

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

JAMES L. BALENTON

Debtor

CASE NO. 03-64400

Chapter 13

JAMES L. BALENTON

Plaintiff

vs.

ADV. PRO. NO. 03-80501

FAIRBANKS CAPITAL CORP.

Defendant

APPEARANCES:

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Of Counsel

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

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

Under consideration by the Court is a complaint filed on December 18, 2003, by James L. Balenton (“Debtor”) seeking a determination of the extent of a mortgage lien held by Fairbanks Capital Corporation (“Fairbanks”) on the Debtor’s residence (the “Premises”). It is the Debtor’s

position that the value of the Premises is less than the claim of Household Finance Realty Corporation of New York (“Household”), which holds a first mortgage on the Premises in the amount of \$36,609.45, and, accordingly, Fairbanks’ claim is entirely unsecured.

A trial was conducted on May 6, 2004, in Utica, New York. The Court heard testimony from the Debtor, as well as from Robert Gerbin (“Gerbin”) and Frank Bertonica (“Bertonica”). The latter two testified as experts concerning appraisals they had performed on the Premises.¹

Following the testimony of Gerbin, who was hired by the Debtor to perform an appraisal of the Premises, the Court reserved on a motion made on behalf of Fairbanks, seeking dismissal of the complaint. The complaint was taken under submission by the Court after testimony by the Debtor and Bertonica, the appraiser hired by Fairbanks, as well as rebuttal testimony from Gerbin. In lieu of closing arguments, the Court provided both parties with an opportunity to submit memoranda of law on or before June 4, 2004.

JURISDICTIONAL STATEMENT

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

¹ The Debtor’s counsel moved to have Gerbin qualified as an expert in rehabilitation/construction in order to present testimony concerning the cost of certain repairs to the Premises. In response to an objection by Fairbanks’ counsel, the Court denied the motion on the basis that there had been no evidence to support Gerbin’s expertise in this area.

FACTS

The Debtor filed a voluntary petition pursuant to chapter 13 of the U.S. Bankruptcy Code, 11 U.S.C. §§ 101-1330 (“Code”) on June 25, 2003. According to Schedule A of the Debtor’s petition, the Premises had a market value of \$38,680 as of the petition date.² The Debtor listed Fairbanks as holding a first mortgage on the Premises in the amount of \$40,000 and Household as holding a second mortgage on the Premises in the amount of \$35,000. *See* Schedule D, attached to the Debtor’s petition. On July 11, 2003, Fairbanks filed a proof of claim in the amount of \$41,740.97. Household filed a proof of claim on August 5, 2003, asserting a claim of \$36,609.45.

On October 6, 2003, Household filed a motion seeking relief from the automatic stay in order to foreclose on the Premises. In its motion, Household provided proof that its mortgage was recorded in the Onondaga County Clerk’s Office on July 15, 1996. On November 3, 2003, Fairbanks filed a motion seeking relief from the automatic stay in connection with the same Premises. In its motion, Fairbanks asserted that it held the first mortgage on the Premises but provided no proof of its recorded mortgage; nor did it include a copy of its mortgage with its proof of claim. In the Debtor’s response to Fairbanks’ motion, the Debtor indicated that he was mistaken in his belief that Fairbanks held the first mortgage on the Premises. Accordingly, the Debtor amended his chapter 13 plan to provide for payment of Household’s first mortgage outside of the plan. The Debtor indicated his intent to void the second mortgage lien held by Fairbanks and, accordingly, commenced the

² The Debtor testified that the value had been estimated based on the amount thought to be owed on the first mortgage, rather than based on any appraisal.

adversary proceeding against Fairbanks on December 17, 2003.³ The Debtor's plan was confirmed by Order, dated January 7, 2004.

The Premises consist of a two story Cape Cod style home built in 1952. The house contains gross living space of 1,291 square feet⁴ and includes four bedrooms⁵ and one bathroom, as well as a detached style single car garage and a rear yard enclosed with a chain link fence. The lot size measures 53 feet by 120 feet or approximately 6400 square feet.

Attached to the Debtor's complaint is an appraisal performed by Eskew Young III ("Young"), dated August 28, 2003, indicating a value of \$35,000 for the Premises based on comparable properties sold between September and December 2002. At the trial, the Debtor's counsel represented to the Court that Young was no longer in the area and, therefore unavailable to testify. Therefore, the Debtor had employed the services of Gerbin, who performed an appraisal ("Gerbin Appraisal") of the Premises on or about May 3, 2004. Gerbin concluded that the property had a market value "as is" of \$35,000 as of May 3, 2004. *See* Debtor's Exhibit A. At the trial he testified that as of the petition date of June 25, 2003, he estimated the value to be \$34,000.

³ The parties do not dispute that Household has a first mortgage on the Premises and is owed \$36,609.45.

⁴ This square footage of living space is supported by a floor plan contained in Bertonica's appraisal. Gerbin's appraisal indicates 1,141 square feet in living space; however, he has provided no floor plan to support the square footage.

⁵ According to Gerbin, the Premises had two bedrooms on the second floor and one bedroom on the first floor. He also identified a dining room on the first floor. However, according to Bertonica, as well as Young, the Premises had two bedrooms upstairs and two bedrooms downstairs. Neither Bertonica, nor Young, identified a dining room on the first floor. In the addendum to Bertonica's appraisal, he indicates that "[u]se of living area for bedrooms or other rooms is considered a reflection of individual taste" and, therefore, he made no adjustment for the difference in the number of bedrooms when making his comparisons. *See* Fairbanks' Exhibit 1 at Addendum.

Gerbin used the sales comparison approach in estimating the value of the Premises. Gerbin testified that he believed the Premises to be in “fair” condition largely due to the fact that the entire front wall of the basement was wet and leaking. According to Gerbin, when he inspected the Premises three days prior to the trial, there was approximately one-quarter inch of water covering 25% of the floor in the basement. He also testified that the mortar was flaking on the front wall, as well as an adjacent wall in the basement.

The Debtor testified that he purchased the Premises from his parents in 1993. According to the Debtor, there had always been a water problem in the basement. It was his testimony that in the spring of 2003 the front wall had begun to leak. He further explained that he had stopped work on remodeling the bathroom in order to work on the foundation because of the water problem.

Gerbin chose three comparable sales that had occurred between May 2003 and September 2003. The first comparable (“G-1”) was located 3/8 of a mile from the Premises and had been sold for \$45,000 in June 2003. Because he considered the Premises to be in fair-average condition, he had made a downward adjustment of \$4,000 to G-1, which he felt was in average condition. He also made a downward adjustment of \$1,000 due to the fact that G-1 had an enclosed porch, which the Premises did not. With gross adjustments of 11.1% and net adjustments of -11.1%, he estimated the adjusted sale price of G-1 to be \$40,000.⁶

Gerbin’s second comparable (“G-2”) was located one block from the Premises and had been sold for \$28,000 in May 2003. Gerbin made upward adjustments of \$1,000 because the lot size of

⁶ The Court has recalculated the gross and net adjustments set forth in Debtor’s Exhibit A for all of Gerbin’s comparables to reflect their values as of June 25, 2003, rather than as of May 3, 2004. Because his comparables were sold between May and September 2003, the original adjustments for the actual dates of sale were unnecessary.

G-2 was somewhat less than that of the Premises; \$4,000 as he considered G-2 to be in fair condition; \$500 to adjust for the fact that although both properties had unfinished basements, G-2 was not a “walk-out” basement; and \$500 due to the fact that G-2 did not have a fenced yard as did the Premises. With gross adjustments of 21.4% and net adjustments of 21.4%, he estimated the adjusted sale price of G-2 to be \$34,000.

Bertonica testified that in his view G-2 was not a good comparable given that it was a “corporate” seller and the original list price had been \$48,000. He acknowledged on cross-examination that the original listing price simply could have been too high, however.

Gerbin’s third comparable (“G-3”) was also located one block from the Premises and had sold for \$37,234 in September 2003. Gerbin had made several downward adjustments to the sale price, including \$4,700 due to the fact that G-3 had approximately 590 square feet more living space than the Premises; \$1,000 for the fact that G-3 allegedly had four bedrooms; \$1,000 for the fact that G-3 had a two car garage; and \$1,000 due to the fact that G-3 had a fireplace, which the Premises did not. With gross adjustments of 23.4% and net adjustments of -18%, he estimated the adjusted sale price of G-3 to be \$30,234.

Bertonica testified that he had not considered G-3 as a comparable given the fact that it was a “HUD sale” following an FHA foreclosure.⁷ He testified, based on his experience with “HUD sales,” that the list price was generally set below the competitive list price in order to sell the property quickly.

All of Bertonica’s comparables, as well as the Premises, were rated by him as in average

⁷ It is the Court’s understanding that FHA, the Federal Housing Administration, is a division within HUD, the U.S. Department of Housing and Urban Development, and is involved with guaranteeing home mortgage loans.

condition.⁸ *See* Fairbanks' Exhibit 1. His first comparable ("B-1") is located on the same street as the Premises and sold for \$61,400 on October 23, 2003.⁹ Bertonica made one upward adjustment of \$500 due to the fact that B-1 did not have a fenced yard. His other adjustments were downward and included \$6,000 for what he termed "seller's concessions;" \$1,000 for the fact that B-1 had two full baths, whereas the Premises has only one; \$2,800 for approximately 400 square feet in additional living space found in B-1; \$1,000 for B-1's two car garage; and \$1,000 due to the fact that B-1 had a fireplace, which the Premises do not. With gross adjustments of 20% and net adjustments of -18.4%, he estimated the adjusted sale price of B-1 to be \$50,100.

Bertonica's second comparable ("B-2") was located within a block of the Premises and sold for \$52,000 in October 2003. The upward adjustments of \$500 for B-2's lack of a fenced yard and the downward adjustment of \$500 because B-2 had a partly finished basement netted themselves out. The only other adjustment was an upward one of \$2,600 due to the fact that B-2's living area was approximately 393 square feet less than that of the Premises. He made no separate adjustment for the fact that B-2 had only three bedrooms. In his appraisal he explains that "any difference in value has been accounted for in the square footage adjustment." Fairbanks' Exhibit 1 at Addendum. With gross adjustments of 6.9% and net adjustments of 5.0%, he estimated the adjusted sale price of B-2 to be \$54,600.

⁸ On rebuttal, Gerbin acknowledged that the leaking in all likelihood would not have been noticeable in January 2004 when Bertonica inspected the Premises because of the freezing temperatures at that time of year.

⁹ B-1 had been purchased in December 2002 for \$25,000. Bertonica indicated that he had not given the prior sale any weight because the owner at the time of the sale had been identified as "Trustee," which according to Bertonica indicated some type of distressed sale. *See* Fairbanks' Exhibit 1 at Addendum.

Bertonica's final comparable ("B-3"), which sold for \$53,900 in June 2003, was located within two blocks of the Premises. As with B-2, Bertonica made offsetting adjustments of \$500 each with respect to the lack of a fenced yard at B-2 and there being an extra half-bath at B-2. His only other adjustment was upward in the amount of \$1,000 to account for approximately 139 square feet of additional living space of the Premises. He made no adjustment for the fact that the lot size of the Premises was approximately 1,230 square feet more than B-3. With gross adjustments of 3.7% and net adjustments of 1.9%, he estimated the adjusted sale price of B-3 to be \$54,900.

Bertonica concluded that the estimated market value of the property as of January 22, 2004, was \$52,000. At the trial, he testified that the same value would have applied to the Premises as of June 25, 2003. This was supported by the fact that the comparables he used in his analysis represented sales of properties that occurred in June and October 2003.

DISCUSSION

It has long been recognized that valuation of assets is 'not an exact science' and the courts have wide latitude in determining value. A court is not bound by values determined by appraisals but rather may form its own opinion as to the value of the subject property after consideration of the appraisers' testimony and their appraisals.

In re Richards, Case No. 97-14798, 1999 WL 14680 at *7 (Bankr. E.D.Pa. Jan. 12, 1999).

Each party has presented testimony by a residential appraiser concerning the value of the Premises. Both experts used the sales comparison method in arriving at their estimated value of the Premises. As noted above, Gerbin estimated the value of the Premises as of June 25, 2003, to be \$34,000. On the other hand, Bertonica estimated the value of the Premises as of the petition date

to be \$52,000. The parties have stipulated that Household, which holds the first mortgage on the Premises, is owed \$36,609.45. If Fairbanks is secured by any equity at all in the Premises, pursuant to Code § 1322(b)(2) its mortgage may not be modified and its lien avoided. *See Pond v. Farm Specialist Realty (In re Pond)*, 252 F.3d 122, 126 (2d Cir. 2001); *In re Jones*, Case No. 03-84129, 2004 WL 298612 at *1 (Bankr. C.D. Ill. Feb. 5, 2004); *In re Scheuer*, 213 B.R. 415, 417-18 (Bankr. N.D.N.Y. 1997).

As noted by the court in *Jones*, the sales comparison method is generally the most reliable method for appraising the value of residential property. *See Jones*, 2004 WL 298612 at *2, citing Miller and Gallagher, *Residential Real Estate Appraisal* 232 (3d ed. 1998). The most important factors to be considered in determining the validity of the data presented by the appraisers are that

- (1) the characteristics of the comparable property are similar to the subject property,
 - (2) the location of the comparable property is relatively close to the subject property,
 - and (3) the date of sale of the comparable property is close to the valuation date. . . .
- . Comparable sales within six months of the valuation date for the subject property are preferred, although in a stable market or where sales activity is low, a period of one to two years is acceptable.”

Jones, 2004 WL 298612 at *2. It is also expected that it will be necessary for an appraiser to make adjustments for differences between the comparable properties and the subject property as no two properties are ever identical. *Id.* at *3. In this regard, greater reliance is to be placed on residential comparables with total adjustments of no more than 25% of the gross selling price or 15% of the adjusted sale price. *See In re Ferman*, Case No. 00-12681, 2001 WL 1755707 at *2 (Bankr. D.N.H. June 4, 2001).

All of the comparables used by both experts were built in the Cape Cod style within fourteen years of the construction of the Premises. They were located in close proximity to the Premises and

all of the sales occurred within six months of the petition date. The adjustments made by the two experts can be summarized as follows:

	<u>Net</u>	<u>Gross</u>		<u>Net</u>	<u>Gross</u>
G-1	-11.1%	11.1%	B-1	-18.4%	20.0%
G-2	21.4%	21.4%	B-2	5.0%	6.9%
G-3	-18.0%	23.4%	B-3	1.9%	3.7%

All of the gross adjustments made by the two experts were for less than 25% of the gross selling price. However, the net adjustments for G-2, G-3 and B-1 are more than 15% of the gross selling price and, therefore, entitled to less weight for purposes of the Court's analysis. There is also the concern raised by Bertonica with respect to G-3, which was the sale conducted by HUD. Bertonica testified that usually prices on houses sold by HUD following foreclosure were more likely to be lower in an effort to get them sold quickly. This was not rebutted by Gerbin. Bertonica's concerns are reinforced by the fact that it was necessary for Gerbin to make a gross adjustment of 23.4% to the sale price of G-3, a figure approaching the 25% guideline for concerns as to reliability.

As noted above, Bertonica made no adjustments for the water problem in the basement. Understandably, due to the cold temperatures, the problem apparently did not manifest itself in January 2004 when he inspected the Premises. However, both the Debtor and Gerbin acknowledged the problem. Gerbin did make adjustments of \$4,000 to G-1 and G-2 to account for the fair-average condition of the Premises, which Bertonica had rated as "average." Unfortunately, there was no admissible evidence available to the Court of the cost of repairs to the foundation.¹⁰ *See In re Manakos*, Case No. 00-10641, Adv. Pro. 00-1067, 2000 WL 33679424 (Bankr. D.N.H. Sept. 8,

¹⁰ Debtor's counsel moved to have Gerbin qualified as an expert in rehabilitation/construction, which the Court denied.

2000).

In *Manakos* the debtors' appraiser had presented estimates to replace the roof, to replace and repair the soffit and fascia boards, and to eliminate termites and made a downward functional utility adjustment of \$10,500. *Id.* at *4. The court actually then reduced the adjustment to \$7,000 in its recalculation of the fair value of the property, ultimately giving equal weight to the adjusted fair values of both appraisals in resolving the differences between the two. *Id.* at *5-6.

Based on the above, the Court will accept as comparables G-1, B-2 and B-3. Even making an adjustment of -\$4,000 to both B-2 and B-3 to account for the water problem, the value of the Premises is estimated by the Court to be between \$40,000 and \$50,900. The Court need not make a specific finding of value because even if the fair value of the Premises is only \$40,000, there is still equity to which Fairbanks' lien attaches based on Household's claim of \$36,609.45. Accordingly, Fairbanks mortgage may not be modified pursuant to Code § 1322(b)(2).

Based on the foregoing, it is hereby

ORDERED that Fairbanks motion seeking dismissal of the Debtor's complaint is granted.

Dated at Utica, New York

this 26th day of July 2004

STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge