Equity? You Don't Have No Stinkin' Equity! Valuation Issues and the Underwater Property

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EQUITY, YOU DON'T HAVE NO STINKIN' EQUITY: VALUATION ISSUES AND THE UNDERWATER PROPERTY

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JENNER & BLOCK CONFERENCE CENTER
CHICAGO, ILLINOIS

Chief Judge Catherine J. Furay
Steven M. Wallace
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Valuation Cheat Sheet
For Bankruptcy Practitioners

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Introduction

An essential skill of a bankruptcy lawyer is the ability to assess whether evidence of value is needed to represent your client effectively in some aspect of the case. When necessary, that skill may also call for presenting expert and lay opinion testimony as to value. The following is an attempt to summarize the literally hundreds of valuation cases and provide a quick guide to get started. Although I have made every attempt to be comprehensive, please be aware that approaches to value vary; that the value of property may be different for different purposes and at different times during the life of a bankruptcy case; and therefore this "cheat sheet" should not substitute for independent legal research and analysis.

I. Valuation Issues Pervade the Bankruptcy Code: A Partial List

► ***Adequate Protection*** under **§ 361** – requiring payments or replacement liens to protect the creditor against a decrease in the value of its interest[1]
► ***Stay relief*** under **§ 362(d)(2)(A)** – whether debtor has "equity" in the property[2]

[1] Adequate protection is to be determined by the value of the creditor's interest in property during the administration of the Chapter 11 case. If that interest is declining, then a secured creditor is entitled to cash or other security in the amount of the decline in value of its collateral during the course of the Chapter 11 case. **In re Apex Oil**, 85 B.R. 538, 541 (Bankr. E.D. Mo. 1988) , *citing* **United Savings Association v. Timbers of Inwood Forest**, 484 U.S. 365, 108 S. Ct. 626, 629-30, 98 L.Ed.2d 740 (1988); no evidence was presented that the value of the debtor's service station would diminish during the course of this Chapter 11 proceeding.

[2] Test for determining whether debtor has any equity in property, for purpose of determining whether stay should be lifted to allow creditor to pursue its rights therein, involves comparison between total liens against property and property's current value; all encumbrances must be considered, whether or not all lienholders have requested relief from stay. **In re Bowman**, 253 B.R. 233 (8th Cir. BAP 2000); **In re Gindi**, 642 F.3d 865 (10th Cir. 2011) *overruled on other grounds* ***TW Telecom Holdings Inc. v Carolina Internet Ltd.***, 661 F.3d 495 (10th Cir. 2011). This is the majority view. *But see* **In re Cote**, 27 B.R. 510 (Bankr. D. Ore. 1983) (equity determined by comparison of value of property to amount owed to senior lienholder; liens of junior lienholders not considered); *compare with* **Stewart v. Gurley**, 745 F.2d 1194 (9th Cir. 1984) (9th Circuit chose not to follow ***In re Cote***, because the language of the statute merely refers to the debtor's "equity," which is defined as the amount or value of a property above the *total* liens or charges); *see also* ***In re White***, 409 B.R. 491, 495 (Bankr. N.D. Ind. 2009) (For purposes of § 362(d)(2), "equity is a function of the property's value, minus the amounts due on account of the liens and encumbrances against it, and any claimed exemption. Consequently, in order to successfully plead a lack of equity, the movant must come forward with all of those facts—how much is the property worth, how much is owed

- ► ***Sales of property*** under **§ 363(f)(3)** free and clear of liens – whether the price of the property to be sold is greater than the aggregate value of all liens on such property and for purposes of whether the buyer is a good faith buyer under **§ 363(m)**[3]
- ► ***Determination of Secured Status*** under **§ 506** (discussed below)
- ► ***Scheduling of Assets***/Disclosure of Transfers under **§ 521 –** schedules and statements require a debtor to disclose under penalty of perjury the "current value" of the asset, and the "value" of the transfer[4]
- ► ***Exemptions*** under **§ 522(a)(2) –**"In this section…value" means "fair market value as of the date of the filing of the petition, or, with respect to property that becomes property of the estate after such date, as of the date such property becomes property of the estate [5]
- ► ***Lien Avoidance*** under **§ 522(f) –** avoidance of liens to the extent they impair an exemption; under **§ 522(f)(2)(A)**, a lien shall be considered to impair an exemption to the extent that the sum of (i) the lien; (ii) all other liens on the

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on account of any liens against it and the amount of any exemption that may have been claimed by the debtor—and it must do so with particularity: a general allegation that there is no equity will not suffice.").

[3] **In re Abbotts Dairies of Pennsylvania, Inc.**, 788 F.2d 143, 149 (3rd Cir. 1986) (in determining whether the purchaser was in good faith, courts consider that whether fair and valuable consideration is given in a bankruptcy sale is when the purchaser pays 75% of the appraised value of the assets). **In re Adam Aircraft Industries, Inc**., 2013 WL 773044 (Bankr. D. Colo. Feb. 28, 2013) (bankruptcy court properly applied replacement and not liquidation value standard in valuing assets sold by a Chapter 7 Trustee at a **§ 363** sale, since the business was being sold as a going concern) *aff'd in part rev'd in part* **In re Adam Aircraft Indus v. City of Pueblo**, 527 B.R. 709, 712 (D. Colo. 2014) (Affirming bankruptcy court's holding on valuation).

[4] **Fed. R. Bankr. P. 1007(b)(1)** requires the filing of schedules of assets and liabilities prepared as prescribed by the appropriate Official Forms. The current forms were revised in December 2007, and require a disclosure of "current value." At some point in the past, however, the official forms required the debtor to list the "current market value" of the debtor's interest in the property – this author was unable to determine when this changed. But, as recently as 2004, the court in **Harker v. West (In re West),** 328 B.R. 736, 749 (Bankr. S.D. Ohio 2004) noted the requirement that debtors value assets at "market value" in the forms. In **West**, the court noted that the phrase "market value" was not defined in the Code or Rules and that there were surprisingly few cases addressing the definition. The court noted that, with only two exceptions, the courts that had considered the question concluded that property should be listed in schedules and valued for exemption purposes at its "fair market value," defined as the price that a willing seller not under compulsion to sell and a willing buyer not under compulsion to buy agree upon "after the property has been exposed to the market for a reasonable amount of time" (cites omitted). Two courts had considered that items such as household goods should be listed at liquidation value. In considering whether debtor's discharge should be denied for valuing jewelry purchased at retail for $30,000 which debtor scheduled as worth $2,000, in reliance on her counsel's advice to use a pawnshop value, the court believed reliance on advice of counsel was reasonable, such there was limited support for that valuation approach and debtor could not reasonably have been expected to know that she should have used fair market, rather than liquidation, values in completing her Schedule B. *See* **Zitwer v. Kelly (In re Kelly),** 135 B.R. 459, 462 (Bankr. S.D.N.Y. 1992) ("The defense of reliance on counsel is not available when it is transparently plain that the advice is improper").

[5] **In re Valentine,** 2009 WL 3336081,*7 (Bankr. D.N.H. Oct 14, 2009) (rejecting trustee's objection to jewelry exemption on grounds of debtor's alleged bad faith in valuing jewelry; finding debtor's testimony that she relied on counsel's advice to value jewelry purchased for $5,520 at $1,000 liquidation value was not bad faith); **In re Orton,** 687 F.3d 612 (3rd Cir. 2012) (Debtor limited to the $1.00 exemption in oil and gas lease, even though $1.00 was the fair market value at the time of the petition; estate entitled to the post-petition appreciation in value, rejecting Debtor's argument that **Schwab v. Reilly**, 130 S. Ct. 2652 (2010) applies only to bad faith undervaluation).

property; and (iii) the amount of the exemption that the debtor could claim if there were no liens on the property; exceeds the value of that the debtor's interest in the property would have in the absence of any liens."[6]

- ► ***Exceptions to discharge*** under **§ 523**, *e.g.,* value of property for purposes of determining fraud, damages
- ► ***Preferential Transfers*** under **§ 547** for purposes of determining insolvency, defined as when the sum of the debts is great than all the property, at a "fair valuation" under **§ 101(32)**[7]; and, for purposes of whether a creditor received more than it would have received in a chapter 7 liquidation.[8]

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[6] The majority view is that fair market value is the appropriate valuation standard for purposes of lien avoidance, and that costs of liquidation should not be deducted. *E.g.,* **In re Wolmer**, 494 B.R. 783 (Bankr. D. Conn. 2013). *See also* **In re Sheth,** 225 B.R. 913, 917-19 (Bankr. N.D. Ill. 1998) (Debtor brought an adversary complaint against creditor seeking to avoid its judicial lien under 11 U.S.C. §522(f)(1) and (f)(2). The court held the debtors were entitled to avoid the judicial lien. However, the court rejected the debtor's liquidation argument finding an allowance "for partial avoidance of a judicial lien to the extent that the lien only partially impairs the debtor's exemption." Further, the court adopted the majority position holding the "estimated liquidation costs . . . should not be deducted from the FMV of the property."); *But see* **In re Walsh**, 5 B.R. 239 (Bankr. D. C. 1980). There is also a split of authority on the issue of whether a judicial lien's priority under state law is relevant in determining whether a debtor may avoid such lien, and whether a debtor may use **§ 522(f)** to avoid a judicial lien that has priority even over the first mortgage. See **In re Moltisanti,** 2012 WL 5246509 (Bankr. E.D.N.Y. 2012) (collecting the cases); *See* **In re Kolich**, 328 F.3d 406, 410 (8th Cir. 2003); **In re Moore,** 495 B.R. 1(8th Cir. BAP 2013) (holding that Missouri state law exception to a debtor's homestead exemption rights did not prevent debtor from asserting her state law homestead exemption rights to avoid a judgment lien that creditor obtained after debtor acquired homestead property).

[7] **In re Trans World Airlines, Inc**., 134 F.3d 188 (3rd Cir. 1998) (fair valuation of assets contemplates a conversion of assets into cash during a reasonable period of time, in this case, 12 to 18 months; rejecting the preference defendant's argument that fair value implies a hypothetical sale for the highest and best price, with no time pressure, *citing* **American Nat'l Bank & Trust Co. v. Bone**, 333 F.2d 984, 987 (8th Cir. 1964); "[T]he reasonable time should be an estimate of the time a typical creditor would find optimal: not short a period that the value of the goods is substantially impaired via a forced sale, but not so long that a typical creditor would receive less satisfaction of its claim, as a result of the time value of money and typical business needs, by waiting for the possibility of a higher price;" also rejecting the defendant's argument that the fair valuation standard applies to liabilities; the Court determines that it should use the face value of debt, rather than market value, in light of the fact the business is being valued as a going concern); **In re Heilig-Meyers Company,** 328 B.R. (E.D. Va. 2005) (balance sheet test of insolvency applies; however, at the threshold, the court must determine whether, on the date of the transfers, the debtor operated as a going concern or was on its deathbed – on deathbed means the valuation should be a liquidation value); **In re Golden Mane Acquisitions, Inc**., 221 B.R. 963 (Bankr. N.D. Ala. 1997) ("Fair value, in the context of a going concern, is determined by the fair market price of the debtor's assets that could be obtained if sold in a prudent manner within a reasonable period of time to pay the debtor's debts).

[8] **In re Nguyen,** 2014 WL 61410 (Bankr. S.D. Tex. Jan. 7. 2014) (denying plaintiff's complaint to avoid foreclosure of property on ground foreclosing creditor received more than it would have received in a chapter 7 case; Wells Fargo bid the amount of its debt; plaintiff asserted that, based on the tax assessed value, which was more than the debt, Wells Fargo had received in excess; plaintiff failed to designate an expert or submit a report in response to Wells Fargo's motion for summary judgment; court accepted Wells Fargo's expert appraisal report opining that value was less than the debt); ***see also*** **In re Gibson,** 2016 WL 489611 *2 (Bankr. W.D. Wis. February 8, 2016) ("For the purpose of determining insolvency, the debtor's liabilities are the sum of the liability on all claims ***at the time of the transfer***.")

In re Lewis W. Shurtleff, Inc., 778 F.2d 1416, 1422 (9th Cir. 1985) (we are unsure whether the bankruptcy court should have deducted the transaction costs of a sale in computing the value of the property transferred. **Section**

- ► ***Fraudulent Conveyances*** under **§ 548(a)(1)(B)(i)** – avoidance of transfers where debtor received less than "reasonably equivalent value"; "value" is defined in **§ 548(d)(2)(A)** as "property, or satisfaction or securing of a present or antecedent debt of the debtor, but does not include an unperformed promise to furnish support to the debtor or to a relative of the debtor"[9]
- ► ***Recovery of transfer or its value*** under **§ 550**[10] -- not defined by the Code; nor does the Code indicate at what time "value" is determined
- ►***Abandonment*** under **§ 554** of property "of inconsequential value and benefit to the estate"[11]

547(b) itself does not address the method by which transferred property should be appraised. Nor does the Code appear to authorize a uniform method for valuation).

[9] **BFP v. Resolution Trust Corp**., 114 S. Ct. 1757 (1994) (We deem, as the law has always deemed, that a fair and proper price, or a "reasonably equivalent value," for foreclosed property, is the price in fact received at the foreclosure sale, so long as all the requirements of the State's foreclosure law have been complied with; rejecting an argument that "reasonably equivalent value" constitutes "fair market value"; the term "fair market value," though it is a well-established concept, does not appear in **§ 548)**; *see also* **In re Russell-Polk,** 200 B.R. 218 (Bankr. E.D. Mo. 1996) (Chapter 13 debtor sought to avoid real property tax sale of her property to tax sale purchaser as a fraudulent transfer; held, that proceeds received from properly conducted real property tax sales in Missouri conclusively satisfied requirement that transfers of property by debtor in year prior to petition filing be in exchange for reasonably equivalent value; "[t]he Court is sensitive to the fact that most, if not all, forced tax sales yield a purchase price much lower than the "fair market value" of the property. The Supreme Court also recognized this fact in the mortgage foreclosure sale context, yet it did not control their analysis. **BFP v. Resolution Trust Corp** 114 S. Ct. 1757, 1762. Similarly, the consideration received at a tax sale should not control the analysis in this case").

[10] **In re Hecker**, 459 B.R. 6, 14-15 (8th Cir. BAP. 2011); **In re American Furniture Outlet USA, Inc**., 209 B.R. 49, 52 (Bankr. M.D. N.C. 1997) (when chapter 11 debtor-retailer returned furniture to supplier within 90 days prepetition, fair market value of transferred goods, the value of the preference, was properly reflected in the amount netted by the supplier in liquidation sales after costs and expenses, not amount grossed at those sales, since supplier acted in a commercially reasonable manner and absent bankruptcy would have been entitled to collect costs and expenses associated with sales under North Carolina law; noting that the Code's failure to prescribe a valuation formula for **§ 550(a)** has engendered some case law; the purpose and thrust of **§ 550** is to restore the debtor's financial condition to the state it would have been had the transfer not occurred; where debtor returned goods to supplier in return for the supplier's full credit of the account, the court holds that the term "value" connotes "market value" or the amount the trustee would receive if he offered the items for sale; the credit memo is not relevant); *But see* **In re First Software Corp**., 84 B.R. 278 (Bankr. D. Mass. 1988), *aff'd* 107 B.R. 417 (D. Mass. 1989) (value that the trade creditor ascribed in a credit memo for returned goods was evidence of the market value of the goods at the time of the transfer); distinguishing those cases because the credit memo was the only evidence of value; return of furniture from Debtor to its supplier was not reflective of arms-length transaction between a willing seller and a willing buyer; amount netted by supplier after its liquidation sale of the furniture was the best evidence of value. *See also* **In re Int'l Ski Serv., Inc.,** 119 B.R. 654, 65 (Bankr. W.D. Wis. 1990) (While section 550(a) does not define "value," nor indicate at what time "value" is to be determined. "It is generally agreed that '[t]he market price at the time of transfer is the proper measure of damages. . . .(*quoting* **In re James B. Downing & Co.**, 74 B.R. 906 (Bankr. N.D. Ill. E.D. 1987)).

[11] **In re Thornton**, 269 B.R. 682 (Bankr. W.D. Mo. 2001) (Chapter 7 trustee would be directed to abandon 15.2-acre parcel of homestead property to debtors, as being of inconsequential value, where property's fair market value of $27,000, as reduced by encumbrances thereon, costs of sale, debtor's homestead and other exemptions thereon, and trustee's 25% fee for distributing the remainder, would result in total distribution of only $1,119.51 (or less than 2%) on general unsecured debt of $66,784.64; benefits to estate of administering property were de minimis); **In re Nelson,** 251 B.R. 857 (8th Cir. BAP 2000) (evidence supported bankruptcy court's determination that the two parcels were of inconsequential value or benefit to the estate, despite trustee's contentions that the parcels had value as rental property, and that equity of redemption in the property provided a source of value for the

► ***Redemption*** under **§ 722** - paying the holder of the lien the amount of the allowed secured claim (as determined under **§ 506**)[12]

► ***Denial of Discharge*** under **§ 727(a)(4)(A)** (false oath)[13]

► ***Cramdown & Strip Offs***: Determination of allowed secured claims in Chapters 11, 12 and 13 **(§§ 506(a), 1129, 1225, 1325(a)(5))** (discussed below)

► ***Liquidation analysis*** or "best interests of creditors" tests in Chapters 11, 12 and 13 (**§§ 1129(a)(7), 1225(a)(4), 1325(a)(4))** – unsecured creditors to receive value, as of the effective date of the plan, that is not less than the amount that such holder would receive if the debtor were liquidated under chapter 7

II. General Valuation Principles

►***Many meanings of value*****:** Justice Brandeis observed, "[v]alue is a word of many meanings." **Missouri ex rel. Southwestern Bell Tel. Co. v. Public Serv. Comm'n**, 262 U.S. 276, 310 (1923) (Brandeis, J., concurring)

► ***Not defined***: With limited exceptions (secured claims under and exemptions, discussed below), "value" is not a defined term in the Bankruptcy Code or Rules or the Official Forms, and, where not defined, is therefore left to case law

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estate; court rejected trustee's argument that the parcels could be rented; argument was speculative at best; trustee did not demonstrate any effort to rent the parcels, and lienholders had assignment of rents clause; court need not consider speculative factors); **In re Weiss**, 111 F.3d 1159 (4th Cir. 1997) (before bankruptcy court may abandon property of estate, trustee must ascertain property's fair market value as well as amount and validity of outstanding liens against property); **Smoker v. Hill & Assoc. Inc.,** 204 B.R. 966, 975-76 (D. N.D. Ind. 1997) (upheld bankruptcy court's finding that commissions were of inconsequential value and benefit because the commissions have generated litigation in which the debtors cannot afford).

[12] **In re Bryan,** 318 B.R. 708 (Bankr. W.D. Mo. 2004) (trade-in value, as defined by the National Automobile Dealers Association Guide (NADA), is generally the most appropriate starting point for value, and is the applicable value in this case). *Accord* **In re Weber** 332 B.R. 432 (10th Cir. BAP 2005). *But see* **In re Smith**, 307 B.R. 912 (Bankr. N.D. Ill. 2004) (determining retail, or replacement value), *rev'd* **Smith v. Household Automotive Finance Corp.**, 313 B.R. 267 (N.D. Ill. Aug 19, 2004). **NOTE**: These are pre-BAPCPA cases; see now **§ 506(a)(2)** (discussed below).

[13] **Harker v. West (In re West)**, 328 B.R. 736, 749 (Bankr. S.D. Ohio 2004) (debtor's undervaluation of jewelry was a false oath; representations in schedules relate to the existence of and disposition of assets of the estate and are therefore material; debtor had purchased jewelry for approximately $30,000 but scheduled the "market value" as $2,000; testimony was that appraised value was nearly $4,000; however, reliance on counsel's advice was a defense) *distinguished by* **Robinson v. Worley**, 540 B.R. 568 (D. M.D.N.C. 2015) appealed filed in 4th Cir.; **In re Charles**, 2013 WL 436441 (Bankr. D. N.D. 2013) (Debtor denied a discharge for undervaluation of real estate; debtor scheduled value of real estate at $225,000, the tax assessed value, but had listed the property for $274,900, and received a written offer of $249,900, and had countered at $274,900; the debtor had no evidence to support his contention that he had valued the property based on an oral offer of $225,000); **In re Edwards**, 2011 WL 2619193, *5 (Bankr. E.D. Ky. Jul 01, 2011) (debtor's discharge denied; debtor was sophisticated business person who knowingly scheduled real estate at values thousands of dollars below their appraised value and valued listed in financial statement given to bank within 6 months of filing bankruptcy in attempt to show no equity; not reasonable for debtor to rely on tax values when debtor knew those values were not fair value); **In re Ferebee**, 2012 WL 506740, *13 (Bankr. E.D. Va. Feb 15, 2012) (valuation of jewelry in schedules at $50 but that had been purchased for $32,000 warranted denial of discharge).

► ***A determination of value inherently incorporates a consideration of time*:** "Logic and common sense inform us that the amount that can be realized from the sale of an asset varies as a function of the time period over which the asset must be sold." **In re Trans World Airlines, Inc.,** 134 F.3d 188, 194 (3rd Cir. 1998). *See also* **BFP v. Resolution Trust Corp**., 114 S. Ct. 1757, 1762 (1994) (discussing value for purposes of whether value received at foreclosure sales constitutes reasonably equivalent value for purposes of § 548; "An appraiser's reconstruction of "fair market value" could show what similar property would be worth if it did not have to be sold within the time and manner strictures of state-prescribed foreclosure. But property that *must* be sold within those strictures is simply *worth less*. No one would pay as much to own such property as he would pay to own real estate that could be sold at leisure and pursuant to normal marketing techniques.") (emphasis in original).

► ***The date/time for determining value is not specified:*** With limited exceptions, the Code does not specify the date as to which the court should determine value; relevant valuation points in time include the date the creditor acquired its interest in the collateral (prepetition); the date of the petition; the date of the motion; and the date of the hearing or final judgment, or some other point.

- **For Purposes of Value of Exemptions--Date of Petition: § 522(a)(2) –**"In this section…value" means "fair market value as of the date of the filing of the petition, or, with respect to property that becomes property of the estate after such date, as of the date such property becomes property of the estate." **In re Polis,** 217 F.3d 899 (7th Cir. 2000) (Assuming that Chapter 7 debtor's TILA claim was not assignable and so could not be the subject of a "market" transaction in the literal sense, that was irrelevant to its status as property of bankruptcy estate, which could be valued for exemption purposes on basis of its fair market value on the date the petition was filed; error for district court to determine exemption had no value due to later events and to dismiss the claim for lack of standing). *But see* **Fitzgerald v. Davis**, 729 F.2d 306 (4th Cir. 1984) (although recognizing that **§ 522(a)(2)** requires the court to determine value of exemption as of the petition date, the, a bankruptcy court should not disregard the price obtained from a sale of the property during the pendency of the bankruptcy proceedings. Under these circumstances, a sale price greatly in excess of an estimate is the more reliable evidence of the "value" defined in **§ 522(a)(2)).**

- **For Purposes of Preference – Split of Authority—Date of Petition/Date Preference period begins: In re Hecker**, 459 B.R. 6,11 (8th Cir. BAP 2011) (whether the transfer enabled a creditor to receive more than they would have received in a hypothetical liquidation for purposes of **§ 547** is conducted as of the petition date. No preferential transfer because there was no equity in the property as of that date; reversed and remanded for determination of trustee's recovery under **§ 550); *but see*, In re Prescott**, 805 F.2d 719, 726 (7th Cir. 1986) (whether the transfer enabled a creditor to receive more than they would have received in a hypothetical liquidation, for purposes of **§ 547**, the trustee must establish a

creditor's value of collateral on the date the preference period begins. Seventh Circuit upheld a Bankruptcy court's finding that a creditor's collateral was worth $131,734.00 on day preference period began, where uncontested evidence showed retail value of inventory was $130,000 two weeks after beginning date of preference, and evidence established the value remained static. The creditor offered no rebuttal evidence speaking to the collateral's value on the date the preference period began).

- **For Purposes of Property of the Estate –Not limited to value as of date of petition:** *In re Potter*, 228 B.R. 422 (8th Cir. BAP 1999) (value of contingent interest in trust; post-petition appreciation belongs to the estate); *see also In re Burkholder*, 177 B.R. 260 (Bankr. N.D. Ohio 1995) (appreciation in the value of estate property inures to the bankruptcy estate, not the debtor).

- **For Purposes of Redemption: Pre-BAPCPA Split of Authority**: **In re Podnar**, 307 B.R. 667, 673 (Bankr. W.D. Mo. 2003 (Redemption value is determined as of the date of the motion to redeem or, if the motion is contested, the date of the redemption hearing; valuing the property as of the date of the petition would place the creditor in a better position than it would be if it were allowed to repossess in the ordinary course of events; but, if the creditor can show undue delay by the debtor, gross negligence, or other acts by which the debtor has unreasonably diminished the value of the collateral between the date of the bankruptcy filing and the redemption hearing, the valuation made be made as of the date of the bankruptcy filing); *but see* **In re Smith**, 313 B.R. 785 (Bankr. N.D. Ind. 2004) (date of petition) *and* **In re Bouzek** 311 B.R. 239 (Bankr. E.D. Wis. 2004) (redemption is akin to surrender of collateral than cramdown. Thus, wholesale value is the appropriate standard to apply in §722 cases. NOTE: BAPCPA redemption is discussed below.

- **For Purposes of Lien Avoidance in Chapter 7**: **In re Wade**, 354 B.R. 876 (Bankr. N.D. Ia. 2006) (When the purpose of the valuation is to determine the amount of the lien surviving discharge in a Chapter 7, petition date is appropriate, since post-petition appreciations in value of the property inure to the benefit of the debtor under the fresh start principle).

- **For Purposes of Cramdown: Valuation of Secured Creditor's Claim at Confirmation: Split of Authority: In re Roach**, 2010 WL 234959, *5 (Bankr. W.D. Mo. Jan. 15, 2010) (For purposes of Chapter 13 modification of mortgage, Court concludes date of confirmation is date for valuation of the home, notwithstanding delay in getting to confirmation and the fact that value had declined; creditor should have asked for adequate protection); **In the Matter of Heritage Highgate, Inc**., 449 B.R. 451 (D. N. J. 2011), *aff'd* 679 F.3d 132 (3rd Cir. 2012) (When value is for purposes of confirming a plan, it should be determined as of the confirmation date); *but see* **In re Johnson**, 165 B.R. 524 (Bankr. S.D. Ga. 1994) (date of petition). In the Sixth and Seventh Circuits, date

of confirmation. *See* **In re Williams**, 480 B.R. 813, 817 (Bankr. E.D. Tenn. 2012); **In re Spraggins**, 316 B.R. 317 (Bankr. E.D. Wis. 2004).

- **For Purposes of Strip-Off & Anti-Modification Provisions: Split of Authority: TD Bank, N.A. v. Landry**, 479 B.R. 1 (D. Mass. 2012) (reversing the bankruptcy court and finding that valuation date was petition date; since the purpose of the valuation was whether the bank's claim was entitled to protection of **§1322(b)(2)** and therefore whether the bank is entitled to relief from stay; **In re Abdelgadir**, 455 B.R. 896, 902 (9th Cir. BAP 2011) (While it might be entirely appropriate to value secured claim of junior deed of trust lender whose lien the individual Chapter 11 debtors were seeking to strip as of time of confirmation of their lien-stripping plan, determination as to whether real property that secured lender's claim was debtors' primary residence, as required for lender to be protected by anti-modification provision of Chapter 11, **§ 1123(b)(5)**, had to be made not as of time of plan confirmation, or as of earlier date when debtors entered into loan, but as of petition date); **In re Marsh**, 475 B.R. 892 (N.D. Ill. 2012) (date of petition or date of entry of final judgment resolving adversary); *But see* **In re Proctor**, 494 B.R. 833 (Bankr. E.D.N.C. 2013) (date of the loan documents). The Court of Appeals for the Seventh Circuit has not addressed the date of valuing a home for purposes of strip-off, but the bankruptcy court for the N.D. of Indiana has held the date of valuation is the petition date. **In re Hegeduis**, 525 B.R. 74 (Bankr. N.D. Ind. 2015).

PRACTICE TIP:
You must parse these cases very carefully and make sure you understand what date the court is going to use for purposes of determining value. A failure to present evidence as of the correct date for determination, when the value has increased or decreased significantly, for example, may result in the court finding no credible evidence to support your proffered value. Since the proper date to value is a legal question, it is reviewed de novo on appeal, and may result in reversal if the bankruptcy court applies – at your urging -- the wrong date.

► ***Numerous Valuation Standards/Approaches***: There are numerous valuation standards used in the Code, in case law, as well as in common parlance. One court has expressed it this way: "Wholesale," "foreclosure," "liquidation," or "quick sale" values describe a proposed disposition of property by surrender to the creditor and prompt conversion of the property by the creditor to cash, usually in accordance with State foreclosure law. "Retail," "going concern," "replacement cost," or "rehabilitation" values describe a proposed retention and use of property in the debtor's ongoing financial reorganization." **In re Johnson**, 145 B.R. 108, 115, n.10 (Bankr. S.D. Ga. 1992), *cited with approval*, pre-**Rash** by **In re Gallup**, 194 B.R. 851, 853, n.2 (Bankr. W.D. Mo. 1996).

Terms used to denote the lowest types of value:

- **"Liquidation Value"**: At least one court has observed, "[w]e do not know of an accepted standard or definition for a liquidation value. It is thought to be a distress sale and less than market value, but that may not always be the case." **In re Yoder**, 32 B.R. 77 (Bankr. W.D. Pa. Aug 16, 1983), *rev'd on other grounds* 48 B.R. 744 (W.D. Pa. 1984).

- **"Pawnshop Value"**: "Simply a different manner of expressing liquidation, or distressed sale value." **In re West**, 328 B.R. 736, 752, n.8 (Bankr. S.D. Ohio 2004).
- **"Foreclosure Value"** or **"Distress Value"** (or **"Distressed Value"):** "What the secured creditor could obtain through foreclosure sale of the property." **Rash,**[14] 520 U.S. at 955-56.
- **"Wholesale Value":** Considered to be synonymous with foreclosure value. **In re Perez,** 318 B.R. 742, 743 (Bankr. M.D. Fla. 2005); what secured creditor could expect to recover by repossessing vehicle and selling it at auction or by other wholesale means. **In re Bouzek**, 311 B.R. 239, 428 (Bankr. E.D. Wis. 2004) (value of vehicle for **§ 722** redemption purposes).

Terms Used to Denote the Highest Value:

- **"Fair Market Value"**: Generally understood as "[t]he price that a seller is willing to accept and a buyer is willing to pay on the open market and in an arm's-length transaction" (*Black's Law Dictionary* (Westlaw 9th ed. 2009)), but considered synonymous with "replacement value" under **Rash.** *But see* **In re Walsh**, 5 B.R. 239 (Bankr. D.C. 1980) (notwithstanding § 522(a) definition of value as fair market value, exemptions must be interpreted in the liquidation context of a Chapter 7 case, and thus, in such a case, "fair market value" is the equivalent of "liquidation value." **NOTE: Walsh** has been soundly criticized. *E.g.*, **In re Wolmer**, 494 B.R. 783 (Bankr. D. Conn. Jun 25, 2013); *and* **In re Sumerell**, 194 B.R. 818 (Bankr. E.D. Tenn. 1996).

- **"Replacement Value"**: What the debtor would have to pay for comparable property, defined by the Supreme Court in **Rash** for purposes of **§§ 506** and **1325(a)(5)(B**) and cramdown of a vehicle; **"[**b]y replacement value, we mean the price a willing buyer in the debtor's trade, business, or situation would pay a willing seller to obtain property of like age and condition." **Rash**, 520 U.S. at 959 n.2.[15]

Terms Used For Something in the Middle:

- "Split-the-difference value" or "midpoint between foreclosure and replacement value": rejected by **Rash**; *but see* **In re Tripplett**, 256 B.R. 594 (Bankr. N.D. Ill. 2000) (appropriate when debtor was proposing to redeem vehicle at midpoint between the vehicle's retail and wholesale value).

Terms Used In Connection With Vehicle Valuations:

- There are three approaches for valuing a vehicle -- retail, replacement and wholesale, liquidation or foreclosure. In some instances, some variation or departure might be

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[14] **Associates Commercial Corp. v. Rash**, 520 U.S. 953, 117 1879, 138 L.Ed.2d 148 (1997).

[15] The 9th Circuit in **In re Taffi**, 96 F.3d 1190 (9th Cir. 1190) had distinguished between fair market value and replacement value; post-**Rash**, these terms are considered to be synonymous for purposes of value under **§ 506(a)**, since, as the Supreme Court explained, "replacement value" does not mean what it would cost the debtor purchase the collateral brand new." **Rash**, 520 U.S. at 959 n.2.

appropriate in the court's equitable discretion. **In re Podnar**, 307 B.R. 667, 670 (Bankr. W.D. Mo. 2003. **NOTE:** This is pre BAPCPA and **§ 506(a)(2).**

- **"Retail Value":** The price a willing buyer is willing to pay for any car. **In re Bryan**, 318 B.R. 708, 710-11 (Bankr. W.D. Mo. 2004).

- **"Replacement Value":** The price a willing buyer is willing to pay for a similar car minus the cost of sale. **In re Bryan**, 318 B.R. 708, 710-11 (Bankr. W.D. Mo. 2004) "In the absence of evidence relating to a vehicle's markup for services or the profit margin which might be included in NADA tables. . . ." Illinois Bankruptcy Court found a 5% discount from the NADA retail value would be appropriate to determine a vehicle's replacement value. **In re McElroy**, 339 B.R. 185, 189 (Bankr. C.D. Ill. 2006).

- **"Wholesale, Liquidation or Foreclosure Value":** "For the most part, though there are subtle differences, courts use the terms liquidation, wholesale, trade-in and foreclosure value interchangeably. In general, the values contained in these terms are defined as either the amount a secured creditor would receive if it repossessed the collateral and sold it in the most beneficial manner it could – foreclosure or liquidation value – or the amount a consumer might expect a dealer to offer when asking the dealer to take a vehicle in trade – trade-in or wholesale value. **In re Bryan**, 318 B.R. 708, 710-11 (Bankr. W.D. Mo. 2004).

- **"Trade-in Value"**: "The retail price of the car minus the costs to recondition and repair the car, the interest paid to finance the care until it is sold, the cost of storing the car, and any profit." **In re Bryan**, 318 B.R. 708, 710 (Bankr. W.D. Mo. 2004).

- "**Private Party Value**": What a buyer can expect to pay when buying a used car from a private party. It assumes the vehicle is sold "as is" and carries no warranty (other than the continuing factory warranty). The final sale price may vary depending on the vehicle's actual condition and local market conditions. **In re Weber** 332 B.R. 432 (10th Cir. BAP 2005) (quoting from Kelley Blue Book definition).

- "**Gross sales price**": The gross amount received at the sale. **In re Bryan**, 318 B.R. 708, 710 (Bankr. W.D. Mo. 2004).

- "**Net to seller price**": The amount received at the sale, less the costs of sale, which include costs of repossession, transportation, storage and sales commission. **In re Bryan,** 318 B.R. 708, 710 (Bankr. W.D. Mo. 2004) (noting that this was not appropriate for redemption value, since there was no sale or repossession).

PRACTICE TIP:
There are three accepted sources or market guides: (1) the Black Book; (2) the Kelley Blue Book; and (3) the National Automobile Dealers Association (NADA) Guide. **In re Bryan**, 318 B.R. 708, 710 (Bankr. W.D. Mo. 2004).

Terms Used In Connection With Asset Sales:

- **"Open Market Value"** or **"Market Value":** The price the assets would bring on the open market; the value a prudent business person can obtain from the sale of an asset when there is a willing buyer and a willing seller; under this approach, it is not appropriate to deduct the costs and expenses associated with the sale, such as real estate transfer taxes, since this method focuses on what a willing buyer would pay, not necessarily what a willing seller would receive; value may be reduced by factors regarding the difficulty of the sale, or if the asset is the subject of extended litigation or where there is no ready market; such factors affect the market price of the asset, not the costs of sale; it is appropriate to adjust the market value by the net cost of making the asset marketable. **In re Golden Mane Acquisitions, Inc**., 221 B.R. 963, 968 (Bankr. N.D. Ala. 1997).

- **"Going Concern Value"**: "The term going concern is commonly understood to refer to "[a] commercial enterprise actively engaging in business with the expectation of indefinite continuance (citing Black's Law Dictionary). In the valuation context, it is generally used in contradistinction to a business that will be liquidated. Essentially, it requires an appraisal to assume the continued operation of the same type and size of business … and to exclude consideration of any merger or liquidation." **In re Adam Aircraft Industries, Inc.**, 2013 WL 773044, n.4 (Bankr. D. Colo. Feb. 28, 2013).

Other Valuation Terms:

- "As Is"
- "Face Value"
- "Book Value"
- "Appraised Value"
- "Value for insurance purposes"
- "Tax-assessed Value"
- "Clean Retail Value"

III. Section 506(a) Value Determinations & *Rash*[16]

►***Secured Claim Valuations: Governed by* § 506(a)**:

§ 506(a)(1): An allowed claim of a creditor secured by a lien on property in which the estate has an interest…is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property… and is an unsecured claim to the extent that the value of such creditor's interest … is less than the amount of the secured claim. ***Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest. (***emphasis added).

[16] **Associates Commercial Corp. v. Rash**, 520 U.S. 953, 117 S. Ct. 1879, 138 L.Ed.2d 148 (1997).

***Personal Property Exception*: § 506(a)(2)** - Personal Property Valuations in Individual Chapter 7/13 Cases:

If the debtor is an individual in a case under chapter 7 or 13, such value with respect to personal property securing an allowed claim shall be determined based on the **replacement value** of such property as of the date of the filing of the petition without deduction for costs of sale or marketing. With respect to property acquired for personal, family, or household purposes, **replacement value** shall mean **the price a retail merchant would charge for property of that kind** considering the age and condition of the property at the time value is determined. (emphasis added)

►***Replacement Value, Not Wholesale or Midpoint for Chapter 13 Cramdown****:* For purposes of cramdown value of a vehicle, bankruptcy court should use replacement, not wholesale value, or the value in between, to determine the amount of the secured creditor's claim. **Associates Commercial Corp. v. Rash**, 520 U.S. 953, 117 S. Ct. 1879, 138 L.Ed.2d 148 (1997).

►***Definition of Replacement Value:*** **"**By replacement value, we mean the price a willing buyer in the debtor's trade, business, or situation would pay a willing seller to obtain property of like age and condition." **Rash**, 520 U.S. at 959 n.2.

► ***Rationale:*** Under the cramdown option, the creditor is exposed to "double risks" in that the debtor keeps the collateral under a court-imposed "crammed down" financing arrangement, with the risk the debtor may again default and the property may deteriorate further. **Rash**, 520 U.S. at 962-63. Because the creditor is receiving back neither its collateral nor its proceeds, liquidation value is not relevant to the debtor's intended use or disposition in the context of a cram down under chapter 13. *Id*.

► ***Two-Step Process*:** In valuing property under **§ 506(a)(1**), a court must engage in a two-step process: First, a court must compare the creditor's claim to the value of the "such property" – the collateral. This determination necessarily requires the court to ascertain the "creditor's interest in the estate's interest in" the property. The second step is the valuation process requires the court to determine how to value the collateral.

► ***But, beware the footnotes***: Bankruptcy Courts, as triers of fact, must determine whether the replacement value is the equivalent of retail, wholesale, or some other value based on the type of debtor and the nature of the property. Adjustments are necessary, where appropriate, to account for the absence of warranties, inventory, storage and reconditioning charges." **Rash**, 520 U.S. at 965, n 6. Courts are to consider the purpose of the valuation, but are not allowed to use different valuation standards based on the facts and circumstances of individual cases. **Rash**, 520 U.S. at 965, n. 5.

►***Rash applies in other contexts besides Chapter 13***: *E.g.,* **In re Adam Aircraft Industries, Inc.**, 2013 WL 773044 (Bankr. D. Colo. Feb. 28, 2013) (applying **Rash** principles in context of a Chapter 7 **§ 363** sale); **Rash**-type analysis applies to Chapter 11 valuation. **In re Inter-City Beverage Co., Inc.,** 209 B.R. 931 (Bankr. W.D. MO. 1997) decided before the Supreme Court handed down **Rash**).

IV. Applying *Rash* in the Real World (or, can you make a *Rash* decision?)

► ***Flexible Standard:*** Section **506(a)** does not specify the appropriate valuation standard. Rather, Congress envisioned a flexible approach to valuation whereby bankruptcy courts would choose the standard that best fits the circumstances of a particular case. **In re Heritage Highgate, Inc.,** 679 F.3d 132, 141 (3rd Cir. 2012).

► But, what about fn.5 "As our reading of **§ 506(a)** makes plain, we also reject a ruleless approach allowing use of different valuation standards based on the facts and circumstances of individual cases." **Rash,** 520 U.S. at 965, n. 5.

Redemption Examples:

Rash required the chapter 13 debtor who proposed to keep the vehicle to pay the secured creditor replacement value, rather than liquidation value, on account of debtor's "proposed use and disposition" of the vehicle under **§ 506(a)** and the risks to the secured creditor of default and depreciation. Pre- BAPCPA, most courts had determined that redemption in a lump sum carried less risk and that a wholesale or trade in value, as of the time of the redemption, was the correct value. **In re Bryan,** 318 B.R.708 (Bankr. W.D. MO. 2004) (trade-in value, as defined by the NADA, is generally the most appropriate starting point for value, and is the applicable value in this case, noting the difference between "retail value" and "replacement value." *Accord* **In re Weber,** 332 B.R. 432 (10th Cir. BAP 2005).

BAPCPA added **§ 506(a)(2),** specifying that value of personal property for an individual chapter 7 or 13 debtor would be "replacement value" as of the petition date, and further defined "replacement value" – in the case of property held for personal, family, or household purposes – as the price a retail merchant would charge for property of that kind considering the age and condition at the time value is determined. **NOTE**: In the same way that Rash equated fair market value with replacement value, Congress has seemingly chosen to equate "replacement value" with "retail value" – for purposes of certain personal property valuations. **In re Pearsall,** 441 B.R. 267, 270 n.2 (Bankr. N.D. Ohio 2010).

- Sixth Circuit Example: **In re Thompson**, 538 B.R. 410, 416 (Bankr. E.D. Tenn. 2015) (Court found $5,225 for a vehicle was reasonable in a Chapter 7 redemption using the N.A.D.A. value of $5,425 minus $200 in needed repairs).

- Seventh Circuit Example: **In re Redpath**, 2009 WL 3242107, *1-*4 (Bankr. C.D. Ill. September 30, 2009) (Chapter 7 debtors filed a motion to redeem pick-up truck by paying creditor $16,000. Creditor objected, arguing the truck's FMV exceeded the proposed redemption price. The debtor sought a liquidation value for the truck, while the creditor proposed a replacement value equal to the truck's retail. The court, using the trucks retail sale price, found a redemption value of $20,500 based on testimony and minimal depreciation).

QUERY: What value does **Rash --** in light of **§ 506(a)(2) --** require the chapter 7 debtor to pay to redeem the vehicle? And when is it determined in light of the arguably contradictory language in the first and second sentences of **§ 506(a)(2)** – "replacement value as of the date of the petition" and "age and condition of the property at the time value is determined."

ANSWER: There is no consensus. *See* **In re Labostrie**, 2012 WL 6554727 (9th Cir. BAP. 2012) (not error for bankruptcy court to reply on NADA retail, minus adjustments for condition and mileage); **In re Perales,** 2012 WL 902790 (6th Cir. BAP 2012) (no error for bankruptcy court to accept Debtor's Edmunds.com private party value in absence of any evidence adduced by creditor and where creditor did not request an evidentiary hearing); **In re Thompson**, 538 B.R. 410, 416 (Bankr. E.D. Tenn. 2015) (Court found $5,225 for a vehicle was reasonable in a Chapter 7 redemption using the N.A.D.A. value of $5,425 minus $200 in needed repairs); **In re Meredith**, 2013 WL 4602966, Bankr. M.D. Pa. (August 29, 2013) (retail value of mobile home determined by comparable sales and NADA guide for mobile home values); **In re Griffin**, 2013 WL 781141 (Bankr. M.D.N.C. Mar. 1, 2013) (90% of NADA retail unless the debtor is prepared to offer evidence of a different value); *but see* **In re Nance**, 2013 WL 2897527 (Bankr. M.D.N.C. June 12, 2013) (in Chapter 13 case converted to Chapter 7, where debtor had paid more than 90% of the NADA retail value as of the petition date, court rejected debtor's argument that redemption amount was $0; debtor had to pay balance of contract price); **In re Pottinger,** 2012 WL 3561966 (Bankr. M.D.N.C. 2012) (denying unopposed motion to redeem for NADA trade in value.); **In re Pearsall**, 441 B.R. 267 (Bankr. N.D. Ohio 2010) (concluding that the "most probative evidence of the value of the vehicle for redemption purposes ... is the actual circumstances of its acquisition" which occurred less than one month before filing, minus adjustments); **In re Gehring**, 2011 WL 2619552 (Bankr. N.D. Ohio July 1, 2011) (rejecting 722. Redemption's appraisal where it didn't specify the trim on the vehicle and was unclear whether vehicle had even been inspected; noting that the most helpful and necessary information is: (1) year, (2) model, (3) trim, (4) options, (5) mileage, (6) condition, and (7) the basis, e.g., inspection or third party report, upon which the person makes the evaluation. This may be supplemented with arguments and evidence concerning variations or adjustments from retail price relating for conditioning expenses and the like.)

Vehicle Cramdown Examples:

QUERY: What is the appropriate value for chapter 13 cramdown in light of **§ 506(a)(2)?**

ANSWER: There is no consensus. **In re Nance,** 477 B.R. 638 (Bankr. E.D. La. 2012) (Among those who utilize the NADA Guide in determining the retail value of a vehicle under § 506(a)(2), four basic approaches have emerged.

1) Under the first, courts establish a presumptive retail value for the vehicle by deducting a certain percentage from the NADA Clean Retail value, *citing* **In**

re Cheatham, 2007 WL 2428046, *3 (Bankr. W.D. Mo. 2007); U.S. Bankr. Ct. Rules E.D. Mo., L.R. 3015–2 and Proc Manual.

2) Under the second, courts set the presumptive value of the vehicle at the full NADA Clean Retail value.

3) Under the third, courts make use of NADA (or Kelley Blue Book (KBB)) values as starting points but hold that the facts of each case determine which value (Clean Retail, Private–Party, etc.) should be used. *See* **In re McElroy**, 339 B.R. 185, 188-89 (Bankr. C.D. Ill. 2006) ("In the absence of evidence of the markup for services or the profit margin which might be included in the NADA tables" court used NADA table as a basis to find a reasonable price in vehicle); *but see* **In re Gonzalez**, 295 B.R. 584, 587 (Bankr. N.D. Ill. 2003) ("Prices in NADA are typically higher than Black Book or KBB because NADA prices do not vary with the vehicle's condition).

4) Finally, under the fourth approach, the one that the court has settled on, courts average the NADA Clean Retail and Clean Trade–In values for a vehicle of the same make, model, and year as the vehicle in question).

Sixth Circuit/Seventh Circuit Mobile Home Cramdown Examples

Section 1322(b)(2) allows a bankruptcy court to modify a secured creditor's rights with regard to any claim "other than a claim secured by a security interest in real property that is the debtor's principal residence." As the Sixth Circuit reasoned in **Reinhardt v. Vanderbilt Mortg. & Fin., Inc. (In re Reinhardt),** 563 F.3d 558, 564 (6th Cir. 2009), a mobile home is subject to cramdown when it retains the "personal property" characterization despite the debtor using the mobile home as his or her permanent residence.

Indiana Mobile Home: **In re Thornton**, 2016 WL 3092280 (Bankr. S.D. Ind. May 23, 2016) (Slip opinion) (creditor had secured claim on a debtor's mobile home. The debtors do not own the land beneath the home. The parties did not dispute the home is personal property acquired for personal, family, or household purposes. Using ***Rash***'s replacement value, NADA pricing guidelines, and expert testimony, the court found NADA's formulaic approach dispositive. The home's base value is adjusted by location, condition, cost of repairs, and any "add-on" components).

Kentucky Mobile Home: **In re Jude**, No. 15-10330, 2016 Bankr. Lexis 2387, *5-*10 (Bankr. E.D. Ky. 2016) (Court rejected a debtor's valuation of his mobile home at $18,468.77. The debtor did not introduce any credible evidence on a mobile home's value, and relied on his own opinion with regard to the home's value even though he based his own opinion on a purchased Value Report from NADA. The court used the **cost-approach** to determine the mobile home's replacement value. The appraiser used a point system as part of the NADA appraisal form to value the mobile home at $40,100.00. The appraiser first found a base value, and then applied numerous

adjustments accounting for the home's age, condition, accessories, and installed components).

8th Circuit Mobile Home Cramdown Examples

Missouri Mobile Home: **In re Coleman**, 373 B.R. 907 (Bankr. W.D. MO. 2007) the court's finding in *Coleman* is **superseded** by section 442.015.1 with respect to whether the manufactured home is considered to be real property. **Section 442.015.1** provides that under Missouri law a manufactured home *is* real property regardless of whether it is affixed to land. Thus, in Missouri a debtor's plan must not modify the treatment of a creditor's claim on a mobile home. **In re Turner**, No. 14-43032 2014 Bankr. Lexis 4817 at *5 (Bankr. W.D. Mo. 2014).

Kansas Mobile Home: In re Kollmorgen, 2012 WL 195200 (Bankr. D. Kan. Jan. 20, 2012) (For purposes of the amount of the secured creditor's claim in a chapter 13, Court rejected Debtor's appraiser's valuation of mobile home at $5,000; NADA value for manufactured home more closely approximated replacement value; value determined to be $16,700; Debtors used a "provisional licensed appraiser" whose appraisals had to be reviewed by a certified appraiser; appraiser had no training or certification specific to mobile homes and employed a market approach based on comparable sales but could give no specifics about adjustments except he relied on professional judgment. The creditor's appraiser was a certified mobile home appraiser, used a cost analysis with adjustments for condition).

Kansas mobile home: **In re Patricia Ann Little**, Case No. 12-12650 (Bankr. D. Kan. Sept. 24, 2013).

Sixth Circuit/Seventh Circuit Vehicle Cramdown Examples

Ohio Motor Vehicle: In re Wcislak, 417 B.R. 24 (Bankr. N.D. Ohio 2009) (When faced with competing, contradictory evidence offered by a debtor and creditor in determining a vehicle's replacement value section 506(a)(2) requires a valuation analysis based on the facts presented in each case. Blue book guidelines provide a neutral and independent source of a vehicle's value, but are not conclusive. Thus, blue book guidelines coupled with expert testimony is the proper course of action for a court to determine a vehicle's price in a Chapter 13 cramdown).

- **In re Getz**, 242 B.R. 916, 920 (6th B.A.P. 2000) (Upheld bankruptcy court's factual finding that the replacement value of a vehicle was the average of N.A.D.A wholesale and retail values, and was consistent with ***Rash***)

Michigan Motor Vehicle: In re McCutchen, 224 B.R. 373, 375 (Bankr. E.D. Mich. (1998) (In determining a vehicle's cramdown value, ***Rash*** suggests that "the starting point must be what it would cost this particular debtor to go out and obtain an automobile of like age and condition." In the absence of evidence from or on behalf of a debtor, *Rash* requires the following evaluation:

1. Stated "retail" value (plus or minus appropriate adjustments by reason of the presence or absence of equipment or accessories affecting retail value)

2. Less: the sum of: (a) any appropriate high mileage deduction in accordance with the publication involved; and (b) any portion of retail value that can be shown to represent reconditioning or repair costs; and (c) any portion of the retail value which by credible evidence can be shown to be attributable to the cost or value of any warranty or guaranty.

Illinois Motor Vehicle 7th Circuit: In re Jones, 219 B.R. 506, 508 (Bankr. N.D. Ill. 1998) (Appropriate date for determining a vehicle's value is the confirmation date because the amount of a secured claim may change during the bankruptcy case.); *but see* **In re Gonzalez**, 295 B.R. 584, 590 (Bankr. N.D. Ill. 2003) (Court rejected all "starting points" and "rules of thumb" in determining "value." The court reasoned that "replacement value" means the price a willing buyer like the debtor would pay for property at issue.) *See also***, In re Scott**, 248 B.R. 786, 793 n.7 (Bankr. N.D. Ill. 2000) (replacement value of the collateral can be determined easily on the date of confirmation).

Wisconsin Motor Vehicle: **In re Engebregtsen**, 337 B.R. 677, 677-79 (Bankr. E.D. Wis. 2005) (In this case, the debtors intended to surrender the vehicle to the creditor. The court reasoned section 502(b) governs the date of determining the amount of a claim when the debtor opposes. Section 502(b) provides if a debtor objects to a creditor's claim, the court shall determine the amount of such claim as of the ***petition date***. The creditor filed both a secured and unsecured claim. Thus, the court proceeded to section 506(a). Since the debtors intended to surrender the vehicle, the court used the liquidation value of the vehicle to determine the creditor's claim. However, had the debtor's intended to keep the vehicle and utilize cramdown, the court would have still found the petition date as the date of determining the value of the vehicle).

8th Circuit Vehicle Cramdown Examples

Kansas Motor Vehicle: In re Feagans, 2006 W.L. 6654576 (Bankr. D. Kan. Oct. 18, 2008 (value of vehicle for purposes of cramdown in Chapter 13; Debtor failed to appear; creditor presented retail merchant in car sales; Court notes that NADA and Kelly Blue Book don't necessarily determine retail value; witness referred to NADA, but testified she would sell the car off her lot for less; court used that value ($3,000 less than NADA), and deducted costs of repairs and reconditioning).

In re De Anda-Ramirez, 359 B.R. 794 (10th Cir. BAP 2007) (not error for court to rely on KBB private party instead of KBB retail)

Sale of Asset Examples:

QUERY: Does **Rash** require liquidation or replacement value when a Chapter 7 trustee sells assets at a **§ 363** sale?

ANSWER*:* Bankruptcy court properly applied replacement and not liquidation value standard in valuing assets sold by a Chapter 7 Trustee at

a **§ 363** sale, since the business was being sold as a going concern. **In re Adam Aircraft Industries, Inc.**, 2013 WL 773044 (Bankr. D. Colo. Feb. 28, 2013) *aff'd* 532 B.R. 814 (D. Co. 2015). **In re Engman**, 395 B.R. 610, 625 (Bankr. W.D. Mich. 2008) ("The court's obligation in §363(b) sales is to assure that optimal value is realized by the estate under the circumstances." In addition, "A duty is imposed upon the trustee to maximize the value obtained from a sale, particularly in liquidation cases").

QUERY: How do you allocate value when assets are not sold as part of one sale?

ANSWER: In determining whether a compromise over the amount of creditor's super-priority claim, based on a sale of assets, was reasonable, district court affirms the bankruptcy court's approval; bankruptcy court had valued the assets that were sold at a **§ 363** sale as a going concern value with respect to the portion of the business that was being sold as a going concern, and had valued the remainder of the assets, that were liquidated, at the appropriate liquidate value; rejecting the objecting parties' argument on appeal that, as a matter of law, the bankruptcy court should have considered liquidation value only in valuing the assets. **In re SK Foods, L.P.,** 487 B.R. 257 (E.D. Cal. 2013)

Real Estate Examples:

QUERY: For purposes of Chapter 12 confirmation, does **Rash** require farmland to be valued as farmland or at its more valuable use as vacant development property?

ANSWER: District court affirmed bankruptcy court's refusal to give bank's appraiser's testimony any weight, when appraiser valued farmland at its highest and best use as vacant development land; under **Rash**, the appraisal did not take into account "the proposed disposition and use" of the property as farmland, given that the Chapter 12 debtor intended to continue farming it. **In re Southall, III**, 475 B.R. 275 (M.D. Georgia 2012). *But see*, **In re Bell**, 304 B.R. 878, 880-81 (Bankr. N.D. Ind. 2003) (Court rejected chapter 12 debtor's argument that since they are farmers who wanted to keep the property and continue farming operations, the court should consider only its value as a farm. The court reasoned, under ***Rash***, value is based upon "what the debtor would have to pay for comparable property." Here, the debtors rely on their own contemplated use. "A buyer who is willing to devote the property to a higher and better use will be willing to offer a higher price than one not interested in using the property to its best advantage. These market pressures influence land's value).

QUERY: For purposes of determining extent of judgment creditor's lien in single family homes Debtor used as residential care facilities, does **Rash** require valuation of the homes as residences or as residential care facilities?

ANSWER: Rash says that the first step is to determine the creditor's interest in the estate's interest before valuing that interest; a judgment lien creditor had no interest in the stream of income or business generated on the property -- therefore, the lien was just on the real estate; so valuation as single family residences, rather than as higher- valued, income generating residential care facilities was more appropriate, particularly where the homes had not been improved as residential care facilities and the license was not transferable. **In re De Leon**, 2013 WL 3805733 (Bankr. N.D. Cal. July 18, 2013).

QUERY: In context of Chapter 11 confirmation, does **Rash** require consideration of the value of low income housing credits in valuing the real estate, when the Debtor asserts the creditor doesn't have a lien in tax credits?

ANSWER: In re Lewis and Clark Apartments, L.P., 479 B.R. 47, 52-53 (8th Cir. BAP 2012); legal error for bankruptcy court not to have considered tax credits in valuing property. Ultimately, both the benefits and burdens associated with property ownership are relevant in valuing the real property. **In re Creekside Senior Apartments, L.P.**, 477 B.R. 40, 58 (6th Cir. B.A.P. 2012).

QUERY: Debtor's Chapter 11 plan proposes to pay the EPA and relieve the debtor of the cleanup liability. Does **Rash** require the court to value the property as though it is still contaminated?

ANSWER: The court has to value the property as it exists in the debtor's hands and for the debtor's use; appropriate to discount the value on account of its environmental contamination. This valuation method does not include any consideration of factors that are particularly unique to the debtor, such as the negotiated exemption with the EPA. **In re Arden Properties, Inc**., 248 B.R. 164 (D. Ariz. 2000).

QUERY: For purposes of stripping of IRS lien attached to debtor's TBE interest in house owned with non-filing spouse who doesn't owe taxes, does **Rash** require a $0 value since no willing buyer would buy the debtor's interest?

ANSWER: Broker testified that debtor would have limited ability to sell his interest in the house doesn't render his interest worthless; **Rash** focuses on a willing buyer in the debtor's situation; the debtor's situation is as an owner of a TBE property, not a third party purchaser; his marriage is sound; his actual use, rather than what he could sell his interest for, is the measure of value. **In re Basher,** 291 B.R. 357 (Bankr. E.D. Pa. 2003) *rejected by* **Popky v. U.S., 419 F.3d 242, 245 (3rd Cir. 2005)** (Third Circuit rejected debtors' use of ***In re Basher*** in valuing a tenant's interest in entireties by way of life expectancies. "As the District Court correctly observed, 'the equal division of assets between spouses ... parallels the distribution of entireties property when an entireties estate is severed because of a sale with consent of both tenants, divorce or other reasons.'")

V. Now That You Understand *Rash*, How Do You Put on Value Evidence? -- The FREs

FRE 104(a) – Preliminary Questions

The court must decide any preliminary question about whether a witness is qualified, a privilege exists, or evidence is admissible. In so deciding, the court is not bound by evidence rules, except those on privilege.

In valuation context: court must be satisfied both that such items are of the type actually relied upon by experts in the field AND that such items are sufficiently trustworthy to much such reliance sufficiently trustworthy – cross reference to **FRE 703**

FRE 403 – Excluding Relevant Evidence

The court may exclude relevant evidence if its probative value is substantially outweighed by a danger of one or more of the following: unfair prejudice, confusing the issues, misleading the jury, undue delay, wasting time, or needlessly presenting cumulative evidence.

FRE 701 – Opinion Testimony by Lay Witness

If a witness is not testifying as an expert, testimony in the form of an opinion is limited to one that is:
(a) rationally based on the witness's perception;
(b) helpful to clearly understanding the witness's testimony or to determining a fact in issue; and
(c) not based on scientific, technical, or other specialized knowledge within the scope of Rule 702.

FRE 702 – Testimony by Expert Witnesses

A witness who is qualified as an expert by knowledge, skill, experience, training or education may testify in the form of an opinion or otherwise if:

(a) the expert's scientific, technical, or other specialized knowledge will help the trier of fact to understand the evidence or to determine a fact in issue;

(b) the testimony is based on sufficient facts or data;

(c) the testimony if the product of reliable principles and methods; and

(d) the expert has reliably applied the principles and methods to the facts of the case

FRE 703 – Bases of an Expert's Opinion Testimony

An expert may base an opinion on facts or data in the case that the expert has been made aware of or personally observed. If experts in the particular field would reasonably rely

on those kinds of fact or date in forming an opinion on the subject, they need not be admissible for the opinion to be admitted.

-this is a preliminary question for the Court under Rule 104(a). In determining whether reliance by the expert is reasonable, the court must be satisfied both that such items are of the type actually relied upon by the experts in the field AND that such items are inherently trustworthy to make such reliance reasonable. Russell, Rule 703.
-can rely on hearsay, but it is not substantive evidence

FRE 705 – Disclosing the Facts or Data Underlying an Expert's Opinion

Unless the court orders otherwise, an expert may state an opinion – and give reasons for it – without first testifying to the underlying facts or data. But the expert may be required to disclose those facts or data on cross-examination.

FRE 706 – Court-Appointed Expert Witnesses

On a party's motion or on its own, the court may order the parties to show cause why expert witnesses should not be appointed…

FRE 803(17)- excepts from the hearsay rule market compilations generally used and relied upon by the public

Rule 26(a)(2)(A) –party must disclose the identity of any witness it may use at trial to present evidence under **FRE 702, 703** or **704**; **(a)(2)(B)** – the disclosure must be accompanied by a written report if the witness is retained or specially employed to provide expert testimony or whose duties as the party's employee regularly involve giving expert testimony.

In sum:

FRE 104: preliminary question: whether expert testimony could assist the trier of fact in understanding the evidence or determining a fact in issue.

Second, whether the witness called is properly qualified to give the testimony sought.

Expert Testimony subject to exclusion under **FRE 403** on grounds of unfair prejudice or waste of time

Daubert v. Merrell Dow Pharmaceutical, Inc., 509 U.S. 570, 597, 113 S.CT. 2786, 125 L.Ed.2d 469 (1993)**:** under **FRE 104**, must make a preliminary assessment of whether the testimony's underlying methodology is scientifically valid and properly can be applied to the facts of the case

VI. Practical Strategic, Evidentiary, & Other Considerations

►***Motion v. Adversary? Fed. R. Bankr. P. 3012:*** "The court may determine the value of a claim secured by a lien on property in which the estate has an interest on motion of any party in interest and after a hearing on notice to the holder of the secured claim and any other entity as the court may direct." Valuation of collateral may be established through the confirmation process if proper notice is given to creditors. **Bennett v. Springleaf Fin. Serv**., 466 B.R. 422 (Bankr. S.D. Ohio). *Compare* **Fed. R. Bankr. P. 7001(2)** (a proceeding to determine the validity, priority, or extent of a lien or other interest in property, other than a proceeding under **Rule 4003(d**)).

►***Burden of Proof -***Neither the Code nor the Federal Rules of Bankruptcy Procedure allocates the burden of proof as to the value of secured claims under **§ 506(a).** There are three approaches to the burden of proof: (1) secured creditor bears the burden of proof; **In re Sneijder**, 407 B.R. 46, 55 (Bankr. S.D.N.Y. 2009); (2) the party challenging the value of a claim, usually the debtor, bears the burden of proof; and (3) burden-shifting analysis, e.g., the debtor bears the initial burden of proof to overcome the presumed validity and amount of the creditor's secured claim, but the ultimate burden of persuasion is upon the creditor to demonstrate by a preponderance of the evidence both the extent of its lien and the value of the collateral securing its claim. The circumstances will dictate the assignment of the burden of proof on the question of value. **In re Herrara**, 454 B.R. 559 (Bankr. E.D.N.Y. 2011) (adopting the burden shifting approach) (debtor had burden of proof on redemption to prove it more likely than not that the value of vehicle was $6500 as proposed; debtor's evidence not credible, where it consisted of NADA guide for a different model)

► ***Standard of Review*** – is a mixed question of law and fact. *E.g*., **In re Lewis and Clark Apartments, L.P**., 479 B.R. 47, 50 (8th Cir. BAP 2012); **In re Abbotts Dairies of Pennsylvania, Inc.**,788 F.2d 143, 149 (3rd Cir. 1986).

► ***Finality for Purpose of Appeal -*** An order determining the value of property pursuant to **11 U.S.C. § 506(a)** is a final order for purposes of appeal if the valuation was made for purposes of plan confirmation. **In re Creekside Senior Apartments, LP**, 477 B.R. 40, 45 (6th Cir. BAP 2012); Since the determination of value was not needed for the stay relief motion, and since the court had not yet ruled on confirmation, the determination as to value was not a final order; granting leave for the appeal to proceed on an interlocutory basis. **In re Lewis and Clark Apartments, L.P**., 479 B.R. 47, 5-52 (8th Cir. BAP 2012). Recently the Seventh Circuit in ***In re Ferguson***, No. 15-3093, 2016 WL 4440508 (7th Cir. August 23, 2016), dismissed a bankruptcy case for lack of jurisdiction under 28 U.S.C. § 158. The Seventh Circuit found the appeal of a district court's order remanding the case back to the bankruptcy court was not final. The court reasoned "[i]t isn't enough, then, to say the bankruptcy court's order was final—we must consider the *district* court's order." *Id*. at *2. "A remand is not final, and therefore not appealable, unless only ministerial acts remain for the bankruptcy court." *Id*. The parties did not know what action the bankruptcy court had to take on remand. *Id*.

►***Local Rules/Continuances:*** Emergency motion to continue valuation hearing denied. Valuation hearing could continue without the debtors because they had scheduled an expert witness to testify. **In re Cumella,** 2013 WL 4441588 (Bankr. M.D. Fla. Aug. 19, 2013); *compare* **McCarron** (continuance denied); expert reports not admitted when not filed or presented in accordance with local rules. **In re Cocreham**, 2013 WL 4510694 (Bankr. E.D. Cal. Aug. 23, 2013)

► ***Weight Given to Expert Testimony -*** The determination of the weight to be given expert testimony or evidence is a matter within the discretion of the trier of fact – which in a nonjury proceeding like the instant case is the bankruptcy court. **Fox v. Dannenberg**, 906 F.2d 1253, 1256 (8th Cir. 1990). Valuation is ultimately the opinion of a particular appraiser and, as such, the weight to be accorded the opinion rests upon a number of factors frequently used by courts in evaluating appraisal testimony. A nonexclusive listing of these factors includes: The appraiser's education, training, experience, familiarity with the subject of the appraisal, matter of conducting the appraisal, testimony on direct examination, testimony on cross-examination, and overall ability to substantiate the basis for the valuation presented. **In re Creekside Senior Apartments, LP**, 477 B.R. 40, 61 (6th Cir. B.A.P. 2012). First, the court determines if the proposed expert qualifies as an expert. **In re Lakes States Commodities, Inc.**, 271 B.R. 575, 587 (Bankr. N.D. Ill. 2002) (Court gave no weight to expert's report when there were no additional facts in the record supporting his report).

► ***Considerations For Assessing Conflicting Expert Testimony*:** The valuation of property is an inexact science and whatever method is used will only be an approximation and variance of opinion by two individuals does not establish a mistake in either. **Boyle v. Wells (In re Gustav Schaefer Co.)**, 103 F.2d 237, 242 (6th Cir. 1939). "Because the valuation process often involves the analysis of conflicting appraisal testimony, a court must necessarily assign weight to the opinion testimony received based on its view of the qualifications and credibility of the parties' expert witnesses. **In re Smith**, 267 B.R. 568, 572 (Bankr. S.D. Ohio 2001).

►***Court Not Bound By Either Appraisal*** --A bankruptcy court is not bound to accept the values contained in the parties' appraisals; rather, it may form its own opinion of the value of the subject property after considering the appraisals and expert testimony. **In re Smith**, 267 B.R. 568, 572-73 (Bankr. S.D. Ohio 2001). *But see* **In re Byington,** 197 B.R. 130, 138 (Bankr. D. Kan. 1996). The court believes that it must review the testimony, the credibility of the witnesses and all supporting evidence, and accept one of the proffered values. It recognizes that a number of courts typically hear all the experts and then arrive at a value somewhere in the range offered. Logically, this approach makes no sense. In effect, the court is believing both (or all) of the experts testifying. Logically, the court should determine which of the experts is most credible and accept that value . . . . No court hears experts on causation and finds that the defendant "sort of" caused the injury. Recognizing that the averaging approach is unassailable on appeal as long as the valuation "found" by the trial court is within the range of evidence.; also, a discussion of use of market guides, such as NADA, which is admissible under **FRE 803(17).**

► ***Owner Testifying As To Value***: Debtor as owner competent to offer a lay opinion of value **FRE 701**, where the debtor is shown to be familiar with the property or its value; the owner of real property has the benefit of a presumption that he is familiar with or has knowledge of, the property and its value, but the presumption is rebuttable. But, unless the debtor is qualified as an expert, the debtor cannot testify as to the types of information that an appraiser would rely on, such as what others have told him concerning the value of his or comparable properties. **In re Cocreham**, 2013 WL 4510694 (Bankr. E.D. Cal. Aug. 23, 2013). When an expert offers an opinion of value, the lay opinion of the debtor is typically found to be less credible. **In re Wilson**, 378 B.R. 862 (Bankr. D. Mont. 2007). *Compare* **In re Cocreham**, 2013 WL 4510694 (Bankr. E.D. Cal. Aug. 23, 2013) (court found creditor's real estate broker's testimony not credible, where he was only familiar with an urban area, and had no experience in the remote, rural area where debtor's property was located; methodology was suspect, because he simply looked for residential property near the subject property, and made no adjustments to account for the differences in the property; and his comparable sales including listings, not actual sales; in the court's experiences, sellers are frequently willing to accept less than asking price) *with* **McDuffie v. West (In re West),** 2016 Bankr. Lexis 109237, *6-*10 (E.D.N.C. July 15, 2016) (Homeowner may not opine to value of home, when the sole basis for the opinion is a tax assessment prepared by a third party. A lay opinion must be based on the witness's perception. Here, the debtor did not express any subjective opinion or belief as to the property's value).

► ***Corporate Representative Not Qualified as Owner*** **-** the presumption that an owner of property is qualified to give his opinion as to its value does not extend to officers of corporate owners of land. **DiPietro v. Boynton**, 628 A.2d. 1019 (Me. 1993); ***Southern Missouri Dist. Council of Assemblies of God v. Hendricks***, 807 S.W. 2d 141 (Mo. Ct. App. 1991).

►***Non-owner, non expert may not testify as to value under FRE 701, 702*****.** **In re Cocreham**, 2013 WL 4510694 (Bankr. E.D. Cal. Aug. 23, 2013).

► ***Zillow.com or Internet Evidence*** **-** Zillow.com and other similar internet based sources are hearsay, **FRE 801**. Zillow.com is not a market compilation under **FRE 803(17)**; it is a participatory site; a homeowner with no technical skill beyond the ability to surf the web can log in to Zillow and add or subtract data that will change the value of his property; therefore, it is inherently unreliable. **In re Cocreham**, 2013 WL 4510694 (Bankr. E.D. Cal. Aug. 23, 2013), *citing* **In re Darosa**, 442 B.R. 173, 177 (Bankr. D. Mass. 2010); **In re Phillips**, 491 B.R. 255, 260, n. 7 (Bankr. D. Nev. 2013); Zillow.com and other internet based sources not admissible; no foundation that these are market compilations generally used and relied upon by the public. **In re Cocreham**, 2013 WL 4510694 (Bankr. E.D. Cal. Aug. 23, 2013);

► ***Tax Assessment Evidence - In re McCarron*****,** 242 B.R. 479, 482 (Bankr. W.D. Mo. 2000) (for purposes of strip off of lien in Chapter 13; court accepted testimony of property manager who exhibited a thorough knowledge of the Debtor's property, the market for single family residences in the inner city of KC where the house was located; discounted the testimony of the County tax assessor because his valuation was prepared

for tax assessment purposes only, not for the purpose of determining present market value; he had not inspected the house and was not aware of its actual condition). *See also* **In re Slovak**, 489 B.R. 824, 826-827 (Bankr. D. Minn. 2013) ("Generally, the assessed value of a property for tax purposes is not considered direct evidence of a property's FMV").

►***Value in Schedules***: Court will accept a lender's unopposed allegation that a property lacks equity based on the value of that property set forth in a debtor's schedules; based on the fact that it is under oath and that an owner is competent to testify as to value. **In re Darosa**, 442 B.R. 173, 177 (Bankr. D. Mass. 2010), *citing* **Klapmeier v. Telecheck Intern, Inc**., 482 F.2d 247, 253 (8th Cir. 1973).

►***Auction*** - Generally speaking, an auction may be sufficient to establish that one has paid value but not if the bidding was collusive or notice inadequate. **In re Abbotts Dairies of Pennsylvania, Inc.,** 788 F.2d 143, 149 (3rd Cir. 1986)

►***Unaccepted Offer Not Evidence of Market Value***. "It is well settled that a mere offer, unaccepted, to buy or sell is inadmissible to establish market value." **Missouri Baptist Hosp. v. U.S.,** 213 Ct. Cl. 505, 555 F.2d 290, 298 (1977).

►***Summary Judgment:*** **In re Roach**, 2010 WL 234959 (Bankr. W.D. Mo. Jan. 15, 2010). For purposes of Chapter 13 modification of mortgage, Court concludes date of confirmation is date for valuation of the home, notwithstanding delay in getting to confirmation and the fact that value had declined; creditor should have asked for adequate protection. Debtor's evidence of written appraisal report and Bank's evidence of tax assessment value present conflicting evidence which renders summary judgment on the issue of value not warranted.

►***An unverified statement of an appraiser is hearsay*** and is not competent evidence as to the value of real property. **In re Light**, 2006 WL 3832810 (Bankr. E.D. Mo. Dec. 28, 2006), citing **FRE 801(c).**

►***Fair & Equitable/Chapter 11***: For purposes of extinguishing debtor's equity interests; bankruptcy court did not err in relying on appraisal compiled by a recognized expert according to accepted professional standards and used an accepted valuation method – income capitalization – that incorporated anticipated future profits and the anticipated reversion value into the final present going concern value of the estate. **In re Westpointe, L.P**., 241 F.3d 1005, 1008 (8th Cir. 2001)

► ***Budget Not Evidence of Value in Chapter 11 --*** **In the Matter of Heritage Highgate, Inc**., 449 B.R. 451 (D. N. Jersey 2011), *aff'd* 679 F.3d 132 (3rd Cir. 2012) (confirmation of plan did not automatically transform budget, which was intended to establish feasibility, into valuation of debtor's assets; budget projected future sales from anticipated completion of real estate project; value as of a future date is inconsistent with Rash; creditor argued that its claims should be deemed wholly secured because projections that accompanied the plan estimated that Debtor would generate enough income to pay them in full; also rejecting the "wait and see" approach to value -- it would

effectively do away with the bankruptcy court's obligation to determine value under **§ 506(a)**).

VII. Short Sales and Carve-out Agreements

►***Trustee's Duties:*** A Chapter 7 Trustee has a duty to "collect and reduce to money the property of the estate for which such trustee serves, and close such estate as expeditiously as is compatible with the best interest of parties in interest." 11 U.S.C. §704(a)(1).

- "A chapter 7 trustee is a fiduciary of the estate whose principal duty is to administer estate property so as to maximize distribution to unsecured creditors, whether priority or general unsecured." *In re Nave*, 2016 Bankr. LEXIS 1006, *25-26 (Bankr. C.D. Ill. Mar. 30, 2016). (quoting *In re All Island Truck Leasing Corp., No. 8-09-77670-REG*, 2016 Bankr. LEXIS 634, *7 (Bankr. E.D.N.Y. Mar. 2, 2016)).

►***Property of the Estate and Exemptions:*** Upon initiating a bankruptcy case pursuant to section 301, 302, or 303 of the Bankruptcy Code, a bankruptcy estate is created that is comprised of "all legal or equitable interests of the debtor in property, wherever located and by whomever held." 11 U.S.C. §541(a)(1). Unless property or rights to property are excluded from the bankruptcy estate pursuant to Section 541(b) or Section 541(c)(2), then it becomes property of the bankruptcy estate. Once the property comes into the bankruptcy estate, the debtor may exempt property **to the extent an exemption is applicable**. Further, "exemptions are determined as of the date the bankruptcy petition is filed." *In re Kaufman*, 2013 Bankr. LEXIS 519, *2 (Bankr. S.D. Ind. Feb. 7, 2013). (citing In re Lantz, 446 B.R. 850, 858 (Bankr. N.D. Ill. 2011)). See also *Owen v. Owen*, 500 U.S. 305, 314 n.6 (1991).

- Exemptions are subordinate to a secured creditor's lien on real property. 11 U.S.C. § 522(c)(2). *In re Brown*, 2015 Bankr. LEXIS 1026, *7 (Bankr. E.D. Mich. Apr. 1, 2015). Therefore, "if the amount of the secured debt exceeds the fair market value of the property such that there is no equity, the exemption is lost." *Brown,* 2015 Bankr. LEXIS 1026 at *7-8 (citing *In re Neal*, 424 B.R. 235, 236 (Bankr. E.D. Mich. 2010)).

►***Authority to Sell:*** A Chapter 7 Trustee has the power to sell property of the estate outside the ordinary course of business under Section 363(b)(1) of the Bankruptcy Code, which provides—"after notice and a hearing, [a trustee] may use, sell, or lease, other than in the ordinary course of business, property of the estate . . ." 11 U.S.C. §363(b)(1). With the consent of the secured creditors, a trustee may sell the property free and clear of liens. 11 U.S.C. § 363(f)(2). Therefore, if a deal is made between the Chapter 7 trustee and a debtor's secured creditors, a motion to sell real estate under Section 363 would

allow the trustee to sell the real estate **even where the sale proceeds would be insufficient to satisfy the liens in full**.[17]

- Traditionally, non-exempt real property that had no equity was abandoned by Chapter 7 Trustees because there would have been no benefit to the bankruptcy estate. However, it is becoming more common for Chapter 7 Bankruptcy Trustees to sell "underwater" real estate **if** a carve-out agreement can be successfully negotiated with the secured creditor and thereafter approved by the Bankruptcy Court.

- *In re Brown*, 2015 Bankr. LEXIS 1026, (Bankr. E.D. Mich. Apr. 1, 2015)—The Bankruptcy Court stated that it was "unaware of case law which would preclude an undersecured creditor from negotiating with the trustee for a sale in lieu of foreclosure. This is especially true where the sale will yield proceeds for the estate that would not otherwise be available. Such a sale is entirely consistent with the trustee's duties to the estate and does not come at the debtor's expense because the debtor had no equity to exempt on the date the case was filed." *Brown*, 2015 Bankr. LEXIS 1026 at *15. (citing *In re Bunn-Rodemann*, 491 B.R. 132 (E.D. Cal. 2013)).

- *In re KVN Corp.,* 514 B.R. 1 (9th Cir. BAP 2014)— "There is no per se rule that bans this type of contractual arrangement [carve-out agreements]: '[C]reditors are generally free to do whatever they wish with the bankruptcy dividends they receive, including to share them with other creditors.'" *In re KVN Corp*., 514 B.R. 1, 6 (B.A.P. 9th Cir. 2014). (quoting *Official Unsecured Creditors Comm. v. Stern (In re SPM Mfg. Corp.)*, 984 F.2d 1305, 1313 (1st Cir. 1992)). However, carve-out agreements "have been reviewed under a standard of heightened scrutiny due to past abuses." *KVN Corp*., 514 B.R. at 7. This "presumption of impropriety" is rebuttable— "the case law directs the following inquiry: Has the trustee fulfilled his or her basic duties? Is there a benefit to the estate; i.e., prospects for **a meaningful distribution to unsecured creditors**? Have the terms of the carve-out agreement been fully disclosed to the bankruptcy court? If the answer to these questions is in the affirmative, then the presumption of impropriety can be overcome." *Id*. at 8.

- "[A] carve-out that merely benefits administrative professionals is improper." *In re All Island Truck Leasing Corp*., 546 B.R. 522, 533 (Bankr. E.D.N.Y. 2016). (citing *KVN Corp*, 514 B.R. at 6-8)

- *U.S. DOJ Exec. Office for U.S. Trs., Handbook for Chapter 7 Trustees*, p. 4-14 (2012)—"A trustee may sell assets only if the sale will result in a meaningful distribution to creditors. In evaluating whether an asset has equity, the trustee

[17] There are companies that will assist in analyzing whether certain "underwater" properties would be good candidates for a short sale. For example, BK Global (www.bkginc.com) advertises a system that allows them to negotiate these types of short sales, and market the properties for the Chapter 7 Trustee.

must determine whether there are valid liens against the asset and whether the value of the asset exceeds the liens. The trustee may seek a 'carve-out' from a secured creditor and sell the property at issue if the 'carve-out' will result in a meaningful distribution to creditors. The trustee must also consider whether the cost of administration or tax consequences of any sale would significantly erode or exhaust the estate's equity interest in the asset. If the sale will not result in a meaningful distribution to creditors, the trustee must abandon the asset."

► ***Benefits to Secured Creditor:*** Several factors could motivate a secured creditor to agree to pay the bankruptcy estate a portion of the proceeds from a short-sale of property by the Chapter 7 trustee. Those factors may include the following—

- "Once the creditor becomes the owner [through foreclosure process], it has to take on the responsibility of being an owner, including, (1) evicting the borrower/former owner, (2) managing the property as an asset of the creditor, (3) paying insurance, property taxes, and utilities, (4) employing people or third-party vendors to secure, repair, and maintain the property while it is being marketed, and (5) engaging a real estate broker to sell the property." *In re Bunn-Rodemann*, 491 B.R. 132, 135 (Bankr. E.D. Cal. 2013);

- Avoid the expense of a state-court foreclosure proceeding,—what a secured creditor has to give up in a carve-out agreement may be similar to, or less than, fees and expenses otherwise incurred in a state-court foreclosure;

- Avoid the time consumer state-court foreclosure proceeding, including applicable consumer protection procedures—a Chapter 7 Trustee may be able to liquidate the real estate much quicker than a state-court foreclosure proceeding, through either a private sale or auction process.

- Avoid or reduce risks associated with questionable validity of creditor's secured status or balance owed on the secured debt;

- Secured creditor may have other collateral from which to recover payment of the debt;

- Multiple secured creditors with competing priority claims; and

- Real estate can best be marketed through a sale by the bankruptcy estate.

►***Benefits to the Debtor:*** The debtor may be able to negotiate for incentives related to the maintenance and marketing of the property. "Most likely, a trustee wants a debtor to remain in physical possession, keeping the property insured and protected as an occupied home. The debtor would like to stay in possession, paying only the current insurance and maintenance costs, allowing the debtor to avoid paying rent for housing and delaying moving expenses during the first months of a Chapter 7 fresh start." *Bunn-Rodemann*, 491 B.R. at 137. Further, the debtor and secured creditor will likely want the debtor to

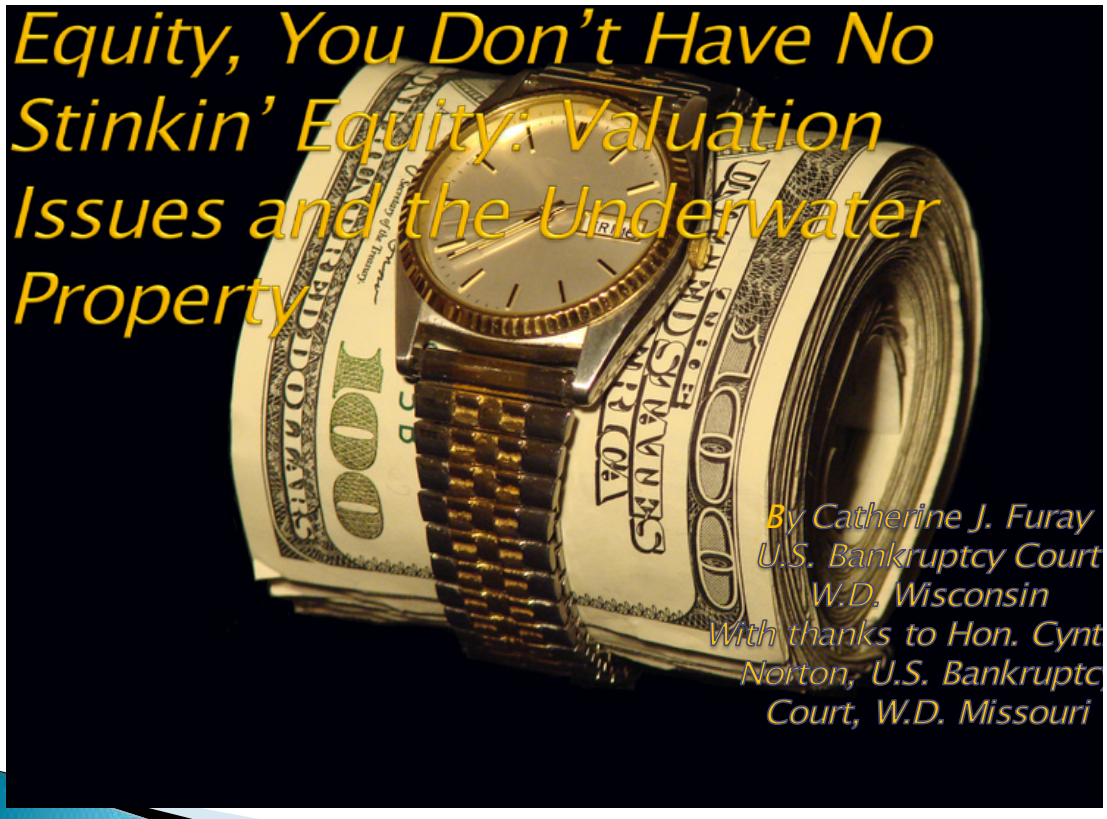
occupy the property in a manner that will "maximize the short-sale proceeds," which would likely maximize the estate's "incentive payment" for conducting a short sale. *Id*. "Additionally, the trustee and creditor want a debtor to not only cooperate with the real estate broker for the estate and the marketing efforts, but to voluntarily move out of the property after the short-sale is completed so that the buyer can immediately take possession of the property." *Id*. "While the no-rent incentive may balance paying the current insurance and maintenance expense, that may not be sufficient incentive for a debtor to cooperate with the trustee and creditor for the short-sale. A debtor may negotiate for a portion of the 'incentive payment,' including moving expenses." *Id*. Other benefits to the debtor include the following—

- Payment of priority debts;
- Payment of debts for which co-debtors or guarantors might be liable; and
- Avoidance of a protracted foreclosure case during which the debtor is the owner of the property and liable for home owners' association dues and zoning violations.

►***Debtor cannot claim exemption to receive short-sale proceeds (majority view)*:** Both the Fourth and Sixth Circuit Courts of Appeals have determined that a debtor cannot realize any return on a claimed exemption of a carve-out from the proceeds of a short-sale. See *Reeves v. Callaway (In re Reeves)*, 546 Fed. Appx. 235 (4th Cir. 2013); *In re Baldridge*, 553 Fed. Appx. 598 (6th Cir. 2014). Although *Reeves* and *Baldridge* are both unpublished cases, and therefore do not constitute binding precedent, they represent the only discussions of this type of exemption issue at the Circuit Court level, and are the most reliable predictors of how those courts would rule in published cases. See *Brown*, 2015 Bankr. LEXIS 1026, at *3-4 and fn 2.

- *Reeves*— The Fourth Circuit concluded that the debtors' exemption was subordinate to the first mortgage lien and the federal tax lien. *Reeves*, 546 Fed. Appx. at 241-42. Thus, effectively, there was no value to which the exemption could attach.
- *Baldridge*— The Sixth Circuit held that the carve-out agreement, which was recovered by the trustee upon closing the sale of the debtors' property, was not part of the bankruptcy estate and therefore could not be subject to the debtors' exemptions at the time the bankruptcy case was commenced. Further, the court held that the trustee had the authority to waive the right of redemption as a condition of the sale. Finally, the court held that inasmuch as the sale proceeds were insufficient to satisfy the obligations owed to the secured creditors, there was no residual equity in the property to which the debtors' exemptions could attach. *Baldridge*, 553 Fed. Appx. at 598-99.
- *In re Wilson*, 494 B.R. 502 (Bankr. C.D. Cal. 2013) (minority view)—The court allowed the debtor to claim a wild-card exemption in the "underwater" properties

sold by the Chapter 7 Trustee at short-sale, concluding that the debtor's exemptions attached to the properties themselves rather than the carve-outs. *Wilson*, 494 B.R. at 505. The carve-outs were simply the means by which the bankruptcy estate was acquiring funds that were subject to the exemptions. *Id*.



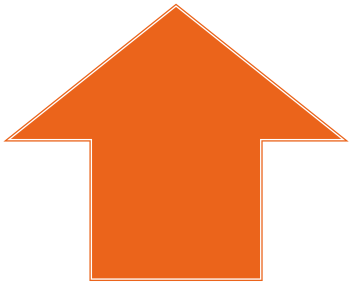
Why Do We Care?

- Stay relief
- Sales
- Value of exemptions
- Lien avoidance
- Discharge
- Avoidance
- Abandonment
- Cramdown
- Strip Off
- Liquidation Analysis

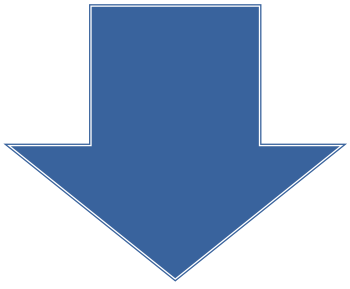
Valuation Principles – Part I

- Many meanings of "Value"
- The G/R: Code doesn't define "Value"
- A few exceptions, discussed below
- "Value" incorporates a consideration of Time/Timing
- The G/R: Code doesn't fix the date for determining "Value"

Valuation Principles – Part II



High Values



Low Values

Secured Claim Exception: § 506(a)(1)

- An allowed claim … secured by a lien … is a secured claim to the extent of the *value* of such creditor's interest … .
- Such value shall be determined in light of *the purpose of the valuation*
- and of the *proposed disposition* or use of such property
- and *in conjunction with any hearing* on such disposition or use or on a plan affecting such creditor's interest

Rash: Cramdown = Replacement Value

- **Or, "the price a willing buyer in the debtor's trade, business, or situation would pay a willing seller to obtain property of like age and condition"**

RASH: Two-Step Process

- **First:** Determine the creditor's interest in the estate's interest in the property
- **Second**: Determine how to value the interest

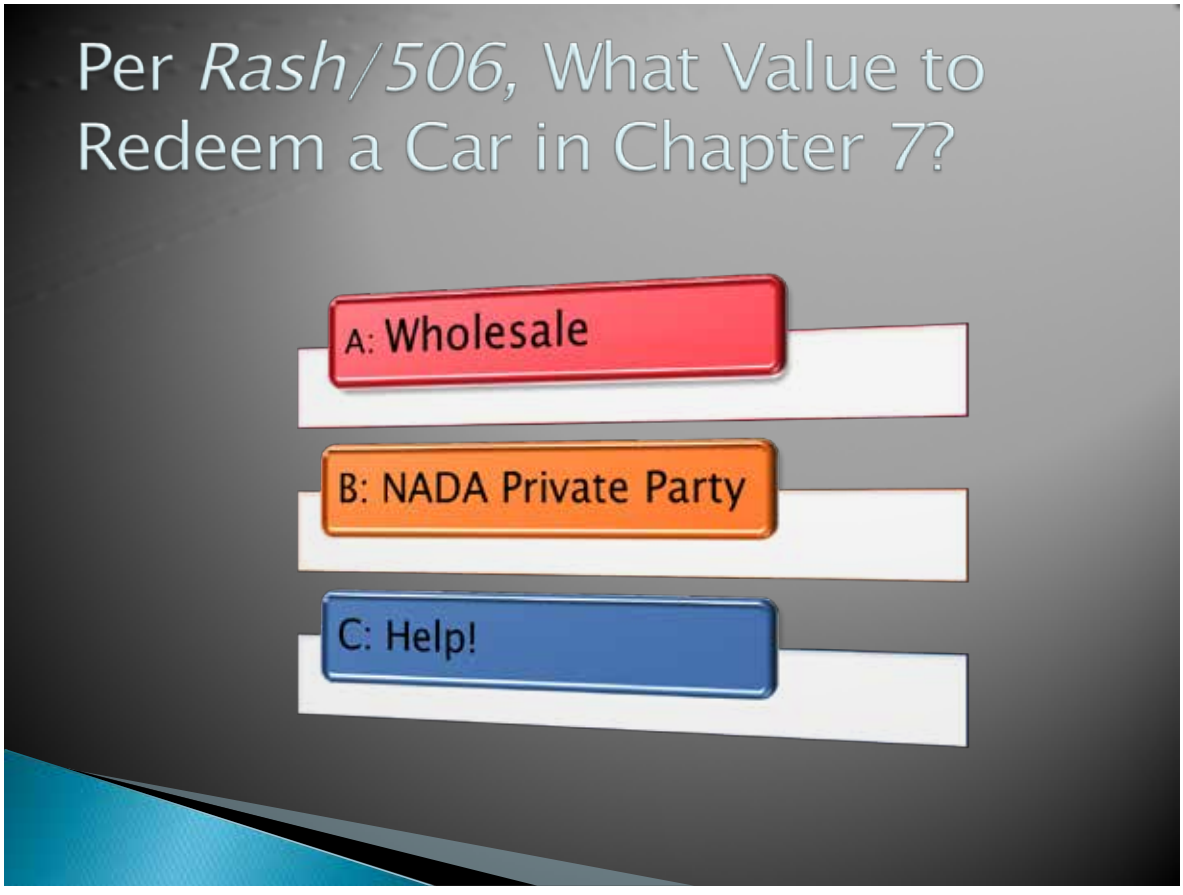
BAPCPA: § 506(a)(2) INDIVIDUAL PERSONAL PROPERTY VALUATIONS

- Individual Debtors in *7 or 13*
- Secured *personal property* claims
- Shall be determined based on *replacement value*
- As of the *date of the filing* of the petition
- *Without deduction* for costs of sale/marketing

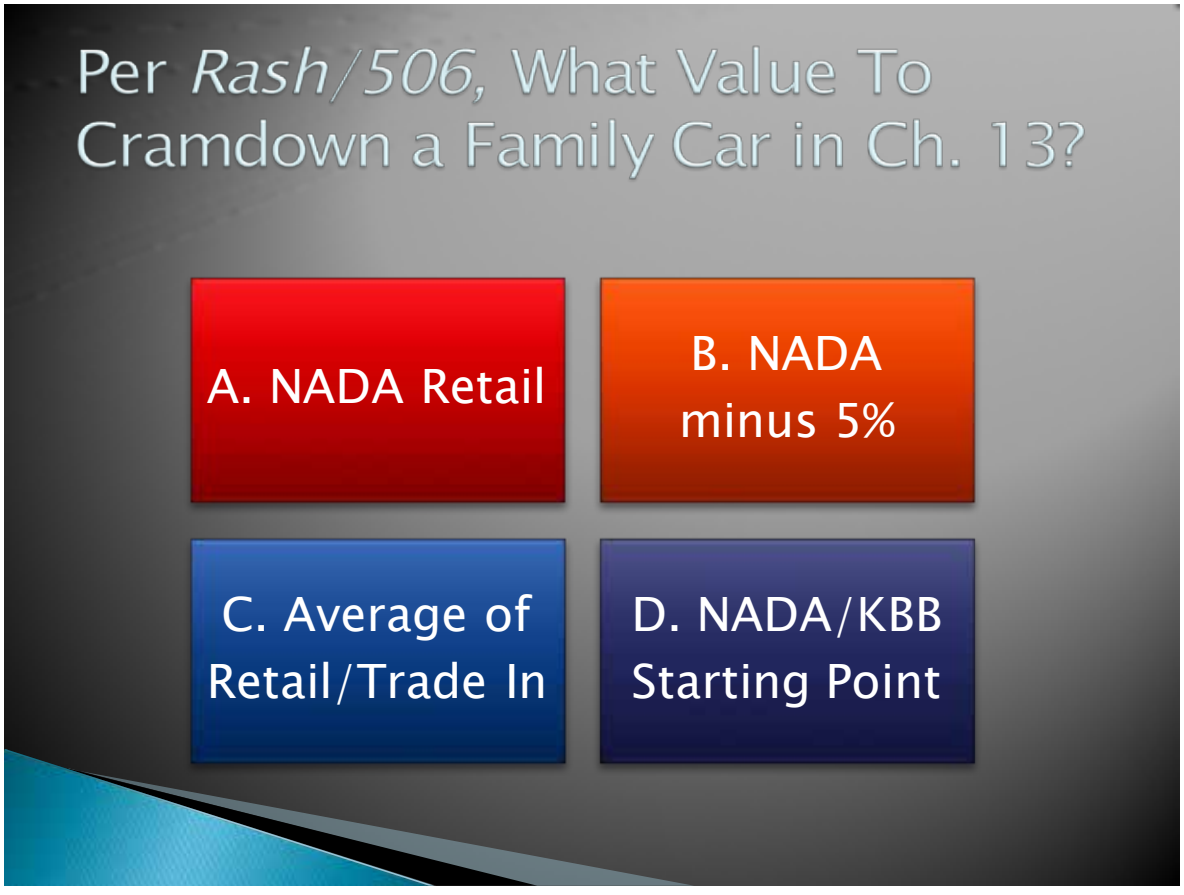
Replacement Value: Defined For Property Acquired for Personal, Family or Household Purposes

- The price
- A retail merchant
- Would charge for property of that kind
- Considering the age and condition
- Of the property
- At the time value is determined


Category I: Vehicles


Per *Rash/506*, What Value to Redeem a Car in Chapter 7?
A: Wholesale
B: NADA Private Party
C: Help!

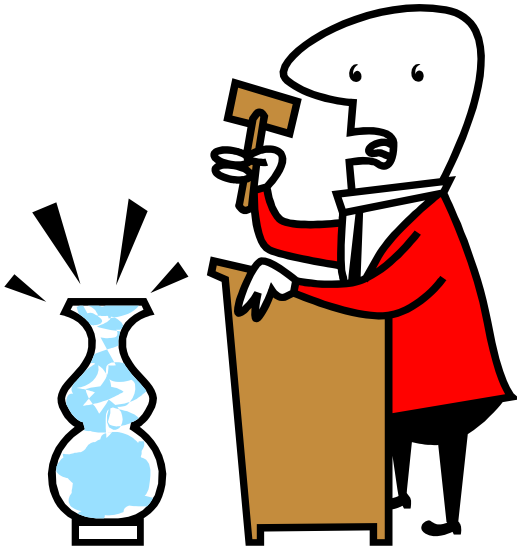

The Answer is: (Courts are Split)
C: Help!

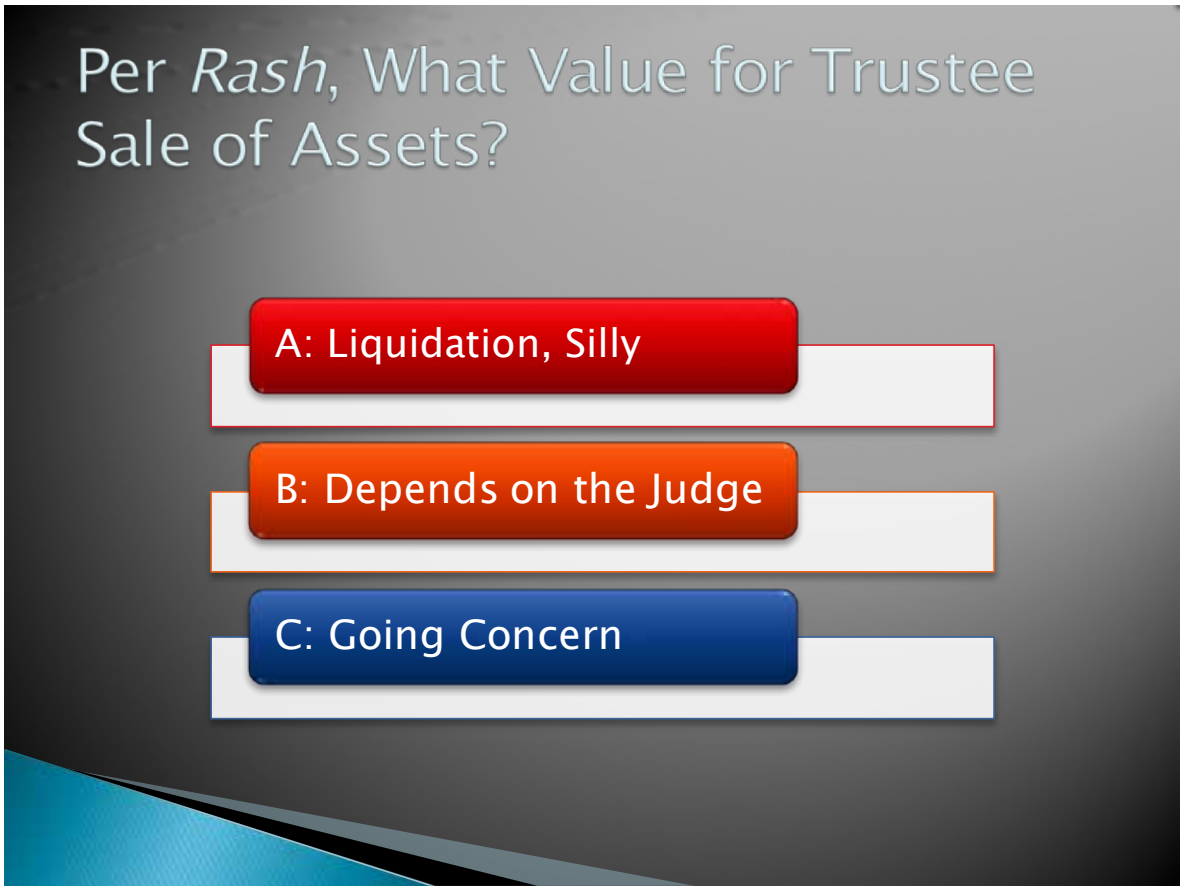

Per *Rash/506*, What Value To Cramdown a Family Car in Ch. 13?
A. NADA Retail
B. NADA minus 5%
C. Average of Retail/Trade In
D. NADA/KBB Starting Point

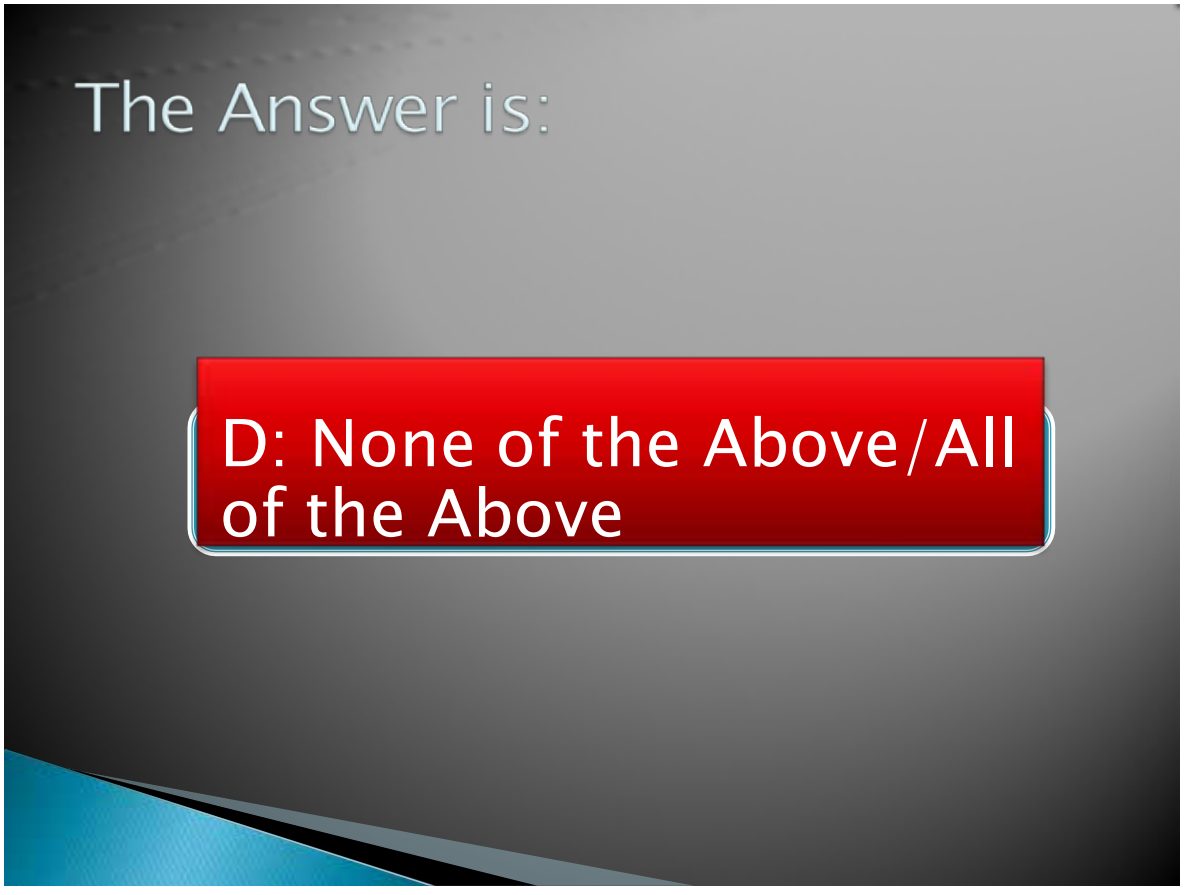
The Answer is: (Courts are Split)

E: Depends on the Court

Category II: Liquidation Sales




Per *Rash*, What Value for Trustee Sale of Assets?
A: Liquidation, Silly
B: Depends on the Judge
C: Going Concern


The Answer is:
D: None of the Above/All of the Above

Category III: Real Estate

Per *Rash/506*, What Value for Chapter 12 Farmland?

- A: Its Highest/Best Use as Development Property
- B: Not sure/depends
- C: Its Actual Use as Farmland

The Answer is:

C: Its actual use as farmland, where plan proposed Debtor would continue to farm

Per *Rash/506*, What Value for Single Family Homes Used as Residential Care Facilities?

The Answer is:

B: As Single Family Homes – judgment lien creditor had no interest in going concern value of the business

Category IV: Play if you dare…

Rules you need to know

- **FRE 104(a)** – Preliminary Questions
- **FRE 403** – Excluding Relevant Evidence
- **FRE 701** – Opinion Testimony by Lay Witness
- **FRE 702** – Expert Witness
- **FRE 703** – Bases of Expert's Opinion
- **FRE 803** – Hearsay
- **FRE 803(17)** – Market Compilations

Final Category (almost finished)

Practical/Strategic Considerations

- Motion v. Adversary?
- Burden of Proof?
- Standard of Review
- Finality for Appeal
- Local Rules/Continuances
- Weight Given to Experts
- Appraisals Binding on the Court?

Expert Considerations

Owner Testifying As To Value

Other Evidence of Value

- Corporate Rep
- Non-owner
- Zillow.com/internet evidence
- Tax Assessed values
- Scheduled values
- Auction
- Offers
- Budget