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WRITTEN DECISION - NOT FOR PUBLICATION

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CLERK, U.S. BANKRUPTCY COURT SOUTHERN DISTRICT OF CALIFORNIA	
BY	gdo DEPUTY

UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF CALIFORNIA

In re: } BK. No. 08-05229-JM13  
Matthew W. Berger and April R. Berger }  
Debtors. } MEMORANDUM DECISION

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Debtors Matthew W. Berger and April R. Berger (collectively, "Debtors") filed a Motion for Valuation of Debtors' Residence and Avoidance of Second Trust Deed Thereon in Connection With Confirmation of Chapter 13 Plan (the "Lien Strip Motion"). Debtors allege in the Lien Strip Motion that the value of their residence is less than the amount owed to the first trust deed holder and request that this Court confirm this valuation pursuant to Fed. R. Bankr. P. 3012. As a result, they also seek to strip the second trust deed held by JP Morgan Chase ("Lender") under 11 U.S.C. § 1322(b)(2).<sup>1</sup> Lender disputes Debtors'

<sup>1</sup> Hereinafter references to code sections refer to Title 11 of the United States Code, also referred to as the "Bankruptcy Code" unless otherwise specified. References to Rule refer to the Federal Rules of Bankruptcy Procedure, unless otherwise indicated.

1 valuation, alleges that it holds an undersecured rather than unsecured claim, and argues that,  
2 as a result, Debtors cannot strip or otherwise modify its trust deed.

3 The Court held a valuation hearing on February 27, 2009. At that time, the Court  
4 heard testimony from experts for Debtors and for Lender. The Court has carefully reviewed  
5 the evidence contained in the written appraisal reports and the testimony of the appraisers at  
6 the valuation hearing. The Court now renders its decision.

7  
8 **Facts**

9 1. Debtors filed a Voluntary Chapter 7 Petition on June 12, 2008.

10 2. Their concurrently filed Schedule A values their single family home located at  
11 6770 Obsidian Place, Carlsbad, California (the "Residence") at \$972,783.00. There is no  
12 dispute that the Residence is Debtors' principal residence within the meaning of  
13 section 1322(b)(2). Debtors' schedules also list a claim secured by a first trust deed against  
14 the Residence in the amount of \$869,422.00 and Lender's claim secured by a second trust  
15 deed against the Residence in the amount of \$163,342.00.

16 3. On October 20, 2008, Debtors filed an *ex parte* motion requesting conversion  
17 of their chapter 7 bankruptcy to a proceeding under chapter 13 (the "Conversion Motion").  
18 The Court granted the Conversion Motion by its order dated October 21, 2008.

19 4. On November 5, 2008, the Debtors filed additional and revised schedules in  
20 their chapter 13 case. The revised Schedule A valued the Residence at \$850,000.00 and  
21 revised Schedule D included a \$21,430.00 claim of the San Diego County Tax Collector  
22 secured by a lien on the Residence.

23 5. Debtors also filed a chapter 13 Plan (the "Plan") on November 5, 2008. The  
24 Plan provided for monthly payments of \$1,920.00 and payment of 22% to unsecured  
25 creditors. In addition, at paragraph 19, the Plan provided that: "Debtors will be filing a  
26 Motion for Valuation of Debtors' Residence and Avoidance of Junior Trust Deed Thereon  
27 (lien stripping action) against [Lender], creditor holding the second deed of trust on the  
28

1 subject property, pursuant to 11 U.S.C. 1322(b)(2) as the lien is completely under-secured in  
2 that the balance owed under the first deed of trust exceeds the fair market value of the  
3 subject property. Upon confirmation, said creditor will be deemed to have accepted the  
4 allowed secured value and the fair market value of its security interest set forth below and,  
5 pursuant to this provision, will be binding unless said creditor timely objects to the Plan  
6 and/or the Court orders otherwise. This provision is in no way meant to contest the validity,  
7 extent, or priority of the creditor's lien but, rather, solely in furtherance of an action to be  
8 filed to strip off a creditor's wholly unsecured lien through a valuation process under  
9 11 U.S.C. [§§] 506(a), 1322(b)(2) and Rules 3012 and 9014. *See, In re Pereira,*  
10 394 B.R. 501, (*sic*) (Bankr. S.D. Cal. 2008); *In re Millsbaugh,* 302 B.R. 90, (*sic*) (Bankr. D.  
11 Idaho 2003)."

12 6. Consistent with the Plan, on November 20, 2008, the Debtors filed the Lien  
13 Strip Motion and set this matter for hearing on January 27, 2009. A review of the proof of  
14 service of the Lien Strip Motion indicates that in serving the motion Debtors did not comply  
15 with Rule 7004.<sup>2</sup>

16 7. Debtors supported the Lien Strip Motion with the Declaration of Brad S.  
17 Webber ("Webber Declaration"). Mr. Webber is a licensed real estate appraiser and has  
18 been a California residential real estate appraiser since 2002. The Webber Declaration  
19 evidences that Mr. Webber performed his appraisal on October 3, 2008 and that he valued  
20 the Residence at \$850,000.00 as of that date. The Webber Declaration attached a written  
21 Appraisal of Real Property (the "Webber Appraisal") as Exhibit "A."

22 8. Lender filed its Stipulation on Debtors' Motion to Value Collateral on  
23 December 8, 2008 (the "Opposition"). The Court is unclear as to why the document was  
24 entitled a "stipulation" as it finds no evidence that the Debtors agreed to the content of this  
25 document or to its filing. This short document, in the main, argues that Debtors have failed

26 \_\_\_\_\_  
27 <sup>2</sup> This Court allows debtors to obtain a valuation determination under section 506(a) in aid of  
28 a section 1322(b)(2) lien strip by motion, but requires that debtors serve such motion as required by  
Rule 7004. *See, In re Pereira,* 394 B.R. 501, 506-507 (Bankr. S.D. Cal. 2008).

1 to carry their burden of proof due to the conflict between the scheduled value and  
2 Mr. Webber's later valuation and that, as a result, the Lien Strip Motion must be denied.  
3 This document did not attach any appraisal evidence.

4 9. The Debtors responded to the Opposition with a Supplemental Declaration of  
5 Brad S. Webber that valued the Residence as of the Debtors' petition date (the "Petition  
6 Date"). Mr. Webber's valuation remained consistent at \$850,000.00. The Debtors also  
7 filed a supplemental declaration advising of their decision to request a Petition Date  
8 appraisal and stating that the originally scheduled value for the Residence was an "estimate"  
9 reached without utilization of comparable sales data or other data ("Debtors' Suppl. Decl.")).  
10 The Debtors concluded that: "We were obviously wrong in light of evidence of comparable  
11 sale prices which we reviewed as reflected on the appraisal and supplemental appraisal  
12 performed by Brad Webber." Debtors' Suppl. Decl. 2:7-9.

13 10. At the January 27, 2009 hearing on the Lien Strip Motion, Lender advised that  
14 it had only recently obtained a full appraisal for the Residence. The Debtors objected to  
15 introduction of this appraisal evidence, but the Court exercised its discretion to overrule the  
16 objection in order to allow this matter to proceed to an evidentiary hearing on the merits.  
17 The Court noted, in particular, that Lender had not been served until November 20<sup>th</sup> and  
18 that it was not unreasonable to allow a creditor time to obtain an appraisal.<sup>3</sup> The Court also  
19 found no prejudice to the Debtors since an evidentiary hearing could be held promptly. As a  
20 result, the Court scheduled an evidentiary hearing for February 27, 2009. The Court  
21 directed Lender to file a declaration of its appraiser in lieu of direct testimony on or before  
22 February 3, 2009, and allowed for additional briefing and other matters by order entered on  
23 February 9, 2009.

24 11. Lender timely filed the Declaration of Leland Hill on February 2, 2009.  
25 Mr. Hill is a Certified General Real Estate Appraiser in the State of California and has over  
26 30 years of appraisal experience. Mr. Hill valued the Residence as of the Petition Date at

27 \_\_\_\_\_  
28 <sup>3</sup> The fact that the notice given did not comply with Rule 7004 underscores the  
appropriateness of allowing Lender this time.

1 \$990,000.00. A copy of his Residential Appraisal Summary report is attached to his  
2 declaration as Exhibit "B." Thus, under Mr. Hill's appraisal, Lender was an under-secured  
3 not an unsecured creditor.

4 **Legal Background.**

5 The Bankruptcy Code expressly provides that a chapter 13 plan may "modify the  
6 rights of holders of secured claims, other than a claim secured only by a security interest in  
7 real property that is the debtor's principal residence, . . ." 11 U.S.C. § 1322(b)(2). In  
8 *Nobelman v. American Savings Bank et al*, 508 U.S. 324 (1993), the Supreme Court  
9 confirmed that section 1322(b)(2) modification is not available when a section 506(a)  
10 valuation establishes that a lender's claim is partially secured. After *Nobelman*, however,  
11 the Ninth Circuit Court of Appeals, along with the majority of other circuit courts, held that  
12 the anti-modification protection of section 1322(b)(2) does not prohibit modification of the  
13 rights of a junior creditor holding a lien on a debtor's primary residence where senior liens  
14 exceed the value of the residence such that the junior creditor is wholly unsecured<sup>4</sup>.  
15 *Zimmer v. PSB Lending Corp. (In re Zimmer)*, 313 F.3d 1220 (9<sup>th</sup> Cir. 2002).

16 In this case, Debtors seek to modify the rights held by Lender pursuant to  
17 section 1322(b) and request that the Court determine the secured status of Lender's claim  
18 pursuant to section 506(a).<sup>5</sup> Section 506(a) provides that such "value shall be determined in  
19 light of the purpose of the valuation and of the proposed disposition or use of such property,  
20 and in conjunction with any hearing on such disposition or use or on a plan affecting such  
21 creditor's interest." In this case, Debtors intend to retain the Residence, to avoid Lender's  
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24 <sup>4</sup> Such modification is commonly referred to as "lien stripping."

25 <sup>5</sup> Debtors' legal argument includes references to section 506(d). As clearly settled by the  
26 Supreme Court in *Dewsnup v. Timm (In re Dewsnup)*, 502 U.S. 410, 415-16 (1992), the function of  
27 section 506(d) is to void "a lien whenever a claim secured by the lien itself has not been allowed."  
28 Thus, the Supreme Court held that: section 506(d) does not allow a debtor to 'strip down' a  
creditor's lien, where the creditor's claim is secured by a lien and has been fully allowed pursuant to  
section 502. *Dewsnup v. Timm*, 502 U.S. at 417. The Court reads *Dewsnup* as precluding a lien  
strip (*i.e.* an order allowing a debtor to require reconveyance) based solely on a section 506(a)  
determination of collateral value.

1 lien entirely, and to pay Lender's claim under their chapter 13 plan as a wholly unsecured  
2 claim (*i.e.* Lender to receive a pro rata share of \$60,630.88). To accomplish this goal, the  
3 value of the Residence cannot exceed the amount owed to the holders of liens against the  
4 Residence that are senior to Lender's lien.  
5

6 In this case, the parties initially disagreed as to the correct day for a section 506(a)  
7 valuation in aid of a section 1322(b)(2) lien strip. Ultimately, however, they agreed that the  
8 appropriate date for valuation would be the Petition Date. The Court notes that the case law  
9 on this topic is divided with some courts utilizing the petition date while others have chosen  
10 other dates such as the confirmation date. Given the agreement of the parties, however, and  
11 given that the Petition Date is an appropriate and logical date for the valuation, the Court  
12 utilizes the Petition Date as the appropriate date for valuation for purposes of this decision.<sup>6</sup>  
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#### 15 **Analysis Of Valuation Evidence.**

16 At the evidentiary hearing, this Court heard testimony from appraisers for the  
17 Debtors and the Lender. Their appraisals reflect a \$140,000.00 difference in value. Despite  
18 this wide difference in value, both appraisers utilized a comparable sales approach to  
19 valuation.<sup>7</sup> Only one comparable, however, was common to both appraisals.  
20

21 As the Lender correctly noted in closing argument, with such a substantial difference  
22 in a residential real property appraisals, the Court's analysis must focus on which appraisal  
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25 <sup>6</sup> The petition date is the "watershed date of a bankruptcy proceeding." *Johnson v. GMAC (In*  
26 *re Johnson)*, 165 B.R. 524,528 (S.D. Ga. 1994.) And, "...creditors' rights are fixed (as much as  
27 possible)" as of this date. *Id.* This approach is: "clearly supported by 11 U.S.C. § 502 (b) which  
28 states the general rule that, when an objection to a claim is raised,...'the court, after notice and a  
hearing, shall determine the amount of such claim as of the date of the filing of the petition..."  
*Brager v. Blum (In re Brager)*, 39 B.R. 441, 443 (Bankr. E.D. Pa. 1984).

<sup>7</sup> Mr. Webber also gave the cost approach supportive consideration.

1 is more credible. To aid in this endeavor, the Court focused on those factors typically  
2 utilized by other courts such as the appraisers' methodologies, the quality of the appraisal  
3 report, their testimony on direct and cross examination, and the appraisers' respective ability  
4 to substantiate the basis for the valuation. The appraisers' use of valuation methods  
5 common in the industry was relevant, as was the relative experience of the appraisers. After  
6 consideration of these factors, the Court concludes that the Lender's appraisal is  
7 significantly more credible. As a result, the Court finds that the Lender is an undersecured  
8 rather than unsecured creditor and that the Debtors are not entitled to strip Lender's lien  
9 under their chapter 13 plan.

#### 12 **Webber Appraisal.**

13 In considering the substance of Mr. Webber's appraisal, the Court is heavily  
14 influenced by the unrefuted evidence from Lender's expert establishing that Mr. Webber's  
15 comparables largely are not appropriate comparables for use for an appraisal of the  
16 Residence.

17 Both appraisers used Comparable One. The principal difference in value attributable  
18 to Comparable One relates to the discount applied against the subject property on account of  
19 a superior view. Mr. Hill made an adjustment of \$28,000.00 while Mr. Webber made a  
20 \$75,000.00 adjustment to value. The Court was not provided sufficient information to  
21 independently determine this issue. Instead, the Court adopts Mr. Hill's determination based  
22 on the overall qualitative superiority of his appraisal. The Court also notes that even if a  
23 more significant reduction was made to Mr. Hill's Comparable One analysis it would not so  
24 impact his appraisal as to render the Lender unsecured.

25 Mr. Hill testified that the remainder of Mr. Webber's comparables were not  
26 appropriate for use as comparables in this case. The Court finds his testimony compelling.  
27 Comparable Two involved a distressed sale and short sale and, thus, reflected the lower  
28

1 limits of sales activity in the area. Mr. Webber's appraisal fails to identify the distressed  
2 short sale nature of this transaction, one which reflects not a typically motivated seller, but a  
3 distressed seller with no opportunity for profit and every incentive to sell the property  
4 quickly.

5         Comparable Three also involved extraordinary sale conditions and, again, this fact  
6 was not identified in Mr. Webber's appraisal. Mr. Hill testified that Comparable Three  
7 involved a seller who was a "motivated builder" interested in clearing out inventory so that  
8 the sales office could be closed. Once again, sale factors other than those of a typically  
9 motivated seller existed and should have been reflected in the Webber appraisal. Even more  
10 significant, however, is the fact that Comparable Three was sold in an unlandscaped state.  
11 Mr. Webber made no positive adjustment as compared to the Residence to reflect the fact  
12 that the Residence enjoys excellent landscaping. Mr. Hill testified that six figure  
13 landscaping expenses could be anticipated. Thus, a substantial upward adjustment to value  
14 was appropriate in connection with Comparable Three, but did not occur.

15         Comparable Four, however, is the most inappropriate of Mr. Webber's alleged  
16 comparables. First it is located in a different development from the Residence.  
17 Notwithstanding, Mr. Webber identified this property as otherwise quite comparable given  
18 the size of the property. In rebuttal, Mr. Hill testified that Comparable Four was more than  
19 17 years older than the Residence, not attractive, vacant, and seriously vandalized. He  
20 described Comparable Four as having holes in the walls, dry wall missing, a mantel missing,  
21 and no carpet or floor covering. Mr. Webber's appraisal contains no adjustment in light of  
22 these factors, and it is unclear that he was aware of these facts. As a result, the Court finds  
23 that there are serious questions regarding Mr. Webber's appraisal that make it inappropriate  
24 for the Court to assume that it correctly reflects the value of the Residence.

25                     **Hill Appraisal.**

26         Mr. Webber alleged some errors in the Hill Appraisal. These errors, however, are far  
27 less significant than those outlined above or proved to be in error. Thus, they do not  
28 suggest that the Hill Appraisal is unreliable.

1 First, Mr. Webber incorrectly testified that Mr. Hill inappropriately utilized square  
2 footage for one of his comparables. Mr. Webber based this assertion on the Multiple Listing  
3 Service which reflected a more significant square footage and that a third garage had been  
4 converted to use as an office. Mr. Webber suggested that an upward adjustment was  
5 necessary in order to account for the increased living space square footage. Mr. Hill  
6 convincingly testified that Mr. Webber's approach was inappropriate. He related that he  
7 contacted the County and determined that his square footage was appropriate as the only  
8 conforming use for the "office" was as the third garage. Mr. Hill, an appraiser with 30 years  
9 of experience and the author of a handbook for use by residential real estate appraisers,  
10 established that where a non-conforming use is the result of an illegal conversion the  
11 appraiser is not entitled to include the non-conforming property in the square footage used  
12 for comparison. Thus, the Court finds that Mr. Hill utilized the appropriate methodology in  
13 this regard and that Mr. Webber's suggestion to the contrary reflects poorly on his analysis  
14 and not on Mr. Hill's.

15 Mr. Webber did correctly note that on one comparable Mr. Hill made a mathematical  
16 error in the calculation of the appropriate adjustment on account of a superior view.  
17 Mr. Hill's testimony was that view adjustments range from 3 to 5% in value. However, his  
18 adjustment fell below the 3% range. The Court's review establishes, however, that even  
19 using a 5% adjustment, the impact on the appraisal would not be significant.

20 Mr. Webber in presenting his "rebuttal" of the Lender's appraisal also advanced two  
21 alternative theories of valuation. First, he presented the Court with an October 1, 2006  
22 listing for the Residence showing that the Residence was on the market for 65 days at a  
23 price between \$975,000.00 and \$1,075,000.00. He testified, without any objection, that the  
24 Residence was not sold at this price and opined that this indicated that it was not properly  
25 priced. The Court gives this testimony no weight. First, this activity occurred more than  
26 twenty months prior to the Petition Date. As a result, it is of dubious temporal relevance.  
27 Further, without any evidence as to the marketing efforts and without any information  
28 regarding the activity in the market at that time, it is impossible for the Court to determine

1 whether unusual factors influenced the Debtors' inability to achieve this price. Indeed, the  
2 fact that Mr. Webber testified that the Residence was not on the market for the average  
3 marketing time is indicative of the highly unreliable nature of this testimony.

4 Mr. Webber also utilized a second alternative theory. Mr. Hill testified that the  
5 market in this area had been in a declining position for approximately 12 months. As a  
6 result, in their rebuttal case, the Debtors supplied a "comparable" listing for a home  
7 allegedly similar to the subject and selling for \$1,025,000.00 approximately one year prior  
8 to the Petition Date. Mr. Webber discounted this amount by 14% and then further  
9 discounted this amount to account for the "golf course view" of the comparable. He then  
10 concluded that it supported his valuation of \$850,000.00 as it would reflect a value of  
11 \$855,055.00. The Court again finds this testimony entitled to limited if any weight. The  
12 problems with Mr. Webber's report are serious and this analysis cannot form a substitute for  
13 a valuation determination appropriately obtained through the use of appraisal methodology  
14 typically relied upon by appraisers. Further, this was not an appraisal methodology relied  
15 upon by Mr. Webber in his appraisal and the unrefuted testimony of Mr. Hill established  
16 that, this is not an appropriate appraisal methodology. Finally, the methodology, if it were  
17 to be used, would require additional details in order for it to be afforded more than a  
18 minimal weight by the Court. While Mr. Webber testified that the home is "similar" to the  
19 Residence, the Lender established on cross-examination that Mr. Webber did not know the  
20 condition of this property and, in fact, had obtained information regarding the house only off  
21 the multiple listing service. As a result, there is no way for the Court to determine whether  
22 this property is truly comparable to the Residence.<sup>8</sup>

23 Finally, the Court in reviewing Mr. Hill's appraisal finds that his comparables  
24 appeared to involve sales closer to the Petition Date and properties closer in proximity to the  
25 Residence. There is no testimony indicating that Mr. Hill's comparables were inappropriate

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27 <sup>8</sup> It is also worth noting that such an approach involves a serious inconsistency on  
28 Mr. Webber's part in that he asks the Court to assume a fourteen percent decline in Residence value  
over the year prior to the petition date while concurrently testifying that the value in October of  
2008, his initial valuation date, was unchanged since the June 2008 Petition Date.

1 or subject to adjustment except as discussed above. While not dispositive, the Court notes  
2 that Mr. Hill is the more experienced appraiser.

3 Thus, the Court finds Mr. Hill's appraisal to be the more credible and determines, as a  
4 result, that the value of the Residence is \$990,000.00. As a result, Debtors are not entitled  
5 to modify the Lender's trust deed in their chapter 13 plan as Lender is an undersecured  
6 rather than an unsecured creditor.<sup>9</sup>

7  
8 DATED: April 2, 2009

  
LAURA S. TAYLOR, JUDGE  
United States Bankruptcy Court

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<sup>9</sup> Lender is instructed to promptly file an order consistent with this Memorandum Decision.