process. Piedmont Trust Bank v. Linkous (In re Linkous), 990 F.2d 160, 162 (4<sup>th</sup> Cir. 1993) (stating that confirmed plan was not binding on creditors if order was entered without notice to creditors and opportunity to object). Cf. In re Ruehle, 296 B.R. 146, 164 (Bankr. N.D. Ohio 2003)(holding that due process requires that student loan creditor receive notice reasonably calculated to apprise the creditor that its rights may be altered), aff'd, 307 B.R. 28 (B.A.P. 6<sup>th</sup> Cir. 2004), aff'd, 412 F.3d 679 (6<sup>th</sup> Cir. 2005). See, also, 3 Keith M. Lundin, Chapter 13 Bankruptcy § 232.1 (3<sup>rd</sup> ed. 2000 & Supp. 2004) (stating that

when notice is insufficient to inform creditors that rights are at risk, courts have limited effects of confirmation) (footnotes omitted).

The Debtor's remaining argument that the non-judicial sale should be set aside because it did not conform to the requirements of the statute constitutes a collateral attack on the validity of the sale. Irregularities in a foreclosure proceeding are subject to judicial review in the state court. Ark. Code Ann. § 18-50-116(d) (Michie 2003).<sup>2</sup> See, e.g., Henson v. Fleet Mortg. Co., 319 Ark. 491, 892 S.W.2d 250 (1995)(holding that irregularities in foreclosure sale required that the sale be set aside); Union Nat'l Bank v. Nichols, 305 Ark. 274, 807 S.W.2d 36 (1991) (holding foreclosure sale was invalid because notice of default and intention to sell was not timely mailed).

Whether the sale should be set aside should be determined in a proceeding brought in the appropriate state court. In re Henson, 157 B.R. 867, 869 (Bankr. W.D. Ark. 1993); In Re Matlock, 154 B.R. 721, 723 (Bankr. E.D. Ark. 1993). Although this Court has jurisdiction to determine what is property of the estate, in the interest of comity and pursuant to 28 U.S.C. § 1334(c)(1), the Court abstains from determining the state law issue of whether the foreclosure was valid under the Statutory Foreclosure Act. In re DiMartino, 144 B.R. 225, 226 (Bankr. D.R.I. 1992) (stating that fundamental issue in deciding whether bankruptcy court should abstain is which forum is better suited to adjudicate present dispute between the parties).

Therefore, for the reasons stated, the provisions of 11 U.S.C. § 362 do not apply and no

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<sup>2</sup> The statute acknowledges that the Statutory Foreclosure Act does not impair the rights of persons or entities "to assert . . . legal and equitable rights in a court of competent jurisdiction . . . [p]rovided . . . that any such claim or defense shall be asserted prior to the sale or be forever barred and terminated." Ark. Code Ann. §18-50-116(d)(2)(B) (Michie 2003).

stay became effective when this case was filed because the home was not property of the estate, Castle was not a creditor of the Debtor, and the confirmed plan cannot bind Castle to a contrary result.

IT IS SO ORDERED.



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JAMES G. MIXON  
UNITED STATES BANKRUPTCY JUDGE

DATE: 12/13/05

cc: Cade L. Cox, Esq.  
David D. Coop, Esq., Trustee  
Michael Knollmeyer, Esq.  
Debtor