SO ORDERED,

Judge Jason D. Woodard

United States Bankruptcy Judge

The Order of the Court is set forth below. The case docket reflects the date entered.

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF MISSISSIPPI

In re:	)		
	)		
EMILY D. JONES,	)	Case No.	15-12254-JDW
	)		
Debtor.	)	Chapter	13

ORDER (1) GRANTING MOTION TO COMPROMISE, AND (2) DENYING SUBSTITUTION OF COLLATERAL (DKT. # 64)

This cause comes before the Court on the *Motion to Compromise, Authorize Settlement and to Authorize Substitution of Collateral* (the "Motion")(Dkt. # 64) filed by the debtor Emily Jones (the "Debtor"), and the *Response* (Dkt. # 67) filed by Garrison Used Cars (the "Creditor"). The Debtor's vehicle, which is the collateral for the Creditor's secured debt, has been totaled and the Debtor seeks to use the insurance proceeds to buy a new vehicle. The Debtor proposes to substitute the new vehicle as the collateral for the Creditor's secured debt. The Creditor objects to the substitution of collateral and requests that the insurance proceeds be paid to it as the loss payee under the insurance policy.

At the hearing on September 8, 2016, Bridgette Davis appeared on behalf of the Debtor and Edwin Priest appeared on behalf of the Creditor. Both parties presented argument and at the conclusion of the hearing the Creditor was allowed to file a supplemental brief citing the case law for his position. The Court has considered the Motion, the Creditor's Response to the Motion, and the supplemental brief of the Creditor. In addition, the Court has considered the record in this case, the arguments of counsel, and the applicable law. For the reasons set forth below, the Court finds that the insurance proceeds are not property of the estate and the Debtor is not allowed to substitute collateral over the objection of the Creditor.

I. JURISDICTION

This Court has jurisdiction pursuant to 28 U.S.C. §§ 151, 157(a) and 1334(b) and the United States District Court for the Northern District of Mississippi's Order of Reference of Bankruptcy Cases and Proceedings Nunc Pro Tunc Dated August 6, 1984. This is a core proceeding arising under Title 11 of the United States Code as defined in 28 U.S.C. § 157(b)(2)(A), (M), and (O).

II. FACTS

The pertinent facts in this case are brief and undisputed. The Debtor filed her chapter 13 bankruptcy petition on June 25, 2016 (Dkt. # 1). In her schedules, the Debtor claimed ownership of a 2006 Dodge Charger (the "Vehicle"), and listed the Creditor as having a secured claim of $7,100 that is collateralized by the Vehicle (Dkt. # 12). As required by the financing contract, the Debtor had insurance on the Vehicle and the Creditor is named as the loss payee. On August 10, 2015, the

Creditor filed a proof of claim that asserted its secured claim was a "910 claim"[1] in the amount of $10,079 (Claim # 1-2). Shortly thereafter, the Debtor filed an *Objection to Claim of Garrison Used Cars* (Dkt. # 26), claiming that "the net balance or payoff balance of the claim was approximately $7,100" on the petition date. No response was filed to this objection.

The Debtor's chapter 13 plan was confirmed on December 21, 2015 (Dkt. # 54). Pursuant to the confirmed plan, the Debtor is to pay the Creditor $7,100 plus 5% interest over the life of the plan for the Vehicle (Dkt. # 54).

After plan confirmation, the Vehicle was totaled in a car accident (Dkt. # 64). The insurance provider agreed to pay $6,384 as the value of the totaled Vehicle. The Debtor filed the Motion, seeking approval of the compromise with the insurance company and approval to use the proceeds to buy a new car and to substitute the new car as collateral for the Creditor's secured claim.

III. ANALYSIS

The central question before the Court is whether the insurance proceeds are property of the estate. If the insurance proceeds are property of the estate then the Debtor may, under certain circumstances, use the proceeds to purchase a new car with the approval of the Court pursuant to § 363 of the Bankruptcy Code.[2] If the

[1] A "910 claim" refers to a claim of a creditor who has a purchase money security interest in a vehicle that was purchased by the debtor within 910 days of filing the bankruptcy petition. The flush language found at the end of § 1325(a) provides that § 506 does not apply to "910 claims." Consequently, the debtor must pay the full amount owed of the debt, rather than having the option of paying the value of the collateral plus interest.

[2] All statutory references are to Title 11, United States Code (the "Bankruptcy Code" or "Code"), unless otherwise noted.

insurance proceeds are not property of the estate, then the Debtor would have to obtain the Creditor's consent in order to use the proceeds. Section 541(a) provides that an estate is created as of the commencement of the case that is comprised of "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a). "Proceeds . . . of or from property of the estate" are also included in the bankruptcy estate. 11 U.S.C. § 541(a)(6). But not all proceeds are property of the estate.

A closer look at the meaning of "proceeds" is necessary for clarifying the precise definition ascribed thereto. The Senate and House Reports for § 541(a)(6) explains the main thrust of the provision: "[t]he conversion in form of property of the estate does not change its character as property of the estate." S.Rep. No. 989, 9th Cong., 2d Sess. 83 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5869; H.R.Rep. No. 595, 95th Cong., 1st Sess. 368 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6324. Another statement explaining the scope of § 541 also helps clarify § 541(a)(6): section 541 "is not intended to expand the debtor's rights against others more than they exist at the commencement of the case." S.Rep. No. 989 at 82, 1978 U.S.C.C.A.N. at 5868; H.R.Rep. No. 595 at 367, 1978 U.S.C.C.A.N. at 6323. Accordingly, the purpose of § 541(a)(6) is not to capture proceeds that the debtor was never entitled to receive, but instead it "maintains the value of the estate to the extent that property which is property of the estate is converted to some other form." *Landry v. Exxon Pipeline Co.,* 260 B.R. 769, 799 (Bankr. M.D. La. 2001).

The Court of Appeals for the Fifth Circuit has long held that "when the debtor has no legally cognizable claim to the insurance proceeds, those proceeds are not property of the estate." *Matter of Edgeworth*, 993 F.2d 51, 56 (5th Cir. 1993). Stated another way, the "central question when determining whether insurance proceeds associated with a policy are property of the bankruptcy estate is whether, in the absence of the bankruptcy proceeding, the proceeds of the policy would belong to debtor when the insurer pays a claim." *In re Equinox Oil Co., Inc.,* 300 F.3d 614, 618 (5th Cir. 2002). The rationale being that "[w]hen payment by the insurer cannot inure to the debtor's pecuniary benefit, then that payment should neither enhance nor decrease the bankruptcy estate." *Edgeworth,* 993 F.2d at 55-56. As a result, if an insurance policy lists a creditor or third party as the loss payee, the proceeds will not be part of the bankruptcy estate to the extent of the secured creditor's claim.

This Court has previously addressed a similar issue and applied the same Fifth Circuit precedent. *See In re Bailey,* 314 B.R. 103 (Bankr. N.D. Miss. 2004). In *Bailey*, the creditor and trustee agreed that the insurance proceeds up to the amount of the creditor's secured claim were to be paid to the creditor because under the insurance policy the proceeds had been assigned to the creditor. *Id.* at 104. The Court then considered whether the excess insurance proceeds—those proceeds left over after paying the creditor's secured claim as fixed by the chapter 13 plan—were owed to the creditor as well. The Court examined the Fifth Circuit cases previously mentioned and held that because of the assignment provision in the insurance

policy, the insurance proceeds were not property of the estate. Therefore, the proceeds were to be paid to the creditor.[3]

The majority of the courts that have addressed an issue similar to the one before this Court have agreed with this reasoning—that where a debtor is not entitled to receive the proceeds of an insurance policy, § 541(a)(6) does not create new rights for the bankruptcy estate. *In re Huff,* 322 B.R. 661, n. 21 (Bankr M.D. Ga. 2005)(compiling cases); *Bailey,* 314 B.R. at 106; *Carey v. Gen. Motors Acceptance Corp. (In re Carey),* 202 B.R. 796 (Bankr. N.D. Ga. 1996); *In re Shamburger,* 189 B.R. 965 (Bankr. N.D. Ala. 1996); *In re Suter,* 181 B.R. 116 (Bankr. N.D. Ala. 1994). As such, where a creditor is named as loss payee under an insurance policy and is entitled to receive the insurance proceeds when the collateral is destroyed, the proceeds are not property of the estate and the debtor cannot force substitution of collateral over the objection of the creditor. The main case relied on by the Debtor also bears this out. *See In re Coker,* 216 B.R. 843, 848-53 (Bankr. N.D. Ala. 1997).

The court in *Coker* recognized that where a secured creditor is designated as loss payee, "its right to insurance proceeds is superior to the debtor's rights." *Id.* at 848.[4] Two other cases were cited by the Debtor to bolster her position that insurance proceeds are property of the estate: *In re Young* and *In re Granville*.

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[3] This issue is not before the Court here. *See also Ford Motor Credit Co. v. Stevens (In re Stevens),* 130 F.3d 1027 (11th Cir. 1997). There are no excess proceeds in the instant case. After payment of all proceeds to the Creditor, the Creditor will have an unsecured deficiency claim.

[4] *Coker* agreed with the general principle that a loss payee is entitled to the proceeds. However, in *Coker*, the secured creditor was not named as a loss payee and so the debtor prevailed. *Coker* is distinguishable based on this very material fact.

Young, 2000 WL 33673801 (Bankr. M.D. N.C. June 21, 2000); *Granville,* 2014 WL 1347039 (Bankr. E.D. Ky. Apr. 4, 2014). Both of these cases are also distinguishable, however. In *Young*, the parties agreed that the proceeds were property of the estate, so the court never decided that issue. 2000 WL 33673801 at *2. Rather, the question there was whether the creditor "violated the stay in delaying the substitution of collateral." *Id.* at *3. Likewise, in *Granville*, the court dealt with a difference set of facts. 2014 WL 1347039 at *1. The debtor's car was totaled in an accident caused by a third party. *Id.* The court likened the third party's actions to a tort against the debtor and found that the fact the third party's insurer was making the payment to the debtor was immaterial. *Id.* at *2. The "proceeds" were due to the debtor because a tort was committed against the debtor and the debtor was entitled to compensation. *Id.*

Here, the Debtor took out an insurance policy on the Vehicle and named the Creditor as the sole loss payee. The Vehicle has been totaled, and the insurer is ready to write a check for $6,384 as the net payout for the Vehicle. Because the Creditor is the loss payee, it is entitled to receive the check from the insurer. If not for the bankruptcy filing, there would be no question as to who owns the insurance proceeds. According to Fifth Circuit precedent, the Debtor does not have a legally cognizable interest in the insurance proceeds and, thus, those proceeds are not property of the estate.

IV. CONCLUSION

The insurance proceeds are owed to the Creditor per the insurance policy and do not constitute property of the estate. Accordingly, the Debtor must have the Creditor's consent in order to use the proceeds to purchase a new vehicle and to substitute new collateral. Here, the Creditor has firmly rejected such a proposal.[5] Therefore, the Debtor may not use the insurance proceeds against the will of the Creditor and the Motion is due to denied. Accordingly, it is hereby

ORDERED, ADJUDGED, and **DECREED** that the Motion (Dkt. # 64) is **GRANTED IN PART** and **DENIED IN PART.** The Motion is **GRANTED** to allow the settlement with the insurance company, but **DENIED** as to distribution of the insurance proceeds to the Debtor and substitution of collateral. The insurance proceeds must be tendered to the Creditor.

##END OF ORDER##

[5] It is not uncommon for Debtors to file similar motions to substitute collateral. Today's ruling is not an outright prohibition on substitution of collateral if the creditor consents.