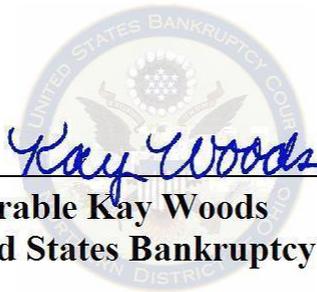


IT IS SO ORDERED.

**Dated: October 30, 2006
03:12:55 PM**



**Honorable Kay Woods
United States Bankruptcy Judge**

**UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO**

IN RE:	*	
	*	CASE NUMBER 05-43885
VILLA MARIE ESTATES, INC.,	*	
fdba COUNTRYSIDE GOLF COURSE	*	CHAPTER 11
	*	
Debtor.	*	HONORABLE KAY WOODS
	*	

M E M O R A N D U M O P I N I O N

This cause is before the Court on the Motion of Nancy A. Valentine, Esq., the Chapter 11 Trustee ("Trustee"), for the Entry of an Order Assessing Surcharge Pursuant to 11 U.S.C. § 506(c) and Reservation of Rights to Assert Future Surcharges and Claim Objections as Necessary filed on September 1, 2006 ("Motion for Surcharge"). Secured Creditor American Tax Funding ("ATF") filed its Response on September 20, 2006. On October 2, 2006, Trustee filed her Reply.

Debtor Villa Marie Estates, Inc. ("Debtor") operated an 18-hole, approximately 150-acre golf course, pro shop, kitchen and bar

in Lowellville, Ohio ("golf course"). On July 1, 2005, Debtor filed its voluntary petition for relief under Chapter 11 of the Bankruptcy Code. On July 29, 2005, the United States Trustee ("UST") appointed a Committee of Unsecured Creditors ("Committee") pursuant to 11 U.S.C. § 1102(a).

Debtor continued to operate the golf course as a debtor-in-possession for approximately eight months; however, the monthly reports for July, August, and September, 2005 reflected continuing net operating losses. Debtor did not file any monthly operating reports after September 30, 1995.

As a consequence, on March 16, 2006, UST filed a Motion to Dismiss the Case or Convert it to a Case Under Chapter 7 of the Bankruptcy Code. At the hearing on the Motion to Dismiss held on April 12, 2006, the Court determined that certain economic and practical considerations favored the case proceeding under Chapter 11. Accordingly, the Court granted the Committee's oral motion for the appointment of a trustee to administer the Chapter 11 case pursuant to 11 U.S.C. § 1104(a)(3). The Court approved the selection of Trustee on April 19, 2006.

Following her appointment, Trustee assumed custody and control of all of Debtor's assets. Trustee ceased operations at the golf course on April 26, 2006. Shortly thereafter, Trustee determined that it was in the best interest of the estate to sell substantially all of Debtor's assets.

Pursuant to the Sale Procedure Order entered by this Court on August 1, 2006, an auction of Debtor's assets was conducted at

which Marucci & Gaffney Excavating Inc. submitted the highest bid of \$1,200,000.00 ("Sale"). The second highest bid of \$1,150,000.00 was submitted by Thomas and Ann Grischow (the "Stalking-Horse Bidder"). On August 11, 2006, this Court entered an Order approving the Sale ("Sale Order"). In the Motion for Surcharge, Trustee asserts that the estate incurred \$222,931.52 in fees and expenses in connection with the maintenance, preservation, protection, and sale of Debtor's assets between April 26, 2006 and August 31, 2006.

ATF acquired its secured status in this case when it purchased seven tax certificates issued on Debtor's property from the Mahoning County Treasurer ("Treasurer") between March 29, 2003 and June 30, 2005 pursuant to R.C. Chapter 5721.

R.C. §§ 5721.32 and 5721.33 authorize a county treasurer to conduct an auction or a negotiated sale of tax certificates to third parties. Section 5721.35(A) grants a first lien to the purchaser of such tax certificates:

Upon the sale and delivery of a tax certificate, such tax certificate vests in the certificate holder the first lien previously held by the state and its taxing districts under section 5721.10 of the Revised Code for the amount of taxes, assessments, interest, and penalty charged against a certificate parcel, superior to all other liens and encumbrances upon the parcel described in the tax certificate, in the amount of the certificate redemption price.

Ohio Rev. Code Ann. § 5721.35 (West 2006).

Trustee concedes that the tax certificates at issue in this case carry a total "certificate purchase price"¹ of \$104,441.75 and that interest on the certificate purchase price accrues on the first day of each month at a contract interest rate of 18% *per annum* pursuant to R.C. § 5721.41.

On or about August 30, 2006, Trustee issued a check to ATF from the proceeds of the Sale in the amount of \$89,080.19 and directed ATF to apply the payment to the certificate purchase price in order to "stop the bleed" created by the contract rate of interest ("August 30 payment"). On October 26, 2006, Trustee filed a Notice that an additional payment of \$15,361.56 was hand delivered to counsel for ATF. As a consequence and as conceded by ATF (see Response at p. 8), Trustee has paid ATF in full for the certificate purchase price (*i.e.*, principal) portion of its claim. The unpaid portion of ATF's claim consists of accrued interest at a rate of 18% *per annum*.

In the Motion for Surcharge, Trustee seeks authorization from this Court to reduce the estate's final payment to ATF, pursuant to 11 U.S.C. § 506(c), by an amount directly proportional to ATF's percentage of the secured debt in this case. Trustee relies upon

¹R.C. § 5721.30 reads, in pertinent part:

"Certificate purchase price" means, with respect to the sale of tax certificates under sections 5721.32 , 5721.33, and 5721.42 of the Revised Code, the amount equal to delinquent taxes, assessments, penalties, and interest computed under section 323.121 of the Revised Code charged against a certificate parcel at the time the tax certificate respecting that parcel is sold. . . . "Certificate purchase price" also includes the amount of the fee charged by the county treasurer to the purchaser of the certificate under division (H) of section 5721.32 of the Revised Code.

R.C. § 5721.30 (West 2006).

11 U.S.C. § 506(c) which permits a trustee to "recover from property securing an allowed secured claim the reasonable and necessary costs and expenses of preserving, or disposing of, such property to the extent of any benefit to the holder of such claim." 11 U.S.C. § 506 (1984).

According to Trustee, ATF's secured claim in the amount of \$151,730.30 represents 17.61% of the aggregate secured proofs of claim filed (\$861,442.99). As a consequence, Trustee requests that this Court approve a reduction in the amount of \$39,266.97 of ATF's secured claim for the reasonable and necessary expenses incurred in preserving and ultimately disposing of the real property.

In its Response, ATF objects to the assessment of the proposed surcharge for two reasons: First, ATF asserts that its status as a holder of a secured claim for real estate taxes prohibits Trustee from assessing a surcharge against ATF for reasonable and necessary expenses under § 506(c). According to ATF, because real estate taxes run with the land, attaching to the real estate itself², the taxes themselves are "a 'reasonable and necessary' cost or expense of the preservation of the real property," and, as a consequence, are not subject to surcharge under § 506(c). Response at p. 5.

ATF also argues that the August 30 payment did not affect the accrual of interest on the tax certificates, because, pursuant to

²At the hearing, Trustee contended that ATF's argument regarding the nature of real estate tax liens was premised upon the theory that the ATF's lien was still attached to the real property. ATF conceded that the Sale Order clearly stated that the assets of the estate were sold free and clear of all liens and that the real estate liens would attach to the proceeds of the Sale. As such, counsel for ATF rejected the idea that his argument was, in fact, a collateral attack upon the Sale Order.

R.C. § 5721.30(E)(1)(a), interest continues to accrue on the certificate purchase price until the entire amount due, including interest and fees, is paid in full. R.C. § 5721.30(E)(1)(a) defines the phrase "certificate redemption price" for tax certificates sold at auction, and reads, in pertinent part:

(E) With respect to a sale of tax certificates under section 5721.32 of the Revised Code . . . both of the following apply:

(1) "Certificate redemption price" means the certificate purchase price plus the greater of the following:

(a) Interest, at the certificate rate of interest, accruing during the certificate interest period on *the certificate purchase price*, calculated in accordance with section 5721.41 of the Revised Code;

(b) Six per cent of the certificate purchase price.

Ohio Rev. Code Ann. § 5721.30 (West 2006)(Emphasis added).

The Court conducted a hearing on the Motion for Surcharge on October 3, 2006. Trustee argued that the expenses listed in the Motion for Surcharge were narrowly tailored and resulted in a direct benefit to the secured creditors of the estate. Trustee further argued that ATF's contention that interest continues to accrue on the "certificate purchase price" despite the August 30 payment would constitute the accrual of compound interest in violation of R.C. § 5721.41, which states that interest on the certificate purchase price is simple interest. Ohio Rev. Code Ann § 5721.41 (West 2006).

ATF countered that any interest accruing on the certificate purchase price was simple interest, despite the fact that, according to ATF's interpretation of the statute, interest would continue to accrue even if the certificate purchase price was paid in full and only interest and fees remained outstanding.

ATF also continued to assert that the nature of the real estate liens as "reasonable and necessary expenses" prevented a holder of such liens from being surcharged pursuant to § 506(c). Furthermore, ATF by underscoring the fact that taxes are the state's "life's blood," argued that the unique nature of their secured claim prevented the assessment of a surcharge on the real property securing its claim.

At the close of the October 3 hearing, the Court requested additional briefing on two issues: (1) whether ATF "stepped into the shoes" of the state when it purchased the tax certificates at issue in this case, and whether, as a consequence of its status as a holder of a lien for real estate taxes, Trustee is prevented from assessing a surcharge against the property securing ATF's claim; and (2) whether interest continues to accrue at 18% *per annum* on the full certificate purchase price despite Trustee's partial payment of the certificate purchase price on August 30, 2006. Simultaneous briefs were filed on October 24, 2006.

As a general rule, in order to prevail on a § 506(c) claim, the claimant bears the burden of proving that the costs were reasonable, necessary, and a benefit to the secured party. *Daniel v. AMCI, Inc. (In re Ferncrest Court Partners, Ltd.)*, 66 F.3d 778,

782 (6th Cir. 1995). The purpose of § 506(c), which was derived from common law, has been explained as follows:

The general rule is that normal administrative expenses of the bankruptcy estate may not be charged against secured collateral but may share in the distribution of the unencumbered assets of the debtor. . . .Section 506(c) of the Bankruptcy Code is the exception to that rule. . . . The provision is equitable in origin, preventing a windfall to a secured creditor at the expense of the trustee or debtor in possession by shifting the costs of preserving or disposing of a secured party's collateral from the bankruptcy estate to the secured party.

Architectural Building Components v. McClarty (In re Foremost Mfg. Co.), 137 F.3d 919, 923 (6th Cir. 1998)(quoting *I.R.S. v. Boatmen's First Nat'l Bank*, 5 F.3d 1157, 1159 (8th Cir. 1993)).

In the case *sub judice*, ATF does not dispute that the expenses listed in Trustee's Motion were reasonable, necessary, and provided a benefit to secured creditors.³ Instead, ATF contends that, because it "stepped into the shoes of the state" when it purchased the tax certificates, ATF has the first and best lien on the proceeds of the Sale pursuant to R.C. § 5721.35. In fact, there is no question that ATF holds "the first lien . . .superior to all other liens and encumbrances upon the parcel described in the tax certificate, in the amount of the certificate redemption price." See R.C. § 5721.35. However, contrary to ATF's argument, the

³In its Supplemental Response to the Motion for Surcharge, ATF argues that the expenses listed in the Motion did not provide a benefit to ATF because ATF would have recovered the full amount of its lien at a state foreclosure sale. Because the Court ordered additional briefing on two specific issues, the Court will not consider ATF's benefit argument, which was raised for the first time in its Supplemental Response.

surcharge proposed by Trustee has no effect on the *priority* of ATF's lien.

The legislative history of the statute reveals that § 506(c) was intended to shift the burden of maintaining and selling the property to the secured lien holder, not to alter the priority of claims set forth in 11 U.S.C. § 507:

At any time the trustee or debtor in possession expends money to provide for the reasonable and necessary cost and expense of preserving or disposing of a secured creditor's collateral, the trustee or debtor in possession is entitled to recover such expenses from the secured party or from the property securing an allowed secured claim held by such party.

H.R. Rep. No. 950598, at 1 (1977), reprinted in 1977 U.S.C.C.A.N. 5963, 6451. As a consequence, ATF's argument that it is the first and best lien holder pursuant to Ohio law, is irrelevant to the § 506(c) analysis.

Furthermore, despite ATF's protestations, the fact that ATF acquired the tax certificates from the Treasurer in no way insulates ATF from a surcharge under § 506(c). Several bankruptcy courts have held that holders of tax liens are nonetheless subject to the provisions of § 506(c) where the requirements of reasonableness, necessity, and benefit to secured creditors have been met. See *In re Council*, 1990 WL 266353 (Bankr. E.D. Cal. Nov. 14, 1990)(IRS as holder of secured tax lien surcharged to pay portion of expenses incurred by special counsel to create fund used to pay IRS claim); *Radtko Heating and Sheet Metal Co., Inc. v. State Bank of Cherry (In re Radtko)*, 103 B.R. 932 (Bankr. N.D. Ill. 1989)(IRS tax lien subject to surcharge for reasonable and

necessary expenses); *Goldberg v. City of New York (In re Navis Realty)*, 193 B.R. 998 (Bankr. E.D. N.Y. 1996)(city as holder of secured tax lien surcharged for administrative expenses pursuant to 506(c)).

Finally, ATF contends that the recent amendment to § 506(c) by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"), which recognizes *ad valorem* property taxes as "reasonable and necessary costs and expenses," prohibits Trustee from assessing a surcharge against holders of real estate liens. According to ATF, a holder of a lien for a reasonable and necessary expense cannot be surcharged for other reasonable and necessary expenses. Not surprisingly, ATF cites no case law to support this claim.

The argument of ATF misses the mark in three respects. First, BAPCPA is not controlling to the issue before the Court because this case was filed prior to the effective date of BAPCPA. Next, two courts interpreting pre-BAPCPA § 506(c) held that the payment of post-petition real estate taxes does not fulfill the "benefit to secured creditors" prong of the § 506(c) analysis. See *United Jersey Bank v. Miller (In re Consolidated Cotton Gin Co. Inc.)*, 347 B.R. 572 (Bankr. N.D. Tex. 2006); *In re C.S. Assoc.*, 29 F.3d 903, 907 (3rd Cir. 1994). The *C.S. Assoc.* Court wrote:

Monies a government entity derives from the collection of real property taxes fund many governmental operations and services which are not directly related to preservation and disposal of the asset and in no way provide a benefit to the secured creditor. Real estate tax revenues support public parks, libraries, schools, and social services,

which do not constitute expenses peculiarly connected with preserving or disposing of the parcel of land.

Id. at 907.

Last, ATF's secured status is based on pre-petition - as opposed to post-petition - real estate taxes. A tax lien for pre-petition real estate taxes cannot constitute an administrative cost or expense, as required by § 506(c). Even though under BAPCPA, post-petition *ad valorem* taxes can themselves be considered § 506(c) expenses, that does not lead to the conclusion that a secured claim for pre-petition *ad valorem* taxes cannot be surcharged. As a consequence, the Court finds that ATF's argument regarding immunity based upon the status of their lien is not persuasive.

ATF, as a secured creditor, is subject to a surcharge for the reasonable and necessary expenses of maintaining and selling the property securing ATF's lien. Here, the maintenance of the real property - a golf course - was essential to its value at the Sale. There is no question that the golf course would have been substantially less appealing to potential purchasers had the course itself been permitted to become overgrown. Moreover, the winning bid at auction was substantially higher than the original bid of the Stalking Horse. "[W]here preservation of the secured asset requires the expenditure of funds which actually creates a special benefit, such as improving the asset, increasing its value, etc., a surcharge is justified." *Heidelberg Harris Inc. v. Grogan (Matter of Estate Design & Forms, Inc.)*, 200 B.R. 138, 142 (Bankr. E.D.

Mich 1996). Consequently, there is no question that the maintenance and sale of the property benefitted ATF.

Furthermore, the equitable nature of § 506(c) favors the imposition of a surcharge against any secured creditor who benefits from the maintenance and sale of the property securing its lien. Section 506(c) was codified to shift the cost of maintaining and selling property to the creditor who benefits from its maintenance and sale. The benefit accrues to the secured creditor regardless of the type of lien or the manner in which the lien was acquired. Clearly, the expenses at issue in this case should be borne by AFT and any other creditor who benefitted from the enhanced value of the secured property.

Having concluded that AFT is subject to a surcharge pursuant to § 506(c), the Court turns to the issue of the accrual of interest under the Ohio statute. Neither party has cited, nor has the Court found, any state or federal cases law interpreting R.C. § 5721.30(E). Accordingly, it appears that this issue presents a matter of first impression.

Although R.C. § 5721.30(E)(1)(a) read in a vacuum appears to favor ATF's interpretation of the statute, a review of the statute as a whole indicates that the drafters contemplated only one lump sum payment of the "certificate redemption price" and did not contemplate partial payments of this amount.

For instance, R.C. § 5721.30(F), which defines the phrase "certificate redemption price" for tax certificates sold as the result of a negotiated sale, reads, in pertinent part:

(F) With respect to a sale of tax certificates under section 5721.33 of the Revised Code, "certificate redemption price" means the amount equal to the sum of the following:

(1) The certificate purchase price;

(2) Interest accrued on the certificate purchase price at the certificate rate of interest from the date on which a tax certificate is delivered through and including *the day immediately preceding the day on which the certificate redemption price is paid;*

Ohio Rev. Code Ann. § 5721.30 (West 2006)(Emphasis added).

Because the statute references "the day on which the certificate redemption price is paid," the Court finds that the statute presumes a single payment, and, therefore, the drafters did not address the effect of partial payments or installment payments. However, based upon the numerous references to "simple interest" in R.C. Chapter 5721⁴, it is clear that the drafters intended that interest would accrue only on the principal balance⁵ of the certificate purchase price.

In other words, because the drafters foreclosed the accrual of compound interest by statute, the Court finds it unlikely that they

⁴The accrual of simple interest is referenced in R.C. §§ 5721.30, 5721.32, 5721.32, and 5721.41.

⁵ See www.investorwords.com (defining "principal" as "the amount borrowed, or the part of the amount borrowed which remains unpaid (excluding interest)")(emphasis added).

intended to create a payment scheme whereby the failure to pay off the certificate purchase price by, for example, one dollar, would allow a certificate holder to continue to collect interest on the entire amount originally owed.

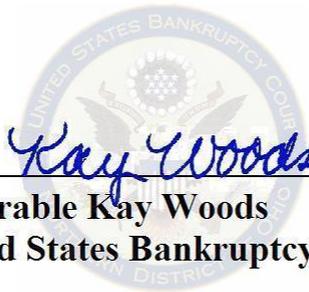
As a consequence, because Trustee has paid ATF the certificate purchase price in full, interest no longer continues to accrue. The only part of ATF's claim that remains unpaid is accrued interest on the certificate purchase price, including the interest which accrued on September 1, 2006 and October 1, 2006 on the then outstanding balance of \$15,361.56. Trustee may deduct the proportionate amount of the surcharge from the remainder of the claim amount and pay the difference in full satisfaction of ATF's secured claim.

An appropriate order will follow.

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IT IS SO ORDERED.

**Dated: October 30, 2006
03:12:55 PM**


Kay Woods

**Honorable Kay Woods
United States Bankruptcy Judge**

**UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO**

IN RE:	*	
	*	CASE NUMBER 05-43885
VILLA MARIE ESTATES, INC.,	*	
fdba COUNTRYSIDE GOLF COURSE	*	CHAPTER 11
	*	
Debtor.	*	HONORABLE KAY WOODS
	*	

O R D E R

For the reasons set forth in this Court's memorandum opinion entered on this date, the Court grants the Motion of Nancy A. Valentine, Esq., the Chapter 11 Trustee, for the Entry of an Order Assessing Surcharge Pursuant to 11 U.S.C. § 506(c) and Reservation of Rights to Assert Future Surcharges and Claim Objections as Necessary filed on September 1, 2006.

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