

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

CYNTHIA L. PILON

Debtor

CASE NO. 97-61760

Chapter 13

APPEARANCES:

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Hon. Stephen D. Gerling, Chief U.S. Bankruptcy Judge

MEMORANDUM-DECISION, FINDINGS OF FACT,
CONCLUSIONS OF LAW AND ORDER

This matter comes before the Court on the motion of Cynthia L. Pilon (“Debtor”), seeking confirmation of her modified plan (“Plan”), filed pursuant to Chapter 13 of the United States Bankruptcy Code, (11 U.S.C. §§101-1330)(“Code”) on June 2, 1997. Also before the Court is an objection to the Plan filed on June 4, 1997, by Green Tree Credit Corporation (“Green Tree”), the holder of a security interest in Debtor’s mobile home.

Green Tree initially objected to the confirmation of Debtor’s Plan on four separate

grounds, alleging that (1) Debtor had not yet made any payments to the Trustee; (2) that the Plan undervalued the amount of Green Tree's collateral, and thus did not comply with the cram-down provisions of Code § 1325(a)(5)(B); (3) that the Plan further failed to comply with Code §1325(a)(5)(B) by paying Green Tree an insufficient rate of interest for the use of its funds; and (4) that the treatment of Green Tree's rights amounted to an impermissible modification of a security interest in real property occupied as a principal residence under Code § 1322(b)(2).

The matter was then adjourned pending the final resolution of the Code § 1322(b)(2) issue in a similar case brought before this Court. On February 6, 1998, this Court's holding that the debtor's mobile home was not real property for purposes of Code §1322(b)(2) was affirmed by the Bankruptcy Appellate Panel of the Second Circuit. *Green Tree Credit Corp. v. Thompson (In re Thompson)*, 217 B.R. 375 (2nd Cir. B.A.P. 1998). A confirmation hearing in the present matter was then held on March 3, 1998, at which time the Court scheduled an evidentiary hearing on Green Tree's objections for June 24, 1998, later adjourned to August 12, 1998 (the "Hearing").

At the Hearing, Green Tree withdrew its first objection, as it appeared that Debtor had since become current on her payments to the Trustee, while the Code § 1322(b)(2) objection was also withdrawn in light of the Bankruptcy Appellate Panel's decision in *Thompson*. The question of the appropriate interest rate was settled by a stipulation on the record after the close of evidence, according to which the parties agreed that the applicable rate would be 9% rather than the 7% proposed by the Plan. As a result, the sole factual question remaining before the Court is the dispute over the value of Green Tree's collateral. Following the Hearing, the parties were given an opportunity to present memoranda of law on the proper valuation standard to be used,

and the matter was submitted for decision on September 11, 1998.

JURISDICTIONAL STATEMENT

The Court has core jurisdiction over the parties and subject matter of this contested matter pursuant to 28 U.S.C. §§ 1334(b), 157(a), b(1), b(2)(A), (L), and (O).

FACTS

The subject of this valuation dispute is a three-bedroom, two-bathroom 1989 Ashford mobile home (“Mobile Home”), which currently sits on a non-permanent foundation on a rented lot at Fawn Estates, Scriba, New York. The Mobile Home was purchased by Debtor in or about 1995 with financing by Green Tree, which obtained a security interest in the property. Green Tree has filed a proof of claim in Debtor’s bankruptcy for \$19,177.83, an amount that both parties agree exceeds the value of the collateral.

In her original Chapter 13 plan, filed on March 26, 1997, Debtor expressed the intention to abandon the Mobile Home, whose value she listed at \$13,000. However, in an amended plan filed on May 1, 1997, Debtor proposed to retain possession, and revised her schedules to reflect a value for the Mobile Home of \$7,500.00. At the Hearing, Debtor admitted that these first two valuations were each based on little more than guesswork. On June 2, 1997, Debtor amended her schedules yet again and reported the value of the Mobile Home as \$10,035.00, in accordance with a appraisal of the property conducted on or about May 1, 1997, by Homer F. Bowman (“Bowman

Appraisal”). Pursuant to the cram down provisions of Code § 1325(a)(5)(B), the Plan also proposed to repay Green Tree’s claim at an effective interest rate of 7%.

The substantive content of the Bowman Appraisal was not offered into evidence at the Hearing. Instead, each party relied on an appraisal made in more recent months. The first of these was performed by Joseph Muscalino (“Muscalino”), an employee of Green Tree, who appraised the Mobile Home at a value of \$15,449.00 in a report dated April 22, 1998 (“Muscalino Appraisal”). A considerably lower figure was obtained by Robert Dellecese (“Dellecese”), a real estate professional retained by Debtor, who inspected the Mobile Home in early July, 1998, and appraised its value at only \$5,000 (“Dellecese Appraisal”).

Dellecese reported extensive water damage to the Mobile Home, which has apparently been caused by the combination of a leaking roof and a faulty septic system. This has resulted in a mildewed carpet that will soon need to be replaced, a large stain on the bedroom wall, and a floor that has been extensively rotted in several places, leading to approximately seven distinct “spongy” patches and, according to Dellecese, a potential safety hazard. Dellecese also noted defects in the block piers supporting the Mobile Home as well as several more minor problems, including a few misaligned or damaged doors. Dellecese did not believe that these necessary repairs could be made at an economically feasible price, and suggested that the most efficient use of the property might be to convert it to a non-residential use, such as an on-site office for a building contractor.

Dellecese claimed that he was unable to find enough comparable sales to establish a market price for the Mobile Home, and professed a lack of confidence in the published guides to mobile home prices. As a result, it is not entirely clear what objective factors, if any, Dellecese

used in arriving at his figure of \$5,000.

On cross-examination, Dellecese was unable to state with certainty whether the defects he observed were necessarily in existence as of the petition date of March 26, 1997, but repeatedly insisted that such deterioration “doesn’t happen overnight.” The Debtor later testified that the water damage had existed at the time of the petition, and indeed was already noticeable when she purchased the mobile home, but conceded that things had gotten much worse in the seventeen months between the petition date and the Hearing. Debtor also admitted that she had done little to maintain the Mobile Home shortly before and during her bankruptcy, owing to uncertainty over whether she would be entitled to keep it.

The Muscalino Appraisal gave a much more positive description of the Mobile Home’s condition, which Muscalino described as above average in relation to other mobile home properties repossessed or inspected by Green Tree. Although Muscalino conceded that some repairs needed to be made, he asserted that the Mobile Home could be sold in its present condition to a retail dealer at a wholesale price of about \$9,500. If necessary repairs were made, Muscalino believed that the Mobile Home could be sold at the retail price of about \$15,000. Muscalino believed that the cost of the repairs to a wholesaler would be about \$2,500, estimated “off the cuff,” but that an individual consumer might pay more, possibly as much as \$5,000. Muscalino did not specify which potential repairs he considered when arriving at this figure, although it appears from his testimony that this would include, at a minimum, the cost of replacing the carpet and certain parts of the floor. Muscalino’s testimony does not include the potential costs of replacing the septic system, which is apparently a part of the underlying real property rather than the Mobile Home.

Muscalino disputed Dellecese's claim that no comparable sales were available, noting that Green Tree alone repossesses and disposes of about twenty to thirty mobile homes in New York state every month. However, Muscalino's written appraisal was not based on a comparable-sales analysis, but rather on the data contained within the National Automobile Dealers Association Manufactured Housing Appraisal Guide ("N.A.D.A. Guide"). Although the "book value" of the Mobile Home appears to have been only \$13,032, Muscalino adjusted the figure upward to \$15,449 based on a number of factors contained on a National Appraisal System worksheet ("N.A.S. Form") including condition (listed as "good," resulting in a multiplier of 105%), location (104% multiplier), size (flat addition of \$895 to the appraisal value) and accessories (added value of \$323). Because the value of mobile homes tends to decrease with age, Muscalino estimated that the valuation for March 1997 would have been \$15,900. Muscalino did not, however, deduct the cost of needed repairs from this total.

In her memorandum of law, submitted after the Hearing, Debtor concedes the weakness of her own expert's testimony and ironically urges the Court to fix the value of the Mobile Home based on the testimony of Muscalino. The appropriate figure, argues Debtor, is \$9,500, representing the Mobile Home's value on the wholesale market.¹

DISCUSSION

As a preliminary matter, the Court must determine whether Debtor, having set a value of

¹ Apart from a brief argument about the relevant time of valuation, Green Tree's memorandum of law does not address the issue of valuation standards, and does not identify which of Muscalino's many figures it regards as the proper value of the Mobile Home.

\$10,035.00 for the Mobile Home on her schedules, is thereby precluded from asserting a lower figure in light of the testimony presented at the Hearing.² As a general rule, bankruptcy courts are reluctant to make determinations of value based on procedural traps such as waiver or res judicata. *See Midlantic National Bank v. Kouterick (in re Kouterick)*, 161 B.R. 755, 760 (Bankr. D.N.J. 1993). This policy consideration is bolstered by the particular circumstances of a Chapter 13 case, where early valuations must often be based on little more than guesswork, and a hard-and-fast rule of waiver may well force debtors to submit needlessly conservative estimations of asset value in their schedules. The Court therefore concludes that it may properly consider valuations for the Mobile Home less than \$10,035.

It is well-established that Chapter 13 places the burden on the debtor to prove that the confirmation standards of Code § 1325 have been met. *See National School Bus, Inc. v. Carignan*, 190 B.R. 739, 741 (N.D.N.Y. 1996). Moreover, for purposes of valuing a secured creditor's collateral under Code § 1325(a)(5)(B), the Court looks to facts as they existed on the date of the petition. *See In re Cerminaro*, 220 B.R. 518 (Bankr. N.D.N.Y. 1998). Although the earliest appraisal entered into evidence was made over a year after the March 1997 petition date, Debtor's testimony suggested that apart from some gradual deterioration, there were no significant changes in the Mobile Home's condition during that period. As a result, the Court finds that Muscalino's extrapolation of the home's March 1997 value based on his April 1998 inspection is persuasive.

In determining the value of collateral retained by the debtor in a Chapter 13 bankruptcy,

² Although Green Tree offered to stipulate to a value of \$10,035 at the start of the Hearing, this proposal was rejected by counsel for Debtor.

a court must look to the asset's "replacement value"-- what the debtor would pay to obtain an identical asset on the open market-- rather than the "foreclosure value," or the amount that the creditor would actually realize in a liquidation sale. *See Associates Commercial Corp. v. Rash*, ___ U.S. ___, 117 S.Ct. 1879, 1885 (1997). Applied to the present case, *Rash* requires that the Court value the Mobile Home not with reference to \$9,500 that Green Tree could recover by selling the property in the wholesale market, but rather by the price in cash that Debtor would have to pay to in order to obtain a Mobile Home of identical age and condition on the open market.

The inquiry into the Mobile Home's price is complicated by the fact that it is currently in need of significant repair. Although Muscalino reported that there is a small consumer market for damaged homes, it appears that it is far more typical that such homes would be repaired and sold by a dealer, who can make the repairs at a far lower cost than a consumer. In such instances, courts applying *Rash* have nevertheless estimated hypothetical replacement values for damaged property by subtracting the cost of repair from the anticipated retail value of the property after repairs. *See In the Matter of McCutchen*, 224 B.R. 373, 375 (Bankr. E.D. Mich. 1998).

Although the Court is persuaded that the retail value of the Mobile Home after repairs would be \$15,900, a further complication is that the evidence established two substantially different costs of repair-- the \$2,500 that a retailer would pay, and the \$5,000 that a consumer would pay. Although the Court has been unable to find any case directly on point, the Court believes that a faithful application of *Rash* requires use of the lesser figure. By adopting replacement cost rather than foreclosure price as the proper standard, *Rash* in effect held that the valuation of a creditor's collateral would include the added value that a good receives when it moves from the wholesale to the retail markets. While most of the added value is in the form of

the retailer's superior ability to reach a greater number of consumers, the Court sees no reason why it should not also include the retailer's ability to make repairs at a greater volume and lower individual cost. Additionally, the Court notes that a consumer-cost-of-repair standard would unfairly punish many secured creditors, who often have little or no control over the events that necessitated the repairs. As a result, the Court finds that the valuation of the damaged Mobile Home is properly measured by subtracting the cost of repair to a retail dealer (\$2,500) from the anticipated retail value after repairs are made (\$15,900), giving an adjusted valuation of \$13,400.

Where a Chapter 13 plan proposes to block a secured creditor's right to foreclosure, Code § 1325(a)(5)(B) requires that the secured creditor be compensated with a stream of payments whose present value is at least equal to that of the secured portion of the claim. *See Valenti v. General Motors Acceptance Corporation (In re Valenti)*, 105 F.3d 55, 63 (2nd Cir. 1997). In the present case, it appears that Debtor's Plan undervalues the secured portion of Green Tree's collateral by \$3,365. In addition, the parties have agreed by stipulation that the proper interest rate on Green Tree's claim is 9%, rather than the 7% in the Plan. Based on these two figures, the Court concludes that the present value of the stream of payments to Green Tree under the Plan is less than the value of Green Tree's secured claim, and thus fails to satisfy the confirmation requirements of Code § 1325.

Based on the foregoing, it is hereby

ORDERED that the confirmation of Debtor's Plan is denied, and it is further

ORDERED that Debtor may, on or before December 14, 1998, file an amended plan in compliance with the Decision herein along with notice of the confirmation hearing on the amended plan. Failure to file such an amended plan and notice it for a confirmation hearing shall

result in the entry of an Order dismissing the within Chapter 13 case for cause pursuant to Code § 1307(c)(1), without further notice or hearing.

Dated at Utica, New York

this 13th day of November

STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge