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3 U.S. BKCY. APP. PANEL
4 OF THE NINTH CIRCUIT

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UNITED STATES BANKRUPTCY APPELLATE PANEL
OF THE NINTH CIRCUIT

In re:) BAP No. OR-16-1300-BJuF
CECIL C. GILL,) Bk. No. 3:16-bk-30589-RLD
Debtor.)
CECIL C. GILL,)
Appellant,)
v.) O P I N I O N
RANA KIRRESH; STEPHEN P.)
ARNOT, Chapter 7 Trustee,)
Appellees.)

Submitted Without Oral Argument
on July 27, 2017

Filed - September 26, 2017

Appeal from the United States Bankruptcy Court
for the District of Oregon

Honorable Randall L. Dunn, Bankruptcy Judge, Presiding

Appearances: Appellant Cecil C. Gill, pro se, on brief;
Appellee Stephen P. Arnot, Chapter 7 Trustee, pro
se, on brief.¹

Before: BRAND, JURY and FARIS, Bankruptcy Judges.

¹ Appellee Rana Kirresh did not appear in this appeal.

1 BRAND, Bankruptcy Judge:

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3 Chapter 7² debtor Cecil Gill appeals an order denying his
4 motion to compel the chapter 7 trustee to abandon the estate's
5 interest in Debtor's residence ("Residence"), which was subject to
6 a tax lien by the Internal Revenue Service ("IRS"). A portion of
7 the IRS's lien included penalties assessed for Debtor's failure to
8 pay income taxes. The bankruptcy court determined that, because
9 the chapter 7 trustee could avoid and preserve the penalty portion
10 of the lien for the benefit of unsecured creditors, "substantial
11 value" existed in the Residence precluding abandonment.

12 Whether the chapter 7 trustee could avoid and preserve the
13 penalty portion of the IRS's tax lien against the Residence is an
14 issue of first impression before the Panel. We conclude that he
15 could, and we AFFIRM.

16 **I. FACTUAL BACKGROUND AND PROCEDURAL HISTORY**

17 In 2009, Debtor purchased his Residence in the Murray Hill
18 area of Beaverton, Oregon for \$310,000. Rana Kirresh holds the
19 promissory note secured by the Residence. Debtor defaulted on the
20 note in or around May 2015.

21 Debtor converted his chapter 13 bankruptcy case to chapter 7
22 on April 18, 2016. Stephen Arnot was appointed as the chapter 7
23 trustee. Debtor received a discharge on July 26, 2016.

24 In his schedules, Debtor valued the Residence at \$500,000 and
25 claimed a total of \$128,034.78 in unsecured nonpriority debt,

27 ² Unless specified otherwise, all chapter, code and rule
28 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and
the Federal Rules of Bankruptcy Procedure, Rules 1001-9037.

1 including \$80,000 in student loans. Thus, approximately \$48,000
2 of Debtor's unsecured nonpriority debt was subject to discharge.

3 Prior to the conversion of Debtor's case, Kirresh filed a
4 \$368,558.57 secured proof of claim, which included several years
5 of delinquent property taxes. The IRS filed an amended proof of
6 claim for \$211,586.87, of which \$161,530 was a secured claim that
7 included \$48,276.33 in tax penalties. The IRS's secured tax lien
8 against the Residence was filed in 2015 and covered tax
9 assessments made during the years 2009 through 2013 for unpaid
10 income taxes from years 2005 through 2011.

11 **A. Motion for relief from stay**

12 Kirresh later moved for relief from stay to proceed with
13 foreclosure on the Residence. By this time, the total debt owed
14 to her was approximately \$371,000. Kirresh alleged that, between
15 her lien and the IRS lien, the Residence was underwater and there
16 was no equity for Debtor.

17 Debtor opposed the stay relief motion, contending that
18 Kirresh's lien was adequately protected because the Residence was
19 "valued higher than the amount claimed by Creditor (\$500,000)" and
20 "continue[d] to increase." Debtor disputed Kirresh's assertion
21 that no equity existed in the collateral beyond the delinquent
22 property tax, Kirresh's lien and the IRS lien.

23 Kirresh and Trustee ultimately entered into a stipulated
24 order on the stay relief motion allowing Trustee six months to
25 sell the Residence. The court approved Trustee's application to
26 employ Steve Kaer, an Oregon licensed broker and realtor, to sell
27 the Residence. Kaer intended to list the property for \$539,000;
28 Kaer's commission on any sale would be 6%.

1 **B. Debtor's motion to compel Trustee's abandonment of the**
2 **Residence**

3 Debtor then moved to compel Trustee to abandon the estate's
4 interest in the Residence ("Motion to Abandon"). Debtor again
5 valued the Residence at \$500,000 and argued that, because the
6 amount of debt against it was in excess of \$650,000 (including
7 liens, Debtor's claimed \$40,000 homestead exemption and proposed
8 administrative fees), it was burdensome or of inconsequential
9 value and benefit to the estate and should be abandoned.

10 Trustee opposed the Motion to Abandon, contending that
11 abandonment of the Residence was inappropriate because unsecured
12 creditors stood to receive approximately \$48,000. As Trustee
13 explained, he intended to sell the Residence for at least \$500,000
14 free and clear of the IRS's tax lien under § 363(f) and pay off
15 the \$371,000 first lien, with the IRS lien attaching only to the
16 remaining sale proceeds to the extent available. Pursuant to
17 §§ 724(a), 726(a)(4) and 551, he could then avoid, subordinate and
18 preserve the penalty portion of the IRS tax lien (\$48,276.33)
19 against the remaining sale proceeds and distribute those funds to
20 unsecured creditors.

21 As for Debtor's claimed homestead exemption, Trustee argued
22 that it was subject to the IRS's lien to the full extent of the
23 Residence and was not exempt to the extent of the lien. Thus,
24 unless the lien was satisfied, no proceeds were available for
25 Debtor's homestead exemption.

26 In response, Debtor stated that his \$500,000 valuation of the
27 Residence was based on his analysis of the history of similar
28 properties sold in the surrounding areas and was the value he

1 hoped to realize after the completion of deferred maintenance.

2 Before the evidentiary hearing on the Motion to Abandon,
3 Debtor and Trustee submitted various exhibits. Trustee included a
4 list of comparable properties that were for sale or had sold in
5 the past 12 months. The comparable list was supported by a
6 declaration from Kaer. Kaer opined that, based on his review of
7 the comparable properties, the Residence's value was \$539,000,
8 taking into consideration its current condition, including the
9 need for a new roof and siding. Debtor submitted his declaration
10 along with a property report from Classic Realty Group ("Classic
11 Report") and a recent bid for replacement of the Residence's roof,
12 siding and gutters. The Classic Report provided a "Current
13 Estimated Value" of the Residence of \$516,720 and a "Comp Analysis
14 Value" of \$434,039. The bid for replacement of the roof, siding
15 and gutters was \$74,991.

16 **1. Evidentiary hearing on the Motion to Abandon**

17 Kaer was the only witness to testify at the evidentiary
18 hearing. Kaer testified that he began selling homes in the Murray
19 Hill area shortly after its development in 1968; however, he had
20 not personally sold any homes in that area in the past 12 months.

21 Kaer explained how he determined his \$539,000 valuation for
22 the Residence and the factors involved when creating a list of
23 comparables. Kaer stated that his valuation considered roof
24 repairs, but he did not factor in replacement of the siding
25 because he believed that a good coat of paint would repair it.
26 Kaer further explained that after a physical inspection of the
27 Residence, he believed it also needed interior painting and carpet
28 cleaning.

1 Overall, Kaer thought the Classic Report offered by Debtor
2 was a fine report, but he questioned its accuracy because it did
3 not use comparables exclusively from the Murray Hill area; only
4 three of the seven homes listed were located in Murray Hill. On
5 cross-examination, Kaer conceded he was not entirely sure what
6 parameters were used to compile his list of comparables because
7 his staff had put it together. He further conceded that, just
8 like the Classic Report, at least some of the comps used were not
9 located in Murray Hill.

10 In closing argument, Trustee explained the sale process for
11 the Residence and what the estate could expect to receive from the
12 proceeds based on a hypothetical sale price of \$500,000. Although
13 no one from the IRS testified, Trustee made an offer of proof that
14 the IRS had consented to the sale free and clear of its lien and
15 would file an amended proof of claim once the amount of sale
16 proceeds were determined, which would then adjust the secured
17 portion of the tax and penalties due from the estate.³

18 The bankruptcy court rejected Debtor's declaratory testimony
19 that his \$500,000 valuation was based on a repaired home. The
20 court opined that for valuing real property one generally takes
21 the value for a pristine house and discounts it down for the cost
22 of necessary repairs. When Debtor expressed his concern that no
23 one had discussed the Classic Report during the hearing, the court
24 responded that was because no one from Classic came to testify and
25 be cross-examined. Without any testimony from a Classic witness,

1 it was not clear what factors went into the Classic Report's
2 figures.

3 **2. The court's ruling on the Motion to Abandon**

4 The bankruptcy court announced its ruling on the Motion to
5 Abandon from the bench, stating its findings and conclusions.
6 After considering the three valuations offered into evidence, the
7 court found the Residence's value to be \$500,000 as stated by
8 Debtor. Based on that value, the court concluded that Trustee's
9 sale of the Residence would benefit the estate. Accordingly, the
10 Motion to Abandon was denied. Debtor timely appealed the
11 subsequent order.⁴

12 **II. JURISDICTION**

13 The bankruptcy court had jurisdiction under 28 U.S.C. §§ 1334
14 and 157(b)(2)(A). We have jurisdiction under 28 U.S.C. § 158.

15 **III. ISSUES**

16 1. Did the bankruptcy court err in determining the value of the
17 Residence?
18 2. Could Trustee avoid and preserve the penalty portion of the
19 IRS's tax lien for the benefit of the estate?

20 **IV. STANDARDS OF REVIEW**

21 The bankruptcy court's decision to authorize or deny
22 abandonment is reviewed for an abuse of discretion. Viet Vu v.
23 Kendall (In re Viet Vu), 245 B.R. 644, 647 (9th Cir. BAP 2000).
24 A bankruptcy court abuses its discretion if it applies the wrong
25 legal standard or its findings are illogical, implausible or

26 ⁴ In conjunction with the order denying the Motion to
27 Abandon, the court entered an order compelling Debtor to turn over
28 the Residence to Trustee. Debtor's appeal of the turnover order
(16-1289) was ultimately dismissed for his failure to prosecute.

1 without support in the record. TrafficSchool.com, Inc. v. Edriver
2 Inc., 653 F.3d 820, 832 (9th Cir. 2011).

3 A bankruptcy court's valuation of property is a finding of
4 fact reviewed under the clearly erroneous standard. Arnold &
5 Baker Farms v. United States (In re Arnold & Baker Farms), 85 F.3d
6 1415, 1421 (9th Cir. 1996). A finding is clearly erroneous if it
7 is "illogical, implausible, or without support in the record."
8 Retz v. Samson (In re Retz), 606 F.3d 1189, 1196 (9th Cir. 2010).

9 The bankruptcy court's interpretation of the Bankruptcy Code
10 is a question of law we review de novo. Bendetti v. Gunness (In
11 re Gunness), 505 B.R. 1, 4 (9th Cir. BAP 2014).

12 **V. DISCUSSION**

13 **A. Abandonment under § 554(b)**

14 Section 554(b) provides that "[o]n request of a party in
15 interest and after notice and a hearing, the court may order the
16 trustee to abandon any property of the estate that is burdensome
17 to the estate or that is of inconsequential value and benefit to
18 the estate." The moving party has the burden of establishing that
19 the property at issue is burdensome or of inconsequential value
20 and benefit to the estate. In re Viet Vu, 245 B.R. at 647.

21 An order to compel abandonment is "the exception, not the
22 rule." Id. (citing Morgan v. K.C. Mach. & Tool Co. (In re K.C.
23 Mach. & Tool Co.), 816 F.2d 238, 246 (6th Cir. 1987)). Compelled
24 abandonment under § 554(b) is generally reserved for instances
25 where a trustee is merely churning property worthless to the
26 estate just to increase fees. Id.

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B. The bankruptcy court did not abuse its discretion in denying the Motion to Abandon.

At the heart of the Motion to Abandon was the bankruptcy court's valuation of the Residence and whether Trustee could avoid and preserve the tax penalties for the benefit of the estate. Debtor contends that the bankruptcy court erred on both of these issues.

1. The bankruptcy court did not clearly err in determining the value of the Residence.

10 First, Debtor takes issue with the court's factual finding of
11 value. The court considered three types of evidence in relation
12 to valuation: (1) the Kaer comparable analysis; (2) the Classic
13 Report; and (3) Debtor's valuation of the Residence on his
14 Schedule A. Debtor contends the court should not have afforded
15 **any** weight to Kaer's analysis because: (1) he first declared that
16 the siding needed to be replaced, but later testified that it only
17 needed to be painted; (2) he did not prepare his comparables list
18 and could not describe what parameters were used to determine the
19 comparables; (3) his comparables list included properties not
20 located in Murray Hill; (4) he had not sold a home in Murray Hill
21 in the past 12 months; and (5) he lacked knowledge about the
22 Residence and the Murray Hill area.

23 Given the court's valuation ruling, Debtor's argument makes
24 little sense. It rejected Kaer's \$539,000 valuation for the
25 Residence, finding that it was "a little high" because it did not

1 give adequate market effect to the siding issues.⁵

2 After considering the evidence, the court agreed with
3 Debtor's \$500,000 valuation of the Residence:

4 In any event, based on all the – of the factors, I'm
5 prepared to find the value of the property at the value
6 stated by Mr. Gill in his schedules at half a million
7 dollars. He's the one who lives there, has an idea as
8 to the condition of the property. And when he filed his
case, I assume he did his best to provide the
appropriate value, and that's the value he gave it. So
that's the value I would apply . . . to the property at
the present time.

9 Hr'g Tr. (Sept. 7, 2016) 5:24-6:7. The court further determined
10 that Debtor's \$500,000 valuation took into consideration the
11 possible cost of repairs.

12 Debtor contends that the court erred in using his valuation
13 for the Residence; he is not a valuation expert and he had
14 continuously represented to the court that his \$500,000 valuation
15 did not include the necessary repairs to the roof, siding and
16 gutters, which totaled approximately \$75,000. Debtor contends the
17 logical approach would have been to deduct the cost of the
18 repairs, which would have provided a value for the Residence of
19 \$425,000. In that case, Debtor contends that the approximate
20 \$25,000 balance left in sale proceeds (after paying broker fees
21 and Kirresh) was of no value to the estate.

22 The court twice rejected Debtor's testimony that his \$500,000
23 valuation did not include any cost of repairs. As the court
24 explained, to ascertain a value for real property, one generally
25 considers the value of a pristine home and discounts it down for

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27 ⁵ The court also gave little weight to the Classic Report's
values of \$516,720 and \$434,039, because no broker testified as to
what factors went into the report or explained the difference in
28 the two values. Debtor does not contest this.

1 necessary repairs. This approach is not an illogical one.

2 We further note that at a time when it suited Debtor's
3 purpose to place a higher value on the Residence, such as in
4 opposition to Kirresh's stay relief motion, Debtor claimed that
5 Kirresh's \$500,000 valuation of the Residence (which she likely
6 obtained from Debtor's schedules) was too low, that the
7 Residence's value was continuing to increase, and that equity
8 likely existed in the Residence beyond the delinquent property
9 tax, Kirresh's lien and the IRS lien.

10 In light of the record, we conclude that the bankruptcy
11 court's rejection of Debtor's testimony that his \$500,000
12 valuation was based on a repaired home was not clearly erroneous.
13 We further conclude that its \$500,000 valuation for the Residence
14 was not illogical, implausible or without support in the record.

15 **2. Trustee could avoid and preserve the penalty portion of
16 the IRS's tax lien for the benefit of the estate.**

17 The bankruptcy court did not make explicit findings regarding
18 Trustee's ability to avoid, subordinate and preserve the possible
19 \$48,276.33 in tax penalties for the estate under §§ 724(a),
20 726(a) (4) and 551. Yet, by finding that at a value of \$500,000
21 there was "substantial value" for the estate's unsecured creditors
22 with Trustee's sale of the Residence free and clear of the IRS's
23 lien under § 363(f), it implicitly determined that Trustee could
24 do as he intended based on those statutes. If the court had not
25 determined so, then Debtor's claimed homestead exemption would
26 have exhausted the remaining equity after paying Kirresh, leaving
27 nothing for unsecured creditors and making abandonment
28 appropriate.

1 Surprisingly, there is a dearth of case law on this precise
2 issue. However, we conclude that the Code expressly authorized
3 Trustee to avoid, subordinate and preserve the penalty portion of
4 the IRS's tax lien for the benefit of the estate's unsecured
5 creditors.

6 Under § 724(a), the chapter 7 trustee may avoid a lien that
7 secures a claim of a kind specified in § 726(a)(4). Section
8 726(a)(4) subordinates any allowed claim, "whether secured or
9 unsecured, for any . . . penalty . . . arising before the earlier
10 of the order for relief or the appointment of a trustee, to the
11 extent that such . . . penalty . . . [is] not compensation for
12 actual pecuniary loss suffered by the holder of such claim."
13 Taken together, §§ 724(a) and 726(a)(4) allow a chapter 7 trustee
14 (but not the debtor or a third party) to avoid a lien to the
15 extent the lien secures the claim for a penalty, including a tax
16 penalty. Holloway v. Internal Revenue Serv. (In re Odom Antennas,
17 Inc.), 340 F.3d 705, 708 (8th Cir. 2003); In re Bolden, 327 B.R.
18 657, 664 (Bankr. C.D. Cal. 2005) (denying debtor's motion to
19 compel abandonment of estate property because the avoided tax
20 penalties could be preserved for the benefit of the estate and a
21 distribution paid to unsecured creditors).⁶

22 Further, § 551⁷ accords the chapter 7 trustee the statutory
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24 ⁶ It is undisputed that the tax penalties here were assessed
25 against Debtor before the order for relief as a penalty and not as
26 compensation for actual pecuniary loss. The penalties were
punitive in nature and assessed to punish Debtor's failure to pay
income taxes.

27 ⁷ Section 551 provides that any transfer avoided under
28 section 724(a) is preserved for the benefit of the estate but only
(continued...)

1 right to preserve any liens avoided under § 724(a) for the benefit
2 of the estate. In re Bolden, 327 B.R. at 664; 4 Norton Bankr. Law
3 & Practice 3d § 83:2 (2017) (Sections 724(a), 726(a)(4) and 551
4 authorize chapter 7 trustee to avoid liens on property securing
5 debts imposed upon the debtor for punitive purposes, thereby
6 effecting the release of additional funds to satisfy obligations
7 to unsecured creditors); 5 Collier on Bankruptcy ¶ 551.01 (Alan N.
8 Resnick & Henry J. Sommer, eds., 16th ed. 2015).

9 The purpose of § 724(a) is to protect unsecured creditors
10 from the debtor's wrongdoing. In re Bolden, 327 B.R. at 664; Rice
11 v. Internal Revenue Serv. (In re Odom Antennas, Inc.), 258 B.R.
12 376, 384 (Bankr. E.D. Ark. 2001), aff'd, 340 F.3d 705 (8th Cir.
13 2003). Enforcement of penalties against a debtor's estate serves
14 not to punish the delinquent taxpayers, but rather their entirely
15 innocent creditors. Innocent creditors should not be punished for
16 the actions of delinquent debtor taxpayers. Simonson v.
17 Granquist, 369 U.S. 38, 41 (1962); In re Bolden, 327 B.R. at 664.
18 "By avoiding the penalty portions of the tax liens and preserving
19 them for the benefit of the creditors, the estate is enriched
20 while the IRS still obtains the principal portion of its liens,
21 with interest, in the order and priority of each respective lien."
22 In re Bolden, 327 B.R. at 665.

23 Debtor cites no authority contrary to Holloway and Bolden and
24 asserts only two arguments. He first contends that Trustee
25 offered no evidence of an agreement with the IRS for the sale of
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28 ⁷ (...continued)
with respect to property of the estate.

1 the Residence free and clear of its lien and allowing him to
2 subordinate the penalty portion of the lien. No one from the IRS
3 testified at the evidentiary hearing about whether it consented to
4 the sale free and clear, but Trustee did make an offer of proof
5 that he had the IRS's consent and that the IRS would file an
6 amended proof of claim once the amount of sale proceeds were
7 determined, which would then adjust the secured portion of the tax
8 and penalties due from the estate. Moreover, according to
9 Trustee, such sales are commonplace.

10 As for subordination of the penalty portion of the tax lien,
11 it is clear by operation of §§ 724(a) and 726(a)(4) that a penalty
12 which is secured by a tax lien is automatically demoted in a
13 chapter 7 case from the highest priority to the lowest priority,
14 payable only after general unsecured creditors are paid in full.
15 Thus, the Code compels subordination of such penalties; no consent
16 from the IRS is necessary.

17 Next, Debtor attempts to distinguish Bolden, arguing in that
18 case the IRS had eight secured tax liens against the debtor's
19 residence as opposed to one. 327 B.R. at 659. This is a
20 distinction without a difference. As Trustee counters, assuming
21 he can sell the Residence for at least \$500,000, which appeared
22 plausible at the time the bankruptcy court made its decision, the
23 estate stands to receive up to \$48,000 from the avoided and
24 preserved penalties. This would be true whether the IRS has one
25 lien or eight liens totaling the same amount.

26 Not including Debtor's student loans, his scheduled unsecured
27 nonpriority debt totaled approximately \$48,000. With a sale of
28 the Residence at \$500,000 and Trustee's ability to avoid,

1 subordinate and preserve the penalty portions of the IRS's tax
2 lien (and interest thereon), unsecured creditors stand to receive
3 up to \$48,000 from the sale, minus Trustee's fees and other
4 administrative expenses. The Residence was not burdensome or of
5 inconsequential value and benefit to the estate, as required by
6 § 554(b). It was, as the bankruptcy court found, of "substantial
7 value" to the estate. Accordingly, we conclude that the
8 bankruptcy court did not abuse its discretion in denying the
9 Motion to Abandon.

10 **VI. CONCLUSION**

11 For the foregoing reasons, we AFFIRM.

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