

THIS OPINION NOT INTENDED FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION



In re:) Case No. 04-15263
)
ADVANCED MACHINE) Chapter 7
CONTROLS, INC.,)
)
Debtor.) Judge Pat E. Morgenstern-Clarren
)
) **MEMORANDUM OF OPINION**

When the chapter 7 trustee filed his final report, creditor JP Morgan Chase Bank, NA fka Bank One, NA objected to it. The ground for objection is that the trustee treated the bank’s claim as secured when it was actually unsecured and thus eligible to participate in the distribution to unsecured creditors. The trustee responds that he treated the claim as secured because that is how it was filed. (Docket 36, 37, 40, 41). For the reasons stated below, the objection is treated as a motion for leave to amend the proof of claim and as such is granted.

JURISDICTION

Jurisdiction exists under 28 U.S.C. § 1334 and General Order No. 84 entered by the United States District Court for the Northern District of Ohio. This is a core proceeding under 28 U.S.C. §§ 157(b)(2)(A) and (O).

STIPULATED FACTS¹

1. On or about May 8, 1998, Debtor obtained a loan from Bank One in the principal amount of \$35,000.00. The loan is evidenced by a Promissory Note dated May 8, 1998, which Debtor executed and delivered to Bank One (the “\$35,000 Note”).

¹ Docket 42.

2. To secure payment of the Note and performance of other terms contained in it, Debtor executed and delivered to Bank One a Commercial Security Agreement (the “Security Agreement”), which granted Bank One a security interest in all of the Debtor’s inventory, chattel paper, accounts, equipment and general intangibles (the “Collateral”). Bank One properly perfected its security interest by filing financing statements with the appropriate state and local recorders.

3. On or about June 14, 1999, Debtor executed a Promissory Note in the amount of \$48,000.00 (the “\$48,000 Note”), which was a renewal and/or extension of the \$35,000 Note.

4. Debtor defaulted on repayment of the \$48,000 Note.

5. Debtor filed its petition in bankruptcy on April 28, 2004.

6. The Debtor indicated on Schedule B of its Petition that it possessed \$11,692.97 as cash on hand from undeposited funds, \$300.00 in a checking account, \$900 in an account receivable from Lubriquip, \$9,104.25 from a 1998 Chevy Blazer, \$20,000.00 in equipment, and \$1,400 in shop equipment. The total value of Bank One’s collateral per the Schedule B was \$24,292.97. Bank One was listed as a secured creditor with a claim of \$47,897.79 on Schedule D.

7. The Trustee claims that Bank One made no efforts to collect its claim against the Debtor for multiple months prior to the commencement of the Debtor’s Chapter 7 case. The Trustee claims that Bank One did not react to the Notice of Chapter 7 Filing with respect to the Debtor’s bankruptcy case, until a time after the 341 Meeting, and then only after the Trustee made multiple calls to various Bank One offices and locations in an effort to determine whether any funds remained owing by the Debtor to Bank One and if Bank One was intending to make a

claim as a holder of a debt secured by property of the estate, as the Debtor's Schedules, which the Trustee had reviewed, indicated that Bank One had a secured claim and that part of its claim was unsecured.

Bank One believes that none of the alleged facts with respect to Bank One's pre-petition conduct are pertinent to the issue at hand.

8. On May 11, 2004, Bank One filed its original secured Proof of Claim ("Original Proof of Claim") for \$47,897.79. A true and accurate copy of the Original Proof of Claim (without exhibits) is attached hereto as Exhibit A. (Emphasis omitted).

9. The Debtor indicated on Schedule B of its Petition that it possessed \$11,692.97 as cash on hand from undeposited funds. These funds were proceeds from accounts receivable in which Bank One possessed a valid security interest. Although Bank One asserted an interest in all of the funds as proceeds of its accounts receivable, the Trustee requested that he be paid a surcharge for his handling of the funds. Bank One agreed to this, and the Trustee paid \$10,330.74 to Bank One on account of the undeposited funds. On October 13, 2004, counsel for Bank One sent the Trustee a letter, a copy of which is attached hereto as Exhibit B, wherein he indicated that Bank One's acceptance of the funds from the accounts receivable would be "without prejudice to filing a proof of claim in the estate." (Emphasis omitted). As such, the Trustee should have anticipated that Bank One intended to participate as an unsecured creditor in any distributions from the estate.

10. The claims bar date was November 3, 2004.

11. On November 3, 2004, Chase² timely filed an amended Proof of Claim (“Proof of Claim”) for \$38,371.88, indicating the application of \$10,330.74 to the claim. A true and accurate copy of the Proof of Claim is attached hereto as Exhibit C. (Emphasis omitted). Although this Proof of Claim amended the Original Proof of Claim filed on May 11, 2004, the notation of “amended” was inadvertently omitted, and the Proof of Claim was filed as an original. Chase subsequently filed a Withdrawal of the Original Proof of Claim as duplicative of the Proof of Claim.

12. On November 5, 2004, Bank One filed a Motion for Relief from Stay and Abandonment (“Motion”), so that the equipment portion of its collateral could be liquidated. The Motion was amended on December 22, 2004. On January 18, 2005, Chase obtained an Order for Relief from Stay and Abandonment.

13. Chase thereafter liquidated the equipment portion of the Collateral and obtained \$2,000.00. A copy of the secured party sale notice that Chase sent to the Trustee is attached hereto as Exhibit D.

14. Chase filed an Amended Proof of Claim on February 11, 2005 (“Amended Proof of Claim”) amending its Proof of Claim from \$38,671.88 to \$36,371.88 to indicate the application of the proceeds from the liquidation of the remaining Collateral. Chase also amended the Proof of Claim from secured to unsecured, to indicate the deficiency amounts as all of the collateral had been liquidated. A true and accurate copy of the Amended Proof of Claim is attached hereto as Exhibit E. (Emphasis omitted).

15. No objection has been filed to any of Chase’s proofs of claim.

² Chase is the successor by merger to Bank One, NA.

16. The Trustee filed his Final Report and Account with the Court on February 11, 2005. The Final Report shows that the Trustee has funds on hand of \$9,711.94. The Trustee seeks compensation of \$2,778.07, to which no party objects. The balance of \$6,933.87 is proposed to be paid to three unsecured creditors with claims totaling \$18,420.62, resulting in a 37.641% dividend to unsecured creditors. Chase is seeking to be paid on its unsecured claim of \$36,371.88.

17. The Trustee did not propose to pay any funds to Chase on account of its unsecured claim, the proof of which was not filed until after the bar date and after the Trustee had filed his Final Report which had been reviewed by the Office of the U. S. Trustee.

18. Chase filed an Objection to the Final Report on February 15, 2005. A hearing was held on March 10, 2005 at which time the Court requested briefs be submitted.

19. Chase filed a Supplemental Objection on March 22, 2005, and the Trustee filed a timely Response on April 16, 2005.

20. There is no confirmed plan of reorganization to be protected in this matter.

21. No distribution has been made to unsecured creditors. Chase is not seeking to amend its claim after any distribution to other creditors has been made.

22. Chase did not act with intent to delay in filing its Amended Proof of Claim. At the time of the claims bar date, Chase had yet to fully liquidate all of its collateral.

23. Chase has the largest amount of unsecured debt at stake and would account for approximately two-thirds of the total claims pool if its unsecured claim is allowed. As the Trustee has \$6,933.87 on hand to distribute, the three other unsecured creditors will receive more

on account of their claims than they would if Chase were allowed to participate in the unsecured claims distribution.

24. All of the Exhibits attached hereto are either documents of which the Court can take judicial notice or are admissible business records of Chase. Neither party hereto has any objection to the introduction of the Exhibits as evidence in this contested matter.

THE POSITIONS OF THE PARTIES

The parties agree that the February 11, 2005 amended proof of claim was filed after the bar date. The bank did not seek leave to file an untimely, new claim. Instead, it argues that the February 11, 2005 proof of claim amends the timely filed November 3, 2004 claim.³ The bank contends that the February 11, 2005 filing is a true amendment because it corrects a defect in or describes the original claim with greater particularity. Thus, the amendment should be accepted and the claim allowed as unsecured. The bank argues further that equity favors its position.

On the other hand, the trustee maintains that the February 11, 2005 proof of claim is not an amendment but is instead a new claim because it changes the claim status from secured to unsecured. If it is a new claim, it is undeniably late filed and should be disallowed. The trustee emphasizes that the bank did not file the February 11, 2005 proof of claim until after he filed his final report. If the claim is now allowed as unsecured, the trustee will have to file an amended report and renotice it. This, he says, is inequitable because it will disturb and delay the orderly administration of the case.

³ As noted in the stipulations, the bank actually filed three proofs of claim, but the first one quickly became irrelevant.

DISCUSSION

The bank filed one proof of claim before the bar date and a second proof of claim after the bar date. The timely filed proof of claim is the one used by the trustee in his final report. The question is whether the second filing should be treated as an amendment to the timely claim. If it is a permissible amendment, the bank will participate in the dividend to unsecured creditors. If it is not, the bank will not recover any funds beyond those it received from liquidating its collateral.

When a party seeks to amend a proof of claim under these circumstances, courts apply a two-part test:

- (1) does the amendment reasonably relate to the timely filed claim or is it an attempt to file a new claim; and
- (2) would allowing the amendment be equitable under the circumstances.

In re Lee Way Holding Co., 178 B.R. 976, 979 (Bankr. S.D. Ohio 1995).

On the first point, an amendment relates to the original claim if it cures a defect or describes the claim with greater particularity or pleads a new theory of recovery based on the facts of the original claim. *Id.* Here, the bank contends that its amendment either corrects a defect in the original or describes it with greater particularity. The bank does not identify a defect that is corrected and the court will not, therefore, consider that argument further. The contention that the amendment describes the original with greater particularity has merit.

The history of interaction between and among the debtor, the bank, and the trustee shows that from the beginning of the case the parties in interest understood the bank to be a secured creditor but for less than the full amount of the debt due to the collateral value at the time of the bankruptcy filing. The debtor scheduled the bank as a secured creditor with a claim of

\$47,897.79. The schedules also show the bank's security with a value of \$22,300.00. On May 11, 2004, the bank filed a secured claim for \$47,897.79. About five months later, the trustee and the bank resolved questions relating to the bank's accounts receivable collateral. Under the settlement, the trustee retained his statutory commission from the funds and then paid \$10,330.74 to the bank, without prejudice to the bank filing a proof of claim. On November 3, 2004, the bank filed an amended proof of claim in which it reduced its claim by the \$10,330.74 received and withdrew the first claim. The bank then filed a motion for relief from stay to liquidate the equipment portion of its collateral. On November 15, 2004, the bank notified the trustee and other parties in interest of the intended sale. Eventually, the bank realized \$2,000.00 from the equipment sale.

This is the point in the scenario where things fall apart. If, as seems apparent, the bank had liquidated all of its collateral as of that date, it should have filed another amended proof of claim for the unsecured balance of the debt. At the same time, the trustee, knowing the bank was in all likelihood undersecured, could have gotten back in touch with the bank to clarify the situation. Neither one did so. Instead, on December 14, 2004, the trustee submitted his final report to the United States trustee for review, treating the bank as secured (and thus ineligible to participate in the unsecured dividend). On February 11, 2005, the United States trustee filed the final report with the court and served it on the creditors, including the bank. Immediately upon receiving that wakeup call, the bank filed an amended proof of claim providing the final piece of information needed to process its claim and objected to the report. Given the history of communication and activity between the bank and the trustee, the court finds that this amendment does not state a new claim but instead describes the original claim with greater

particularity; i.e., having liquidated its collateral and found itself undersecured, the bank is asserting an unsecured claim for the balance of the same debt.

The second point is whether allowing the amendment would be equitable under the circumstances. The analysis includes these factors:

- (1) whether there is undue prejudice to an opposing party;
- (2) whether other claimants will be prejudiced;
- (3) whether the claimant has justified the inability to file the amended claim when the original claim was filed;
- (4) whether there is bad faith or dilatory behavior on the part of the claimant; and
- (4) whether other creditors would receive a windfall if the amendment is disallowed.

In re Lee Way Holding Co. 178 B.R. at 979-980.

The trustee argues that if the amendment is allowed, he will have to amend his final report and renotice it. The bank counters that no party has detrimentally relied on the final report, no distribution has been made, and the other creditors would receive a windfall if the bank is excluded. Also, it could not have filed the original claim as unsecured because it did not know the amount to which it would be unsecured until it liquidated the collateral. The bank does acknowledge that the distributions to other creditors will be delayed through its failure to file the amendment earlier.

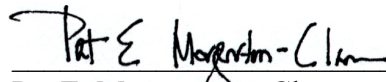
This situation presents a close call because the bank did delay; it certainly had it within its power to act earlier, which would have saved everyone time and money. Allowing the claim at this point will not, however, unduly prejudice any other party in interest. Filing and noticing an

amended final report in this relatively simple chapter 7 is a small task for the trustee. The delay to the other creditors is most unfortunate, but will be relatively short. Barring the bank from receiving its dividend would result in a windfall to other unsecured claimants. All in all, equity favors permitting the bank to amend its claim under the unusual circumstances of this case.⁴

CONCLUSION

For the reasons stated, the objection of JP Morgan Chase Bank, NA to the trustee's final report is treated as a motion for leave to file amended proof of claim and as such is granted. A separate order will be entered reflecting this decision.

Date: 2 August 2005



Pat E. Morgenstern-Clarren
United States Bankruptcy Judge

To be served by clerk's office email and the Bankruptcy Noticing Center

⁴ The trustee has argued that the issue is whether the trustee or the creditor has the burden of filing a motion to value a secured interest under 11 U.S.C. § 506. The court does not view that as the decisive legal issue and will not, therefore, address it.

THIS OPINION NOT INTENDED FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

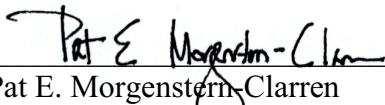


In re:) Case No. 04-15263
)
ADVANCED MACHINE) Chapter 7
CONTROLS, INC.,)
)
Debtor.) Judge Pat E. Morgenstern-Clarren
)
) **ORDER**

For the reasons stated in the memorandum of opinion issued this same date, the objection of JP Morgan Chase Bank, NA to the trustee's final report is treated as a motion for leave to file an amended proof of claim and as such is granted.

IT IS SO ORDERED.

Date: 2 August 2005



Pat E. Morgenstern-Clarren
United States Bankruptcy Judge

To be served by clerk's office email and the Bankruptcy Noticing Center