

IT IS SO ORDERED.



Dated: February 13, 2007
12:29:34 PM

Honorable Kay Woods
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO

IN RE:

CASE NUMBER 05-49330

KIMPEL'S JEWELRY & GIFTS, INC.,

HONORABLE KAY WOODS

Debtor.

M E M O R A N D U M O P I N I O N
NOT INTENDED FOR PUBLICATION

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This cause is before the Court on the Motion of Perpetual Savings Bank for Order (I) Determining That Certain Assets Are Not Property of the Estate and (II) to the Extent Such Assets Are

Property of the Estate, Determining Value of Secured Claim (the "Motion") filed by Perpetual Savings Bank¹ ("Perpetual") on October 24, 2006. The Motion specifically requests the Court to determine: (i) whether Kimpel's Jewelry & Gifts, Inc. ("Debtor") or William Kimpel ("Mr. Kimpel") owns four (4) Gemstones² (as defined *infra*) in possession of Perpetual; and (ii) if the Gemstones are property of Debtor's estate, the monetary value of Perpetual's secured interest in the Gemstones. Home Savings and Loan Company of Youngstown, Ohio ("Home Savings") and National City Bank ("National City") have valid perfected security interests in all of Debtor's inventory and assets, but no interest in Mr. Kimpel's property. On November 13, 2006, Home Savings filed Objection of the Home Savings and Loan Company of Youngstown, Ohio to Motion of Perpetual Savings Bank for Order (I) Determining That Assets Are Not Property of the Estate and (II) to the Extent Such Assets Are Property of the Estate Determining Value of Secured Claim (the "Response").

On December 8, 2006, the Court conducted an evidentiary hearing on the Motion and Response (the "Hearing"). David Hunter, Esq. appeared at the Hearing on behalf of Perpetual. Shirley J. Smith, Esq. appeared at the Hearing on behalf of Home Savings. Richard Zellers, Esq. appeared at the hearing on behalf of Debtor;

¹ At the hearing, Perpetual represented that it had been acquired by Sky Bank, but the Court will refer to this entity as Perpetual.

² The four (4) Gemstones were described as follows: a 3.01 carat rectangular fancy yellow diamond engagement ring, a square 1.02 carat green-yellow diamond engagement ring, a loose .53 carat fancy pink pear cut diamond and a loose 1.20 carat deep yellow-orange emerald cut diamond.

however he did not elicit testimony, offer any documents or provide a statement of any kind. National City did not appear at the Hearing. The Court received testimony of Mr. Kimpel (Debtor's principal and president), Amanda Banner (Perpetual's in-house attorney), and Thomas Duma (expert witness).

This Court has jurisdiction pursuant to 28 U.S.C. §§ 157 and 1334. Venue in this Court is proper pursuant to 28 U.S.C. §§ 1408 and 1409. This is a core proceeding pursuant to 28 U.S.C. §§ 157(b)(2)(A), (B), (K) and (O). The following constitutes the Court's findings of fact and conclusions of law pursuant to FED. R. BANKR. P. 7052.

I. FACTS

Debtor is a closely held corporation whose principal and president is Mr. Kimpel. Mr. Kimpel testified that he and Debtor would loan money to each other and would satisfy such loans with cash or gemstones. Debtor would also sell gemstones owned by Mr. Kimpel. Debtor kept track of all gemstones, whether they were owned by Debtor or Mr. Kimpel, on a computer program known as Jewelry Shopkeeper. Since Debtor's records did not distinguish the ownership of the stones, Mr. Kimpel relied on his accountants - Hill, Barth and King ("Accountants") - to account for which gemstones were owned by Debtor and which gemstones were owned by Mr. Kimpel. Debtor also relied on Accountants to keep records concerning the various loans between Debtor and Mr. Kimpel, including whether and how (i.e., by cash or gemstone) each loan was satisfied. Mr. Kimpel also kept records concerning such

information: however, Mr. Kimpel testified that a briefcase, which contained his records, was stolen prior to the bankruptcy filing.

On or about February 28, 2005, Debtor and Mr. Kimpel executed and delivered promissory note no. 503894-50 ("Note 1") to Perpetual in the amount of \$100,000.00, which evidenced Debtor's and Mr. Kimpel's joint and several repayment obligation. Note 1 was originally secured by an oval pink diamond (not set) weighing .34 carat and a square orange diamond (not set) weighing 1.20 carats. The collateral was pledged by both Debtor and Mr. Kimpel. Perpetual took possession of the oval pink diamond and square orange diamond, thus perfecting its interest pursuant to O.R.C. § 1309.313. Subsequently, on or about June 30, 2005, Debtor, Mr. Kimpel and Perpetual entered into a Change in Terms Agreement, which required (i) Perpetual to release the .34 carat oval pink diamond, and (ii) Debtor and Mr. Kimpel to replace it with a yellow diamond ring set in white gold, weighing 3.01 carats.

On or about March 2, 2005, Debtor and Mr. Kimpel executed and delivered promissory note no. 503894-51 ("Note 2" and collectively with Note 1, the "Notes") to Perpetual in the amount of \$200,000.00, which evidenced Debtor's and Mr. Kimpel's joint and several repayment obligation. Note 2 was originally secured by a pear pink diamond (not set) weighing .53 carat and a square green-yellow diamond in a platinum setting weighing 1.02 carats. This collateral was also pledged by both Debtor and Mr. Kimpel. Perpetual took possession of the pear pink diamond and square

green-

yellow diamond, thus perfecting its interest pursuant to O.R.C. § 1309.313.

Pursuant to the Notes, Debtor and Mr. Kimpel currently owe Perpetual approximately \$285,000.00. As security for these Notes, Perpetual has in its possession a square orange diamond (not set) weighing 1.20 carats, yellow diamond ring set in white gold weighing 3.01 carats, a pear pink diamond (not set) weighing .53 carat and a square green-yellow diamond in a platinum setting weighing 1.02 carats (collectively, the "Gemstones").

Debtor also currently owes National City and Home Savings collectively approximately \$326,000.00. At the Hearing, the parties stipulated that National City has the first and best perfected priority interest in all of Debtor's assets and that Home Savings has the second best perfected priority interest in all of Debtor's assets. The parties also agree that, if Debtor owns the Gemstones, Perpetual has a perfected security interest in the Gemstones, which is junior to both National City and Home Savings. However, if Mr. Kimpel owns the Gemstones, Perpetual has the first and best perfected security interest in the Gemstones and neither National City nor Home Savings has any interest in the Gemstones.

On October 15, 2005 (the "Petition Date"), Debtor petitioned for relief under chapter 11 of the Bankruptcy Code and Mr. Kimpel, individually, petitioned for relief under chapter 7 of the Bankruptcy Code (Case no. 05-49432). On November 9, 2005, Debtor filed Schedule B (Personal Property), which lists inventory located at Perpetual with a value of \$210,000.00. (Doc. # 32.) At the

hearing, the parties agreed that the \$210,000.00 inventory on Debtor's Schedule B describes the Gemstones held by Perpetual. On the same date Debtor filed Schedule B, Mr. Kimpel, as president of Debtor and under penalty of perjury, signed Declaration Concerning Debtor's Schedules. (Doc. # 32.) On November 30, 2005, Mr. Kimpel filed his schedules (Doc. # 17), which did not list the Gemstones. Mr. Kimpel, on his own behalf and in his individual capacity, signed the Declaration Concerning Debtor's Schedules to verify his schedules.

II. OWNERSHIP OF THE GEMSTONES

Perpetual alleges that Mr. Kimpel owned the Gemstones at the time they were provided as security for Notes 1 and 2 and at all times thereafter. Perpetual relies on the Affidavit of William R. Kimpel ("Kimpel Affidavit") dated January 30, 2006.³ Paragraphs 5 and 6 of the Kimpel Affidavit attest that Mr. Kimpel, individually, owned the Gemstones at the time they were pledged as collateral and thereafter. Perpetual also relies on the testimony of Amanda Banner, Perpetual's in-house lawyer in charge of the credit recovery of the Notes. Ms. Banner testified that she understood Mr. Kimpel owned the Gemstones free and clear when Notes 1 and 2 were executed. However, Ms. Banner did not prepare the Notes and did not have first-hand knowledge of any representations about ownership of the Gemstones. Home Savings relies on the schedules filed by Debtor and Mr. Kimpel to support its position that Debtor

³ Perpetual attempted to bolster its argument by stating the Kimpel Affidavit was (i) the result of conversations by, between and among Perpetual, Debtor and Debtor's counsel and (ii) reviewed by Debtor's counsel before signature. (Motion at ¶ 11.) This argument has no relevance.

owns the Gemstones. Hence, the testimony of Mr. Kimpel - as the one person uniquely situated to know - is the determining factor concerning ownership of the Gemstones.

Although the Kimpel Affidavit states that Mr. Kimpel owned the Gemstones personally, at the Hearing, Mr. Kimpel testified that he did not personally own the Gemstones. Mr. Kimpel testified that Debtor would occasionally sell property that he owned personally. When Debtor sold an asset belonging to Mr. Kimpel, Debtor would enter that sale into Jewelry Shopkeeper without designating ownership of the particular gemstone. Mr. Kimpel also testified that he and Debtor would make loans to each other and would satisfy such loans with cash or gemstones, which might include gemstones already located at Debtor's store and entered in Jewelry Shopkeeper. Since Debtor is a closely held corporation and there were numerous transactions between Debtor and Mr. Kimpel, Mr. Kimpel relied on Accountants to keep track of (i) the ownership of each gemstone, and (ii) his indebtedness to Debtor - or *vice versa* - and how such indebtedness was satisfied.⁴ Mr. Kimpel, however, could not recreate the ownership and loan information because he no longer had his briefcase, which contained all of his records. Hence, the only evidence that was presented in regards to the ownership of the Gemstones was his testimony.

Mr. Kimpel testified that he "did not own [the Gemstones] personally [because] they were given back to the store for them to be re-SKU-ed . . . back into the store inventory [so the Gemstones]

⁴ Accountants were not called to testify at the Hearing.

would be the property of the [Debtor] because it would have reduced my indebtedness even though I paid for them personally." Mr. Kimpel also testified that the Gemstones were given to Debtor to reduce his indebtedness "long before the bankruptcy."

Mr. Kimpel explained that the discrepancy between the schedules and his affidavit was the result of confusion when he signed the affidavit. He stated that he put the bankruptcy schedules together very quickly and that the various secured parties were "throwing things" at him, which confused him. He stated his "concern was . . . to get everyone secured and paid off." Furthermore, Mr. Kimpel testified that he knew the Gemstones were in Debtor's inventory, but did not understand how the ownership of the stones affected the various secured parties. Additionally, Mr. Kimpel testified that he thought the import of the affidavit was that he owned the Gemstones at one point in time. He stated that he signed the affidavit not knowing the current status of the Gemstones, but knowing he originally purchased the Gemstones with his personal funds.⁵

On re-direct, Perpetual's counsel asked Mr. Kimpel to clarify his contradictory statements about the Gemstones and state once-and-for-all who owned the Gemstones, to which Mr. Kimpel stated:

At the time that I filed my corporate bankruptcy . . . I felt that [the Gemstones] were owned by the [Debtor]. They are in the [Debtor's] inventory now. I don't own anything personally and I didn't as of the time of my corporate or personal bankruptcy. . . . so I

⁵ Mr. Kimpel testified that a review of his records revealed he had not purchased the yellow diamond ring set in white gold weighing 3.01 carats; rather, Debtor purchased that Gemstone.

guess I misunderstood . . . when I was signing personally that the affidavit that I was signing that I owned [the Gemstones] personally, I knew that I bought them at one point not recognizing that if I transferred them back to the store that they were store property . . . they belong to the corporation even though I originally owned them at one point.

Despite the discrepancy between the schedules and the Kimpel Affidavit, Mr. Kimpel expressly testified at the Hearing that he did not individually own the Gemstones "long before the bankruptcies" and that he did not "own anything personally . . . [at] the time of [his] corporate or personal bankruptcy." As a consequence, this Court finds that the Gemstones are property of Debtor's estate.

III. SECURED AMOUNT OF PERPETUAL'S CLAIM

Since the Court finds that the Gemstones are property of Debtor's estate, it will now address Perpetual's request that the Court determine the amount of Perpetual's secured claim. As previously noted, Perpetual stipulated that National City has the first and best lien on Debtor's inventory, including the Gemstones, Home Savings has the second best lien on Debtor's inventory, including the Gemstones, and Perpetual has a junior secured claim to the Gemstones. Despite its acknowledged third priority status, Perpetual argues that it should be allowed to retain possession of and be able to sell the Gemstones because the total value of Debtor's assets is more than enough to satisfy the liens of National City and Home Savings. Perpetual argues that, if National City and Home Savings were required to marshal their liens,

Perpetual would be entitled to liquidate the Gemstones because the senior perfected secured creditors would be over-secured.

Home Savings counters that Perpetual should not be able to liquidate the Gemstones because Debtor's Disclosure Statement postulates a liquidation value of \$161,000.00 for all of Debtor's inventory. Accordingly, Home Savings argues that, in the event of liquidation, if Perpetual is allowed to retain the Gemstones, it would be paid before the senior secured creditors. This Court agrees with Home Savings. Based on Debtor's liquidation value (which is the only such evidence before the Court), if Debtor liquidates its inventory, the senior secured creditors will not be paid in full. Hence, even if National City and Home Savings were required to marshal their liens, it does not appear that they would be paid in full without utilizing the Gemstones for payment.

Home Savings also argues that Perpetual failed to properly value Debtor's assets. Debtor has proposed a plan of reorganization that contemplates Debtor continuing to operate a retail jewelry business. Under these circumstances, the proper methodology for valuing Debtor's inventory, including the Gemstones, is on a going concern basis (*i.e.*, fair market value). The going concern value is an amount that Debtor could receive in the ordinary course of business for each piece of inventory or, more specifically, "the price which a willing seller under no compulsion to sell and a willing buyer under no compulsion to buy would agree after the property has been exposed to the market for a reasonable time." *United States v. Taffi (In re Taffi)*, 96 F.3d

1190, 1192 (9th Cir. 1996)(en banc), *cert. denied*, 521 U.S. 1103 (1997).

As a consequence, § 506(a) requires the Court to determine the estate's interest and the various creditors' interests in the Gemstones based upon their fair market value.

An allowed claim of a creditor secured by a lien on property in which the estate has an interest . . . is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property . . . and is an unsecured claim to the extent that the value of such creditor's interest . . . is less than the amount of such allowed claim. Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest.

11 U.S.C. § 506(a) (emphasis added).

To determine if Perpetual has any secured interest in the Gemstones, the Court must determine the going concern value of (i) Debtor's inventory and (ii) the Gemstones. See *In re Taffi*, 96 F.3d at 1193 (court must determine value based on actual situation presented). Unfortunately, the Court is not able to conduct this analysis because there is no conclusive evidence regarding the fair market value of either Debtor's inventory or the Gemstones.

Perpetual elicited testimony from Mr. Kimpel regarding Debtor's Inventory Report by Stock Number dated November 29, 2006 (the "Inventory Report")(ex. 3). Mr. Kimpel testified that the Inventory Report listed Debtor's inventory (including the Gemstones) with a cost of approximately \$1.6 million and a retail value of \$3.4 million. However, there was no evidence or testimony

about how these values were derived and/or the accuracy of such amounts. More importantly, there was no evidence about how - if at all - these amounts relate to the going concern value of Debtor. Although the retail value listed on the Inventory Report may be the same as the going concern value of Debtor's inventory, there was no testimony to that effect. Indeed, Perpetual's expert witness, Thomas Duma, testified that there is no standardized pricing for diamonds and, consequently, the retail value is the price a buyer and seller negotiate at any given time. Because there is conflicting evidence about the fair market value of Debtor's entire inventory, the Court cannot determine whether National City and Home Savings are over-secured, which is a necessary first step before the Court can determine whether Perpetual has any interest in the Gemstones.

Even if, *arguendo*, the retail amount in the Inventory Report accurately reflects the going concern retail value of Debtor's entire inventory, including the Gemstones, the Court cannot determine the secured value of Perpetual's claim because Perpetual failed to prove the fair market value of the Gemstones.

Perpetual elicited testimony from Mr. Kimpel regarding the retail value on the Inventory Report for each Gemstone in question. Perpetual's counsel asked Mr. Kimpel to provide "an opinion" as to the value of the Gemstones. Mr. Kimpel testified the current market values were as follows: \$30,000.00 to \$40,000.00 for the square orange diamond; \$45,000.00 for the yellow diamond ring set; \$100,000.00 to \$125,000.00 for the pear pink diamond; and

\$35,000.00 to \$45,000.00 for the square green-yellow diamond. Thus, Mr. Kimpel testified that the fair market value for each Gemstone is a range of values - and such values are not consistent with the values in the Inventory Report. Mr. Kimpel failed to provide any explanation or basis for his range of values.

Perpetual also called Mr. Duma as an expert witness to testify about the value of the Gemstones.⁶ On December 1, 2006, Mr. Duma examined the Gemstones and matched the Gemstones certifications to each individual stone. Mr. Duma valued the Gemstones at replacement cost, which is the price for which he could purchase similar gemstones, plus a reasonable profit margin. Mr. Duma's replacement cost for the Gemstones was: \$12,480.00 for the square orange diamond; \$53,077.00 for the yellow diamond ring set; \$34,450.00 for the pear pink diamond; and \$93,020.00 for the square green-yellow diamond.⁷ However, this testimony does not provide the Court with any guidance because the testimony dealt with replacement value instead of fair market value and "fair market value is not 'replacement value.'" *In re Taffi*, 96 F.3d at 1192. Mr. Duma testified that he could not provide the Court with a fair market value of the Gemstones because there is no standardized pricing for diamonds and he could not predict what a buyer and seller would negotiate for any one of the Gemstones. Because Mr.

⁶ Thomas Duma has been in the jewelry business since 1980 and is currently president of Thom Duma Fine Jewelers. Mr. Duma conducts appraisals on a daily basis for estate purposes, insurance purposes, liquidation purposes and bankruptcy estates (including whole store appraisals).

⁷ Mr. Duma's valuation differs significantly from Mr. Kimpel's valuation (i.e., 65,000.00 to \$90,000.00 difference in the valuation of the pear pink diamond alone).

Duma did not and could not testify about the fair market value of the Gemstones, the Court cannot use Mr. Duma's testimony to determine the value of Perpetuals's secured claim.

IV. CONCLUSION

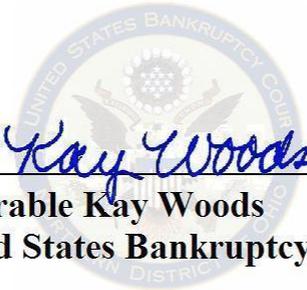
The Court finds that the Gemstones are property of Debtor's estate because Mr. Kimpel specifically testified that he did not own the Gemstones "long before the bankruptcies." The Court cannot determine the amount, if any, of Perpetual's secured claim because Perpetual failed to prove the fair market value of either Debtor's inventory or the Gemstones.

An appropriate order will follow.

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IT IS SO ORDERED.

**Dated: February 13, 2007
12:29:35 PM**



**Honorable Kay Woods
United States Bankruptcy Judge**

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

IN RE:

KIMPEL'S JEWELRY & GIFTS, INC.,

Debtor.

CASE NUMBER 05-49330

HONORABLE KAY WOODS

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O R D E R

For the reasons in this Court's Memorandum Opinion entered on this date, the Court finds that collateral held by Perpetual Savings Bank ("Perpetual") is the property of Kimpel's Jewelry and Gifts, Inc.'s estate. The Court cannot determine an amount, if any, of Perpetual's secured claim because Perpetual failed to prove either the fair market value of Debtor's inventory or the Gemstones.

IT IS SO ORDERED.

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