UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NEW YORK

In Re:

Case No. 92-21236

Axial Properties North II,

DECISION & ORDER

Debtor.

BACKGROUND

On May 4, 1992, the Debtor, Axial Properties North II (the "Debtor"), filed a petition initiating a Chapter 11 case. As required by Rule 1007, the petition was accompanied by a list of creditors and a mailing matrix (the "Matrix"), but it was not accompanied by the required schedules and statements. The Matrix listed Betlem Residential ("Betlem") as a creditor at 204 Clinton Avenue, Rochester, New York, 14620. On June 2, 1992, the Debtor filed the required schedules which also listed Betlem at 204 Clinton Avenue and as a secured creditor with a mechanic's lien on 120 East Avenue, Rochester, New York in the amount of $35,235.54, but the schedules further indicated that Betlem's claim was disputed.

On May 11, 1992, a Section 341 Meeting Notice (the "Section 341 Meeting Notice") was sent by the Court to the creditors listed by the Debtor on the Matrix. This Notice informed these creditors of the filing of the Debtor's Chapter 11 case and various other matters, including their obligation to file a proof of claim if

their claim was listed as disputed, contingent or unliquidated.[1]

On May 21, 1992, the Court forwarded to the attorneys for the Debtor a notice (the "Deficiency Notice") which advised the attorney of three creditors whose Section 341 Meeting Notice had been returned by the Post Office for an insufficient or incorrect address. The Deficiency Notice listed Betlem as one of the creditors whose Section 341 Meeting Notice had been returned. On May 26, 1992, the attorneys for the Debtor filed with the Court an Affidavit indicating that on May 21, 1993 a copy of the Section 341 Meeting Notice had been sent by the attorneys to Pierce, Basinger, Bach, Ltd. ("Pierce"), one of the creditors listed on the

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1 A portion of the Section 341 Meeting Notice read:

> PROOF OF CLAIM. Schedules of creditors have been or will be filed pursuant to Bankruptcy Rule 1007. Any creditor holding a scheduled claim which is not listed as disputed, contingent, or unliquidated as to amount may, but is not required to, file a proof of claim in this case. Creditors whose claims are not scheduled or whose claims are listed as disputed, contingent, or unliquidated as to amount and who desire to participate in the case or share in any distribution must file their proofs of claim. A creditor who desires to rely on the schedules of creditors has the responsibility for determining that the claim is listed accurately. If the court sets a deadline for filing a proof of claim, you will be notified. The place to file a proof of claim, either in person or by mail, is the office of the clerk of the bankruptcy court. Proof of claim forms are available in the clerk's office of any bankruptcy court.

Deficiency Notice, at a corrected address. The Affidavit did not indicate that a copy of the Section 341 Meeting Notice had been mailed to Betlem at a corrected address. Thereafter, as is the practice of this Court, the Matrix was amended to reflect the corrected address for Pierce. The Court records do not indicate that any other request was made to amend the Matrix or the Debtor's schedules to show a corrected address for Betlem, and the Matrix and Court records still show Betlem at 204 Clinton Avenue, Rochester, New York, 14620.

The initial Section 341 meeting was held on June 2, 1992 and adjourned meetings were held on September 22, 1992, November 3, 1992, January 19, 1993, January 26, 1993, March 16, 1993, May 25, 1993, August 3, 1993, and September 28, 1993. The Section 341 meeting minutes filed with the Court show that Betlem was never represented at any of these meetings.

On June 25, 1992, the Office of the United States Trustee (the "U.S. Trustee") appointed a six-creditor committee of unsecured creditors (the "Committee").

A review of the Affidavits of Service filed with the Court in connection with various motions and proceedings in the Debtor's Chapter 11 case indicates an inconsistent history of notice. Several Affidavits of Service indicate that after the appointment of the Committee on June 25, 1992, in accordance with Rule 2002(i) and this Court's practices and procedures, many motions were made

only on notice to the members of the Committee and other necessary parties and not to all creditors. Other Affidavits of Service, such as an October 2, 1992 Affidavit in connection with a motion by the Debtor to use cash collateral and an October 28, 1992 Affidavit in connection with a motion by the Debtor to enter into a utility agreement, indicate that the notices of these motions were not sent by the attorneys for the Debtor to all creditors but were sent to more creditors than just the members of the Committee, fewer creditors than on the list required by Rule 1007(d), and to Pierce at the original address listed for it rather than its corrected address. The notices were not served on Betlem. However, consistent with the Rules, for all motions and proceedings where notice was sent by the Court, Betlem was served at the address on the Matrix and the Debtor's schedules, 204 Clinton Avenue.[2]

On February 11, 1993, the Debtor filed a Disclosure Statement (the "Disclosure Statement") and Plan (the "Plan"). On March 31, 1993, an Order and Notice for Hearing on Disclosure Statement (the "Bar Date Notice") was sent by the Court to the creditors listed by the Debtor on the Matrix, including Betlem at the 204 Clinton

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[2] The Rules do not require it to and the Court does not keep records of returned notices or mailings other than returned Section 341 Meeting Notices. Therefore, there are no Court records indicating whether notices, other than the Section 341 Meeting Notice, which were mailed by the Court to Betlem were returned by the Post Office. This practice is now being revisited by the Court and the Clerk's Office.

Avenue address. The Bar Date Notice informed these creditors that a hearing to consider approval of the Disclosure Statement would be held on May 5, 1993, the last date to file written objections to the disclosure statement was April 30, 1993, and the last day for filing claims was May 5, 1993.

By a June 7, 1993 Order (the "Confirmation Hearing Order"), the Disclosure Statement, with some revisions required by creditors, the U.S. Trustee and the Court, was approved; a date was set for a hearing to consider the confirmation of the Plan; and a date was set for the filing of objections to confirmation. On June 10, 1993, copies of the Confirmation Hearing Order, approved Disclosure Statement and Plan were sent by the Court to the creditors listed by the Debtor on the Matrix, including Betlem at the 204 Clinton Avenue address.

On June 29, 1993, the U.S. Trustee had filed a statement indicating that it had no objection to confirmation. On July 29, 1993, an initial Confirmation hearing was conducted, and the Court considered the only objections to the Plan which had been filed, objections by Chase Manhattan Bank N.A. ("Chase Manhattan") and Horning Construction ("Horning")[3], a creditor which, like Betlem,

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[3] The Plan provided that Betlem and other mechanics lienholders on 120 East Avenue would receive 30% of their allowed claims and contended that their liens were unsecured based on the value of the property and the amount due on prior valid liens. Betlem's claim was listed as disputed on a schedule to the Plan.

held a mechanics lien on 120 East Avenue. Thereafter, the Court allowed a series of adjournments to enable the Debtor to attempt to negotiate a settlement of their objections with Chase and Horning, and on October 27, 1993, the Debtor filed a Second Amended Plan.

At one of the adjourned hearings on confirmation, the Court indicated to the attorney for the Debtor that it required that any and all claims objections be brought before the entry of an order of confirmation. Therefore, on December 20, 1994, the Debtor filed a motion objecting to the claim of Betlem (the "Betlem Claim Objection"), which was finally made returnable by consent on February 9, 1994.

On March 16, 1994, the Debtor filed a Third Amended Plan.[4] On March 31, 1994, at an adjourned confirmation hearing, the Court was advised that Chase and Horning had consented to the provisions of the Third Amended Plan and that a confirmation order had been submitted. The Court took the matter off its Chapter 11 hearing calendar subject to restoration and has not entered the proposed order of confirmation pending its decision on the Betlem Claim Objection.

The Betlem Claim Objection was mailed to Betlem by the attorneys for the Debtor at its 204 Clinton Avenue address, and on January 28, 1994, Betlem, through its attorneys, submitted a

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[4] The Third Amended Plan does not change the treatment of Betlem.

response (the "Betlem Response") in opposition to the Objection.

The Betlem Claim Objection asserted that: (1) In November, 1990 Betlem and the Debtor had entered into negotiations and then an agreement (the "Payment Agreement")[5] concerning the payment of sums due Betlem whereby the Debtor would pay $15,000 on or before November 26, 1990 and then monthly payments of $4,000 beginning December 26, 1990; (2) The Debtor made the initial $15,000 payment by a check dated and alleged to have been delivered on November 28, 1990; (3) Betlem filed a mechanic's lien on December 13, 1990 in the amount of $35,235.54; (4) the mechanic's lien filed by Betlem was willfully exaggerated in violation of New York Lien Law §39 to the extent of $15,000 and the agreement between the Debtor and Betlem; (5) under New York Lien Law §39-a, the Debtor is entitled to recover from Betlem an amount equal to the amount by which the lien was exaggerated plus attorney's fees incurred in proving willful exaggeration; (6) the Debtor scheduled Betlem as a disputed mechanic's lien creditor asserting a claim of $35,235.54 and Betlem did not file a claim in the bankruptcy case by the time allowed by the Court for filing claims (May 5, 1993 as provided in the Bar Date Notice); and (7) the Court should disallow Betlem's claim and

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[5] The Payment Agreement was in the form of a letter on Betlem letterhead dated November 21, 1990. At the bottom of the Agreement in the left margin there is a provision dated November 28, 1990 signed by the Betlem Treasurer indicating that Betlem would do certain additional installation work beginning November 29, 1990.

reserve the Debtor's right to assert its claim for willful exaggeration pursuant to New York Lien Law §39-a.

The Betlem Response asserted that: 1) Betlem rendered goods and services for the improvement of 120 East Avenue and the agreed price and value for those goods and services was $35,235.54; (2) the Debtor failed to pay as originally agreed and a mechanic's lien was prepared for $35,235.54; (3) One of Debtor's principals, Robert Wilson, agreed in writing in November, 1990 that the Debtor would pay $15,000 to Betlem on or before November 26, 1990 and Betlem would forgo filing its mechanic's lien; (4) the payment was untimely made on November 28, 1990 and after cashing the check, Betlem filed its lien with the Monroe County Clerk on December 13, 1990; (5) no credit was given for the untimely $15,000 payment, through inadvertence, and the lien was filed in the amount of $35,235.54 as originally prepared; (6) Betlem commenced an action in New York State Supreme Court to foreclose its lien which was stayed by the commencement of the Debtor's bankruptcy case; (7) there are no grounds to avoid Betlem's duly filed and perfected lien based on the Debtor's argument that the lien was filed in contravention of the November, 1990 agreement, because the initial payment was not made timely under that agreement; and (8) there are no grounds to avoid Betlem's lien as a matter of law based on Debtor's argument that Betlem's lien was willfully exaggerated, since willful exaggeration can only be established in an action or

proceeding to enforce a mechanic's lien and willfulness must be demonstrated.

On March 1, 1994, Garry Brower, Treasurer of Betlem ("Brower"), filed an affidavit (the "Brower Affidavit") with the Court which stated that Betlem rendered goods and services for the improvement of real property located on East Avenue and the agreed price was $35,235.54; the Debtor failed to pay this amount timely and a mechanic's lien was filed in that amount; and the lien was placed for the original amount of $35,235.54 but the lien should have been filed for $20,235.54 since Betlem had received $15,000 from the Debtor. The Brower Affidavit also stated that: (1) Betlem's address has been 704 Clinton Avenue South for the past decade;[6] (2) Betlem never received formal notice of the Chapter 11 case; (3) in January, 1992,[7] Betlem received a copy of a motion by Chase Lincoln and a July, 1993 notice regarding an adjourned confirmation hearing; and (4) Betlem has never received a disclosure statement, or plan, nor had it been notified that the Debtor intended to treat Betlem differently from its other mechanic's lienors.

In a Memorandum of Law, the Debtor asserted that Betlem's

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[6] In fact, the Payment Agreement shows Betlem's address as 704 Clinton Avenue South.

[7] It is assumed that this is a typographical error and that the correct date is January, 1993.

objections to the Plan and Third Amended Plan and treatment of its claim comes too late, because the Court complied with the Bankruptcy Rules regarding the hearing and approval of the Disclosure Statement, noticing the hearings, deadlines for voting and objecting to the Plan and conducting confirmation hearings. The Debtor contends that despite being served with the various hearing notices, Betlem did not vote or object to the Plan and the attorney for Betlem conceded that Betlem did receive the §341 meeting notice and other notices and pleadings in the case, including the Betlem Claim Objection (according to the Debtor, there is no record of any notice being returned to the Bankruptcy Clerk as "addressee unknown"). The Debtor also asserted that Betlem cannot vote on the Plan or Third Amended Plan at this late date since Bankruptcy Rule 3018(a) only allows the Court to permit a creditor to change its vote or withdraw it and not to vote when it has not and there has not been any cause given to allow Betlem to vote outside of the time limits. Further, the Debtor contended that: (1) Bankruptcy Rule 3003(c)(2) bars a creditor who has been scheduled as a disputed claim from voting or receiving a distribution in the case and Betlem took the risk that it would not be left with a claim; (2) the Plan is binding on all creditors; and (3) the Claimant's claim should be disallowed, but afforded the treatment provided in the plan.

DISCUSSION

I. Willful Exaggeration of Filed Mechanics Lien.

The Betlem Claim Objection asserted that Betlem's unfiled claim should be disallowed under Section 39 of the New York Lien Law and that the Debtor is entitled to damages under Section 39-a of the New York Lien Law. Under Section 39,[8] the court is required to declare a lien void and no recovery will be allowed if the court finds that the lienor has wilfully exaggerated the amount which is being claimed. However, under New York law, it is clear that the determination of willful exaggeration may be established only in an action to enforce a mechanic's lien and can not be on affidavits or by submission. *Application of Upstate Builders Supply Corp.*, 37 A.D.2d 901, 902 (1971), *appeal dismissed,* 30 N.Y.2d 515 (1972). The overstatement of a lien as originally filed does not

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[8] Section 39 of the New York Lien Law provides:

> In any action or proceeding to enforce a mechanic's lien upon a private or public improvement or in which the validity of the lien is an issue, if the court shall find that a lienor has wilfully exaggerated the amount for which he claims a lien as stated in his notice of lien, his lien shall be declared to be void and no recovery shall be had thereon. No such lienor shall have a right to file any other or further lien for the same claim. A second or subsequent lien filed in contravention of this section may be vacated upon application to the court on two days' notice.

necessarily render the lien invalid and incapable of amendment. Id. The burden of proof to recover a penalty for willful exaggeration is on the party claiming it. *Goodman v. Del-Sa-Co Foods, Inc.*, 15 N.Y.2d 191, 196 (1965). If the court does find willful exaggeration, then the owner or contractor may get damages to the extent of the willful exaggeration under Section 39-a of the New York Lien Law[9]. *Id.* Therefore, in order for the Debtor to void Betlem's lien under Section 39 and recover damages under Section 39-a, the Debtor must establish in a factual hearing in this Court or in state court that Betlem willfully exaggerated its lien.

II. Failure to File a Claim Within the Time Fixed by the Court.

Bankruptcy Rule 3003(c)(2) requires a creditor whose claim or

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[9] Section 39-a of the New York Lien Law provides:

> Where in any action or proceeding to enforce a mechanic's lien upon a private or public improvement the court shall have declared said lien to be void on account of wilful exaggeration the person filing such notice of lien shall be liable in damages to the owner or contractor. The damages which said owner or contractor shall be entitled to recover, shall include the amount of any premium for a bond given to obtain the discharge of the lien or the interest on any money deposited for the purpose of discharging the lien, reasonable attorney's fees for services in securing the discharge of the lien, and an amount equal to the difference by which the amount claimed to be due or to become due as stated in the notice of lien exceeded the amount actually due or to become due thereon.

interest is scheduled as disputed, contingent, or unliquidated to file a proof of claim within the time prescribed by Bankruptcy Rule 3003(c)(3), which provides that the court will fix and for cause extend the time within which proofs of claim may be filed. If the creditor fails to file a claim within the time period then that creditor "shall not be treated as a creditor with respect to such claim for the purposes of voting and distribution" under Bankruptcy Rule 3003(c)(2). In this case, it is undisputed that Betlem did not file a proof of claim within the time for filing claims (May 5, 1994 as fixed in the Bar Date Notice). Betlem has asserted that it did not receive the Section 341 Meeting Notice or the Bar Date Notice, each of which was sent by the Court to an incorrect street address, 204 Clinton Avenue, instead of 704 Clinton Avenue. The Debtor has asserted that because Betlem received some of the notices in the case, including those acknowledged in the Brower Affidavit and the Betlem Claim Objection sent by the Debtor, there should be a presumption that Betlem received the Bar Date Notice.

The case law is clear that known creditors are entitled to reasonable notice of the bar date for filing proofs of claim, even if the creditor has knowledge of the bankruptcy. *See New York v. New York, New Haven & Hartford Railroad Co.*, 344 U.S. 293, 297 (1953). Where mail is properly addressed, stamped and deposited in the postal system, there arises a rebuttable presumption that

the notice was received by the addressee. *In re STN Enterprises, Inc.*, 94 B.R. 329, 334 (Bankr. D.Vt. 1988). If an incorrect address is used, many courts have found that the presumption does not arise. *In re Randbre Corp.*, 66 B.R. 482, 485 (Bankr. S.D.N.Y. 1986). However, even with an incorrect address, some courts have found a weakened presumption of receipt, if there is sufficient evidence from which to presume that the addressee nonetheless received the incorrectly addressed notice. *Id.* at 486. Some courts have found such a weakened presumption did arise where there was only a missing or incorrect zip code. *STN Enterprises*, 94 B.R. at 333; *In re Longardner & Associates, Inc.*, 855 F.2d 455, 460 (7th Cir. 1988), *cert. denied*, 489 U.S. 1015 (1989).

In this case, as the Bankruptcy Court for the Southern District of New York found when faced with a different street address (addressed to 660 E. 15 Mile Road instead of 6600 East 15 Mile Road) in *In re Randbre*, 66 B.R. 482, 486 (Bankr. S.D.N.Y. 1986), there is not sufficient evidence to presume that the addressee (Betlem) received the incorrectly addressed notice. The Court records establish that: (1) the Section 341 Meeting Notice sent to Betlem by the Court at the 204 Clinton Avenue address was returned by the Post Office for an incorrect address; (2) the Debtor's attorney was notified that the Section 341 Meeting Notice had been returned and the attorneys never sent the Section 341 Meeting Notice to a corrected address or otherwise amended the

Matrix or the Court record to reflect Betlem's correct address; (3) the Bar Date Notice was sent to Betlem at an incorrect address; and (4) the Court does not keep records of notices returned by the Post Office except for 341 Meeting Notices, so there is no evidence as to whether the Bar Date Notice was returned as was the Section 341 Meeting Notice.

Therefore, on the facts of this case, there can be no presumption of receipt and whether Betlem received the Bar Date Notice is a fact which must be proven by the Debtor. The Debtor has come forward stating that Betlem has received some pleadings in the case and therefore must have received the Bar Date Notice and the Bankruptcy Clerk's Office has no record of any notice returned to it.[10] However, Betlem's Treasurer has interposed a sworn Affidavit which indicated that Betlem did not receive the Bar Date Notice.

The Debtor has not met its burden to show that Betlem received the Bar Date Notice. Since Betlem was not afforded fundamental due process in that it did not receive the Section 341 Meeting Notice advising it about the need to file a claim under certain circumstances and it did not received the Bar Date Notice, any claim which it may have cannot be disallowed because of its failure

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[10] This assertion has now been disproved, and it has been established that the Clerk's Office does not keep records of returned notices other than returned Section 341 meeting notices.

to file a proof of claim by May 5, 1993. Betlem will be allowed to file a proof of claim under Rule 9006(b)(1) which allows the Court, at any time in its discretion, to authorize the filing of a motion that would permit a late-filed proof of claim on a showing of excusable neglect since the failure to receive notice of a bar date would constitute excusable neglect on the facts of this case and would warrant and require that Betlem be allowed to file a claim. *See In re Wm. B. Wilson Mfg. Co.*, 59 B.R. 535, 538 (Bankr. W.D.Tex. 1986).

III. Objection to Plan.

The Debtor has also failed to prove that Betlem received a copy of the Disclosure Statement, Plan or Confirmation Hearing Notice setting forth the date for the initial confirmation hearing and the time to file objections, in time for Betlem to file an objection to confirmation within the time required. The Court of Appeals for the Tenth Circuit has held that, notwithstanding the language of Sections 1141(c) and 1141(d) of the Bankruptcy Code that allow any claim to be discharged even though the claimholders have not received notice of the proceeding or of the confirmation hearing, the discharge of a claim without reasonable notice of the confirmation hearing in time to effectively act is violative of the Fifth Amendment to the United States Constitution. *Reliable Electric Co., Inc. v. Olson Construction Co.*, 726 F.2d 620, 623

(10th Cir. 1984). The Court continued by stating that a "fundamental right guaranteed by the Constitution is the opportunity to be heard when a property interest is at stake. Specifically, the reorganization process depends upon all creditors and interested parties being properly noticed of all vital steps in the proceeding so they may have the opportunity to protect their interests." *Id.* In this case, no confirmation order has been entered pending the Court's decision on the Betlem Claim Objection, so that any binding effect of the Plan under Section 1141 is not yet even applicable. Because of a failure of fundamental due process in that it appears that Betlem did not receive a copy of the Disclosure Statement, Plan or Confirmation Hearing Notice in time to protect its interest, it shall be allowed to file an objection to confirmation.

CONCLUSION

Unless within fifteen days of the date of this Decision and Order either: (1) the Debtor and Betlem agree to a treatment of the Betlem Claim and submit a revised confirmation order setting forth such agreed treatment, treatment that is acceptable to the Court; or (2) the Debtor requests a hearing to be able to cross-examine Brower on the allegations set forth in the Brower Affidavit: Betlem is authorized to file a proof of claim by no later than July 22, 1994; Betlem is authorized to file an objection to the

confirmation of the Third Amended Plan by no later than July 22, 1994; an adjourned confirmation hearing will be conducted on July 28, 1994, notice of which is to be sent by the Court to all creditors and parties in interest; as part of the adjourned confirmation hearing on July 28, 1994, an evidentiary hearing will be conducted on the Betlem Claim Objection, including the issues of whether Betlem's filing of a notice of mechanics lien was in violation of the Payment Agreement and whether Betlem willfully exaggerated its lien.

IT IS SO ORDERED.

HON. JOHN C. NINFO, II
U.S. BANKRUPTCY COURT JUDGE

Dated: June 30, 1994