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MAR 27 2002  
UNITED STATES BANKRUPTCY COURT  
EASTERN DISTRICT OF CALIFORNIA

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UNITED STATES BANKRUPTCY COURT  
EASTERN DISTRICT OF CALIFORNIA  
SACRAMENTO DIVISION

ENTERED ON DOCKET  
MAR 29 2002  
UNITED STATES BANKRUPTCY COURT  
EASTERN DISTRICT OF CALIFORNIA

In re	)	Case No. 01-29743-A-13J
THOMAS M. WITTE,	)	Motion Control No. JPJ #2
	)	Date: March 26, 2002
Debtor.	)	Time: 9:00 a.m.
	)	

MEMORANDUM

This chapter 13 case was dismissed on January 29, 2002 at the request of the debtor. Because the case had not previously been converted from another chapter, the court was required to dismiss the case without conducting a hearing. 11 U.S.C. § 1307(b).

Prior to dismissing the case, the court authorized the debtor to sell a residential real property located at 127 Mesquite Court, Folsom, California. The debtor and his spouse owned a one-half interest in that property. The owners of the other one-half interest, the debtor's parents, consented to the sale.

An order permitting the sale was entered on October 22, 2001. Pursuant to the terms of the sale order, approximately \$22,000.00 was deposited into a blocked, interest bearing account

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1 controlled by the chapter 13 trustee. These funds represented a  
2 portion of the sale proceeds and were to be held by the chapter  
3 13 trustee until the bankruptcy court determined whether the  
4 debtor and/or various lien holders were entitled to the funds.  
5 The sale order was very comprehensive and addressed the following  
6 issues.

7 • The sale order identified those lien holders whose  
8 claims were not paid from escrow. It specified the  
9 recording dates for each of these liens. See Paragraph 10.  
10 The sale was "free and clear" of all liens pursuant to 11  
11 U.S.C. § 363(f). See Paragraphs 6 and 8.

12 • It identified those lien holders who were to be paid  
13 from escrow. See Paragraph 11.

14 • The sale order required the debtor to deposit the  
15 remaining sale proceeds into an interest bearing bank  
16 account. The account was placed under the control of the  
17 chapter 13 trustee, Jan Johnson, and subject to invasion  
18 only upon further court order. Until the bankruptcy court  
19 determined which of the unsatisfied lien holders were  
20 entitled to the funds in the account, the proceeds were to  
21 remain "blocked" in the account. See Paragraph 11(f).

22 • At Paragraph 7, the sale order provided: "*Those*  
23 *entities asserting an interest in any or all of the Property*  
24 *will be adequately protected within the meaning of Section*  
25 *363(e) of the Bankruptcy Code by their interests attaching*  
26 *to the proceeds of sale as set forth in this Order.*"

27 • At Paragraph 11(f), the order provided: "*All other*  
28 *[unpaid] liens, claims, encumbrances, including specifically*

1 but not without limitation, those set forth in Paragraph 10  
2 hereinabove, shall attach to the proceeds and shall be of  
3 the same validity, force, status, extent and/or effect as  
4 the liens, claims and encumbrances of such parties in the  
5 property prior to closing."

6 • At Paragraph 18, this court reserved jurisdiction "over  
7 the proceeds of sale, and further retains jurisdiction to  
8 determine any disputes or controversies arising in  
9 connection therewith or relating thereto, including, without  
10 limitation, the determination of the amount[,] validity,  
11 enforceability and priority of claims with respect to the  
12 proceeds."

13 The debtor and the Internal Revenue Service both demand the  
14 funds in the account. Because the trustee has received their  
15 conflicting demands, and because the court has dismissed the  
16 chapter 13 petition, the trustee is asking the court for  
17 instructions on the disposition of the funds.

18 The debtor reasons that he is entitled to the funds in the  
19 account by virtue of 11 U.S.C. § 1326(a)(2), which provides: "If  
20 a plan is not confirmed, the trustee shall return any such  
21 payment to the debtor, after deducting any unpaid claim allowed  
22 under section 503(b). . . ." The term "such payment" is a  
23 reference to section 1326(a)(1) which requires the debtor to  
24 begin "making the payments proposed by a plan within 30 days  
25 after the plan is filed."

26 However, the money held by the trustee is not a payment  
27 proposed by a plan. The original plan required the debtor to  
28 make 36 payments of no less than \$1,500.00 a month from his

1 disposable income. See Chapter 13 plan filed September 4, 2001.  
2 The amended plan required the debtor to pay \$100.00 a month until  
3 June 2002, then to pay \$1,550.00 from July 2002 for the remainder  
4 of the 36-month term. See Amended Chapter 13 plan filed January  
5 15, 2002. Neither plan called for the sale of property or the  
6 payment of the sale proceeds to creditors. The proceeds from the  
7 sale of the property, then, were not plan payments within the  
8 meaning of section 1326(a)(2).

9 The debtor also argues that turnover is required by 11  
10 U.S.C. § 349(b)(3) which provides that dismissal of a petition  
11 *"revests the property of the estate in the entity in which such*  
12 *property was vested immediately before the commencement of the*  
13 *case. . . ."* Section 349(b)(3), however, does not require the  
14 return of the funds in the account to the debtor.

15 First, prior to the commencement of the case, the lien  
16 holders as well as the debtor held an interest in the real  
17 property. Their respective interests, by virtue of the sale  
18 order, attached to the proceeds in the account. If the funds in  
19 the account must be returned to the *"entity in which such*  
20 *property was vested immediately before the commencement of the*  
21 *case,"* the funds must be turned over to the lien holders in the  
22 order of their respective priorities, not to the debtor (at least  
23 in the absence of a surplus). The interest of the debtor and his  
24 spouse is limited to any surplus remaining after payment of the  
25 liens.

26 Second, the preamble of section 349(b)(3) specifies that the  
27 funds are to be turned over *"[u]nless the court, for cause,*  
28 *orders otherwise."* The court has ordered otherwise. The sale

1 order required the trustee to hold the net sale proceeds pending  
2 a further order determining whether and which lien holders were  
3 entitled to the proceeds. The dismissal order did not make this  
4 determination.<sup>1</sup>

5 Third, the sale order directed the trustee to hold the  
6 proceeds in a separate account pending further court order.  
7 Until such an order is issued, the lien holders have a  
8 replacement lien on the account. This was the adequate  
9 protection required by section 11 U.S.C. § 363(e). That  
10 protection did end simply because the case was dismissed. A  
11 contrary holding would mean, given the unqualified right bestowed  
12 on a chapter 13 debtor by section 1307(b) to dismiss a petition  
13 on demand, that any such adequate protection would be so illusory  
14 that the moniker "adequate" protection would be a misnomer.<sup>2</sup>

15 The dismissal of the case did not abrogate the sale order or  
16 the rights of the lien holders in the account.

17 To the extent the debtor makes any argument that the  
18 dismissal of the case terminated the bankruptcy court's  
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20 <sup>1</sup> While the sale order predates the dismissal order,  
21 nothing in section 349(b)(3) requires that the court "order  
22 otherwise" contemporaneously with dismissal.

23 <sup>2</sup> At the oral argument on the trustee's motion for  
24 instructions, the debtor suggested he might file a chapter 7  
25 petition if he were to be paid the funds in the account.  
26 Presumably, he would claim the funds as exempt. As he has done  
27 in this case, the debtor may claim exemptions pursuant to Cal.  
28 Civ. Proc. Code § 703.140(b). Sections 703.140(b)(1) & (5), as  
of January 1, 2002, together permit a debtor to exempt equity up  
to \$18,350.00 in any asset(s). The debtor previously exempted  
\$7,750.00 pursuant to section 703.140(b)(1) & (5). Assuming the  
previously exempted assets are still owned by the debtor and have  
the same value, he could exempt in a new chapter 7 case at least  
\$10,600.00 of the funds if turned over to him.

1 jurisdiction to adjudicate the rights of the lien holders and the  
2 debtor in the sale proceeds, the court notes that its  
3 jurisdiction was specifically reserved in Paragraph 18 of the  
4 sale order.

5 Even if the court's jurisdiction had not been reserved in  
6 the sale order, it is well settled that the bankruptcy court has  
7 post-dismissal jurisdiction to interpret and enforce its orders.  
8 The dismissal of the bankruptcy case moots only issues involving  
9 a debtor's reorganization or liquidation. A dismissal does not  
10 moot issues which are ancillary or collateral to the bankruptcy  
11 case. In re Universal Farming Indus., 873 F.2d 1334, 1335 (9<sup>th</sup>  
12 Cir. 1989). Ancillary matters include interpretation of prior  
13 orders,<sup>3</sup> actions in aid of the execution or implementation of  
14 judgments,<sup>4</sup> actions to determine the rights to property within  
15 possession of the court,<sup>5</sup> recovery of postpetition attorneys'  
16 fees paid without bankruptcy court approval,<sup>6</sup> and motions for an  
17 award of attorneys' fees.<sup>7</sup>

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19 <sup>3</sup> See Beneficial Trust Deeds v. Franklin (In re  
20 Franklin), 802 F.2d 324, 326 (9<sup>th</sup> Cir. 1986).

21 <sup>4</sup> See Lawson v. Tilem (In re Lawson), 156 B.R. 43, 46  
22 (B.A.P. 9<sup>th</sup> Cir. 1993), *affirmed*, 999 F.2d 543 (9<sup>th</sup> Cir. 1993);  
Jones v. Nat'l Bank of Commerce, 157 F.2d 214, 215 (8<sup>th</sup> Cir.  
1946).

23 <sup>5</sup> See In re Ethington, 150 B.R. 48, 51 (Bankr. D. Idaho  
24 1993); In re Harris, 258 B.R. 8, 11-12 (Bankr. D. Idaho 2000);  
Wesley Medical Center v. Wallace (In re Wallace), 46 B.R. 807  
25 (Bankr. W.D. Mo. 1984).

26 <sup>6</sup> See Willis v. Cruse (In re Samford), 125 B.R. 230, 234  
27 (Bankr. E.D. Mo. 1991).

28 <sup>7</sup> See USA Motel Corp. v. Danning, 521 F.2d 117, 119 (9<sup>th</sup>  
Cir. 1975) ; Dahlquist v. First National Bank in Sioux City (In  
re Dahlquist), 751 F.2d 295, 298 (8<sup>th</sup> Cir. 1985); In re

1 If the court could be convinced to ignore the sale order and  
2 to allow the trustee to distribute the funds without regard to  
3 the rights of liens holders, it would direct the trustee to pay  
4 the funds to the Internal Revenue Service. The Internal Revenue  
5 Service levied on the funds since the dismissal of the case.<sup>8</sup> A  
6 trustee must honor any such levy notwithstanding section  
7 1326(a)(2). See Beam v. IRS (In re Beam), 192 F.3d 941, 944-45  
8 (9<sup>th</sup> Cir. 1999).

9 The court concludes, for the reasons given above, that the  
10 sale order survives the dismissal of the case. Therefore,  
11 payment of the funds in the account to either the debtor because  
12 of the dismissal or to the Internal Revenue Service pursuant to  
13 its post-dismissal levy is inappropriate.<sup>9</sup>

14 Unless the debtor, the Internal Revenue Service, or one of  
15 the other unsatisfied lien holders files an action in this court  
16 within 30 days challenging the extent, validity, or priority of  
17 one or more of the liens identified in Paragraph 10 of the sale  
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19 Ethington, 150 B.R. at 50-51.

20 <sup>8</sup> Comparison of the Notice of Levy to the proof of claim  
21 filed by the Internal Revenue Service reveals that the levy  
22 concerns income taxes for years 1993, 1994, 1996, 1997, 1998, and  
23 1999. With the exception of the taxes demanded for 1998 and 1999  
24 (which total \$38,831.36), these taxes were part of the Internal  
25 Revenue Service's secured proof of claim. Thus, the Notice of  
Levy is attempting to collect \$131,832.06 in taxes that are  
secured by tax liens. These tax liens are identified in  
Paragraph 10 of the sale order.

26 <sup>9</sup> The Internal Revenue Service advanced alternative  
27 positions. It preferred that the funds be distributed to the  
28 lien holders in the order of their respective priorities. If the  
court was unwilling to do this, the Internal Revenue Service  
demanded the funds pursuant to its post-dismissal levy. The  
court is ordering the former.

1 order, the trustee is instructed to distribute the funds to those  
2 lien holders in the order their respective liens were recorded.  
3 If all liens are paid in full, the surplus of funds shall be paid  
4 to the debtor and his spouse. If an action is filed, the trustee  
5 shall continue to hold the funds in the account pending a  
6 judgment in the action.

7 The parties will note that these instructions are different  
8 than those announced in open court.

9 The trustee shall lodge a conforming order. Once it is  
10 entered, he shall serve the order, this Memorandum, and a copy of  
11 the sale order on the debtor, counsel for the Internal Revenue  
12 Service, and all of the lien holders identified in Paragraph 10  
13 of the sale order. The 30-day period to file the action  
14 described above shall begin to run 3 days after service of these  
15 documents.

16 Dated: *27 March 2002*

17 By the Court

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19 \_\_\_\_\_  
20 Michael S. McManus, Chief Judge  
21 United States Bankruptcy Court

1 **CERTIFICATE OF MAILING**

2 I, Susan C. Cox, in the performance of my duties as a  
3 judicial assistant to the Honorable Michael S. McManus, mailed by  
4 ordinary mail to each of the parties named below a true copy of  
5 the attached document.

6 Jan Johnson  
7 PO Box 1708  
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10 Norma J. Schrock  
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13 PO Box 683  
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14 Office of the US Trustee  
15 501 I St, Ste 7-500  
16 Sacramento, CA 95814

16 Dated: March 27, 2002

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18 \_\_\_\_\_  
19 Susan C. Cox  
20 Judicial Assistant to Judge McManus  
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