UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

IN RE:	)	CHAPTER 7
	)	
ALEX MICHAEL DIENER,	)	CASE NO. **11-83085** - MHM
BARBARA SUE DIENER,	)	
	)	
Debtors.	)	

ORDER ON TRUSTEE'S FINAL REPORT

Chapter 7 Trustee filed *Trustee's Final Report* December 22, 2014 (Doc. No. 81) (the "Final Report"). Debtors filed *Debtor's Objection to Trustee's Final Report* January 12, 2015 (Doc. No. 83) (the "Objection"). Hearing was held January 27, 2015, after which Debtors filed *Debtors' Memorandum of Law in Support of Objection to Trustee's Final Report* February 6, 2015 (Doc. No. 85) and Trustee filed *Trustee's Response in Opposition to Debtors' Memorandum of Law in Support of Objection to Trustee's Final Report* February 7, 2015 (Doc. No. 86).

BACKGROUND

Debtors filed their Chapter 7 bankruptcy petition November 17, 2011. Debtors were discharged from their debts March 1, 2012. The only value collected on behalf of the estate was $25,267.58 from the sale of 10965 Chandon Way (the "Property"), as the result of an agreement between Trustee and Wells Fargo, the holder of the second and third priority liens on the Property. CitiMortgage held the first-priority lien securing a claim of $227,286.75. Wells Fargo's second and third-priority lien claims total

$128,742.00. Trustee entered into an agreement with Wells Fargo wherein Wells Fargo would receive $9,000.00 from the sale of the Property and Trustee would receive any remaining proceeds after paying the first-priority lien in full (the "Agreement"); this type transaction is known as a "carve-out."

Ultimately, Trustee received an offer to purchase the Property for $280,000.00. Trustee filed June 20, 2012 a *Motion for Approval of Settlement Agreement* (Doc. No. 43), and filed June 21, 2012 a *Motion to Sell Property of the Estate Free and Clear of Liens and Interests and to Disburse Certain Proceeds at Closing* (Doc. No. 44). When no party in interest objected in the time provided by negative notice orders entered June 28, 2012, the Agreement and the sale free and clear of liens stood approved (Docs. No. 46 and 47). Citimortgage's lien was satisfied at closing, and, pursuant to the Agreement, Wells Fargo received $9,000.00 and $25,267.58 was distributed to Trustee on behalf of the estate after satisfaction of taxes and closing costs. Through his Final Report, Trustee proposes to distribute the remaining proceeds as follows:

Trustee's statutory fees:	$ 17,250.04
Trustee's expenses:	$ 99.18
Trustee's attorney fees:	$ 745.37
Trustee's attorney expenses:	$ 275.00
Trustee's accountant fees:	$ 765.00
Trustee's accountant expenses:	$ 35.65
Distribution to unsecured creditors:	$ 6,097.34

Pursuant to 11 U.S.C. § 326, Trustee's statutory fee is $17,250.04. Trustee's attorney fees were originally $14,813.00 with a blended hourly rate of $318.56, but have voluntarily been discounted by nearly 95%, to $745.37, to allow for a 10% distribution to

the Estate's unsecured creditors. Accounting fees represent 3.4 hours of work at $225.00 per hour.

Debtors object to the proposed distribution, arguing that a portion of the $25,267.58 should be distributed to them as they claimed an exemption of $10,000.00 in their original petition.

DISCUSSION

Trustee apparently does not dispute that the exemptions were initially claimed by Debtors in the amount of $10,000.00; however, Trustee argues Debtors' exemptions should not apply to the funds received by the estate pursuant to the carve-out agreement with the lien holders.

Debtors have cited two cases inapposite to the issue at hand. First, Debtors cite *Law v. Siegel*, 135 S.Ct. 1188 (2014) for the proposition that Trustee cannot pay administrative expenses ahead of Debtors exemptions. In *Siegel*, the debtor engaged in bad-faith conduct resulting in increased administrative expenses for the estate. The bankruptcy court disallowed that debtor's exemptions to help defray the costs caused by the debtor's bad-faith conduct; however, the Supreme Court concluded that the bankruptcy court did not have the authority to "surcharge" the debtor's exemptions for any reason. *Siegel*, 134 S.Ct. at 1192-93. In the instant case, Trustee does not seek to surcharge Debtor's exemptions; rather, Trustee argues that Debtor's exemptions could not have attached to the value recovered by the estate. *Siegel* has no bearing in this case.

Debtors also address *In re Mannone*, 512 B.R. 148. In that case, the trustee argued that the value of the debtor's property, as shown by property records and the debtor's schedules, was significantly less than the payoff on the mortgage debt secured by the property, and therefore no equity existed in the property to which the debtor's homestead exemption might attach. 512 B.R. at 150. The trustee located a purchaser willing to assume the mortgage debt encumbering the home and pay $20,000.00 to the trustee, and the trustee sought court approval for the sale. *Id.* Judge Grossman correctly noted, "The very sale proposed by the Trustee establishes that the Debtor's home is not worth less than the debt in that the Purchaser assumes all the debt. The additional $20,000.00 is therefore in addition to the debt, and can be considered equity." *Id.* The court declined to approve the proposed sale because the debtor's exemptions would capture all the proceeds of the sale, leaving the estate with no proceeds and no business rationale in conducting the sale. *Id.* Notably, the *Mannone* court explicitly declined to address the situation presented in the instant case and other cases discussed *infra*, in which the debtors seek to claim exemptions in carve-out proceeds from a short-sale of underwater property. *Id.* at fn1.

The parties do cite cases on point, but none lending more than persuasive authority to this court. Unfortunately, the cases cited highlight divergent legal analyses among courts to have considered the issue. Debtors rely on *In re Wilson*, 494 B.R. 502 (Bankr. C.D. Cal. 2013), in which the court found that a debtor's exemptions must be paid from any proceeds from a § 363 sale regarding that exempted property, without regard to how

the proceeds are identified. Trustee points to *In re Bunn-Rodemann*, 491 B.R. 132 (Bankr. E.D. Cal. 2013) and *In re Baldridge*, 2014 WL 350076 (6th Cir. 2014), which reason that a debtor's exemptions cannot attach to underwater property, and therefore cannot attach to value recovered by a trustee in the short sale of that property.

In *Wilson*, the court concluded that a carve-out functions as a "tip" to the estate to avoid foreclosure proceedings, but the "tip" constitutes proceeds of the Trustee's § 363 sale, subject to validly claimed interests such as liens and exemptions. 494 B.R. at 505-06. The court apparently reasoned that, by agreeing to a carve-out, the lienholders simply agreed to a lesser payoff, allowing the estate to collect remaining proceeds from the sale[1]; because the debtor's exemption takes priority over the estate's interest in the property, the debtor's valid exemptions must be paid from proceeds of the sale before the estate may collect proceeds for distributions to creditors. *Id.*

The 6th Circuit in *In re Baldridge*, 553 Fed. Appx. 598 (6th Cir. 2014) concluded that the sale and carve -out proposed in that case left the junior lienholder partially unsatisfied; because the debtor's interest in the property is subject to the creditors' liens on the property, the debtor's exemptions could not attach to value from the property until the creditors' liens were satisfied: "inasmuch as the sale proceeds were insufficient to satisfy the prior obligations owed to the secured creditors, there was no residual equity in

---

[1] Though both the *Wilson* debtor and trustee apparently believed the property was underwater, the court stated, "Upon [the proposed] sale, Bank of America [the first lienholder] will receive its payoff, Wachovia [the junior lienholder] will receive its payoff, and the Debtor will receive her exemptions, up to the amount validly held."

the property to which debtors' exemptions could attach." *Id.* The court in *In re Bunn-Rodemann*, 491 B.R. 132 (Bankr. E.D. Cal. 2013) addressed the reasoning of both *Wilson* and *Baldridge*. Contrary to the reasoning in *Wilson*, the court in *Bunn-Rodemann* regarded the "tip" recovered as part of a carve-out not as value recovered from the property sold, but as value recovered as a result of the trustee's efforts and powers. A debtor's exemptions reach property as of the petition date. *Id.* at 135, citing *Owen v. Owen*, 500 U.S. 305, 314 n.6 (1991) and *In re Hyman*, 967 F.2d 1316, 1319 n.2 (9th Cir. 1992). Before bankruptcy, a debtor's interest in property might include the debtor's right to negotiate with secured creditors, but once a debtor files a petition under Chapter 7 of the Bankruptcy Code, that right is forfeited and the Chapter 7 trustee is tasked with using his considerably greater leverage to achieve a favorable result for creditors and the estate. *Id.* at 135. Creditors would like an efficient sale process culminating in a sale for the highest possible value; the debtor often wants to remain in the property as long and as cheaply as possible; and the trustee wants to leverage his power to facilitate the other parties by recovering some value for the estate. *Id.* at 135-36. The court reasoned that the debtor cannot claim an exemption in the trustee's rights, powers, and efforts to negotiate with creditors and thereby profit from the trustee's carve-out – the value did not exist when the debtor filed the petition. This interpretation is consistent with 11 U.S.C. § 506(c), which allows a trustee to recover costs and expenses of disposing of property to the extent of any benefit to the secured creditor; the carve-out represents the benefit creditor sees in its arrangement with the trustee.

The reasoning of *Baldridge* and *Bunn-Rodemann* is persuasive in the context of Georgia's exemption statute. O.C.G.A. § 44-13-100(a)(1)[2] provides that Debtors may exempt their "aggregate interest" in their residence. Debtors' aggregate interest in the Property, at the time of filing the petition, was zero – the Property was wholly underwater, and Debtors did not hold an interest superior to the liens of CitiMortgage or Wells Fargo. Debtors' exemptions could not have attached to the Property as of the petition date, and Trustee's carve-out represents the value added from Trustee's efforts and powers, *not* value of the Property itself.

Debtors are asking the Court to forgive them of their debts, and then reward them for it – to find value where none existed previously. The funds created by a trustee's negotiation during a carve-out do not exist at the time the petition is filed. If Trustee had taken no action, Citimortgage would have foreclosed, evicted Debtors, and reported the foreclosure to the credit bureaus. Wells Fargo would have had a claim to whatever funds might have remained, and unsecured creditors would have received nothing. Instead, all of the parties are able to walk away having received something – including Debtors, who received a discharge from their debts without a foreclosure of record.

Finally, Trustee requested $2,500.00 in sanctions from Debtor's attorney for filing a bad faith claim. "Rule 11 is a narrowly cabined provision whose sanctions 'are to be imposed sparingly, as they can have a significant impact beyond the merits of the

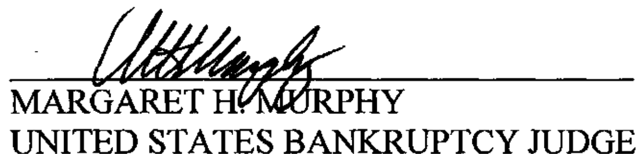
---

[2] The language of O.C.G.A. § 44-13-100(a)(1) is substantially similar to the language of California's exemption statute, as analyzed in *Bunn-Rodemann*. See California Code of Civil Procedure 703.140(b)(1).

individual case and can affect the reputation and creativity of counsel.'" *Bartronics, Inc. v. Power-One, Inc.*, 245 F.R.D. 532, 538 (S.D. Ala. 2007) (*citing Hartmarx Corp. v. Abboud*, 326 F.3d 862, 867 (7th Cir. 2003). Even though Debtor's objection comes late in the case at an inopportune time for Trustee, the totality of the circumstances does not suggest that Debtors' argument was raised in bad faith. Given the different outcomes across courts—and with no settled 11th Circuit precedent directly on point—the objection was not unreasonable, even if it was ultimately unpersuasive. Accordingly, it is hereby

ORDERED that Debtors' Objection is ***denied,*** and Trustee's request for sanctions is ***denied.***

IT IS SO ORDERED, this the 1st day of July, 2015.



MARGARET H. MURPHY
UNITED STATES BANKRUPTCY JUDGE