

**United States Bankruptcy Court
Western District of Wisconsin**

Cite as: [Unpublished]

In re Tri-State Homes, Inc., Debtor
Bankruptcy Case No. 82-00488-7

United States Bankruptcy Court
W.D. Wisconsin, Eau Claire Division

December 31, 1986

Robert E. Hackett, Jr., for debtor.
David E. McDonald, Jr., for The First National Bank of Ironwood.
Thomas Mallery, for The Northern Highlands State Bank.

Thomas S. Utschig, United States Bankruptcy Judge.

**MEMORANDUM OPINION, FINDINGS OF FACT,
AND CONCLUSIONS OF LAW**

The attorney for the debtor Tri-State Homes, Inc., Robert E. Hackett, Jr. (applicant), has filed an application for allowance of fees in this bankruptcy case. The applicant argues that such an allowance constitutes an administrative expense of the estate and requests that said fees be paid out of auction proceeds. The First National Bank of Ironwood (FNB) appears by David E. McDonald, Jr., and objects to the application. The Northern Highlands State Bank (NHSB) appears by Thomas Mallery and has filed written objection to the application. The debtor by Ed Alvey, its president, has also filed an objection to the application. A hearing was held in this matter on September 17, 1986, and the parties have submitted the issues to the court for determination through briefs.

The debtor filed for relief under Chapter 11 of the Bankruptcy Code on March 24, 1982. FNB possessed at that time a valid perfected security interest in virtually all of the assets of the debtor. NHSB also possessed a security interest in a substantial portion of the debtor's assets. A Chapter 11 plan of reorganization was confirmed on November 26, 1984. It subsequently became apparent that the debtor could not effectuate its plan of reorganization. FNB filed a motion for relief from stay in the Chapter 11 proceedings on February 19, 1986. An order was entered on March 18, 1986, by the Honorable Robert D. Martin allowing the debtor ten days to convert to Chapter 7 of the Bankruptcy Code or the motion for relief from stay would be granted. The case was converted to a case under Chapter 7 of the Bankruptcy Code on March 21, 1986, and a trustee was appointed to administer the estate on March 25, 1986.

The trustee found it difficult to determine the exact value of the debtor's assets and filed a motion with the court on June 11, 1986, requesting that an auction sale of the assets of the debtor be held. The trustee also requested that an appraisal not be required as the advertised auction would be the best indication of the fair market value of the assets. FNB believed that an auction would be the most efficient method

of liquidating the assets and agreed to the sale. The court granted the trustee's motion by order of the Honorable William H. Frawley dated June 12, 1986. The applicant did not enter into an agreement with the secured creditors which would allow payment of attorney fees out of auction proceeds.

A nationally advertised auction was held on July 16, 1986. The proceeds of the auction amounted to \$296,718.50. The auctioneer's fees and expenses were \$20,077.30 and \$19,728.46 respectively. The trustee also requested fees from the sale in accordance with § 326 in the amount of \$9,081.56. The auctioneer's fees and expenses and the trustee's fees were approved and ordered payable by court order of September 18, 1986. Certain real estate was offered for sale at the auction on which no bids were received. Subsequent to the auction, on August 25, 1986, FNB was granted relief from stay to foreclose its mortgage on this real estate.

The applicant alleges that at the time the Chapter 11 plan was confirmed, attorney's fees and expenses were allowed in the amounts of \$59,457.50 and \$5,628.83 respectively. Of these amounts, apparently only \$42,100.00 was paid and \$22,986.33 still remains unpaid. The applicant now seeks an additional \$34,500.00 for attorney fees and \$5,501.92 in expenses. Hence, the applicant requests a total of \$62,988.25. The applicant argues that this amount should be allowed as an administrative expense and paid out of the proceeds of the auction. FNB held a security interest in the property sold at the auction and takes a position quite contrary to that of the applicant. FNB is very adamant in its position; this is due primarily to the fact that FNB is apparently undersecured in this bankruptcy case.

The applicant's argument is somewhat confusing and is as follows: He argues that his fees constitute an administrative expense under § 503(b) of the Bankruptcy Code. Administrative expenses are priority expenses under § 507(a). Under § 726 the § 507 priorities receive first distribution from the property of the estate.

The applicant next points out that § 507(b) provides a super priority for claims from the use, sale, or lease of property under § 363. The applicant then asserts that property was sold pursuant to § 363 and FNB did not object nor did it apply for a super priority pursuant to § 507. Hence, the applicant argues that FNB is not entitled to a super priority. The applicant then concludes that since FNB does not have a super priority under § 507(b), the applicant is entitled to first distribution of the auction proceeds pursuant to § 726(a)(I).

The applicant's conclusion is patently erroneous. The applicant fails to recognize the distinction between secured and unsecured property. All of the property sold at the auction was subject to valid security interests. The security interests attached to the proceeds of the auction pursuant to § 552(b). The security interests in the proceeds were not avoided and still remain valid. It further appears that there are insufficient assets in the estate to pay the full amount of the secured claims.

Property that is subject to a valid security interest, or proceeds of such property, must be disposed of in accordance with § 725 and Bankruptcy Rule 6007 prior to the final distribution of § 726. The property remaining in the estate after the § 725 disposition is then distributed in accordance with § 726. At present, all of the assets of the estate are subject to security interests. It is unlikely that there is any equity in the remaining property above the claims of the secured creditors. The applicant is not entitled to the proceeds of secured property to satisfy his claim against the estate. Should the foreclosure yield sufficient proceeds to pay off the secured creditors, then any excess may be available for distribution under § 726. However, it is doubtful that any such equity exists and it is likely that the real estate will be abandoned in the

near future.

In conclusion, the auction proceeds are subject to valid security interests. The applicant cannot receive distribution from the auction proceeds. The auction proceeds are apparently the only assets of any significance in the bankruptcy estate. The applicant may very well have a valid administrative claim against the estate in accordance with § 503. However, the estate does not have any assets available for distribution toward such claims. Should unsecured assets later become available, they would be distributed pursuant to § 726.

This opinion shall constitute findings of fact and conclusions of law in accordance with Bankruptcy Rule 7052.