

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF INDIANA
SOUTH BEND DIVISION

IN THE MATTER OF)
)
SECURITIES INVESTOR PROTECTION) CASE NO. 01-3012 HCD
CORPORATION,)
PLAINTIFF-APPLICANT,)
vs.)
)
SPECTRUM INVESTMENT SERVICES, INC.,)
DEFENDANT.)

)
SECURITIES INVESTOR PROTECTION)
CORPORATION, AS TRUSTEE FOR)
SPECTRUM INVESTMENT SERVICES, INC.,)
PLAINTIFF,)
vs.) PROC. NO. 01-3045
)
MARY L. SANDERS,)
DEFENDANT.)

Appearances:

Patricia Primmer, Esq., attorney for plaintiff, May Oberfell & Lorber, 300 North Michigan, South Bend, Indiana 46601; and

Joseph Bradley, Esq., attorney for claimant Samuel Mercantini, 105 East Jefferson Boulevard, Suite 512, South Bend Indiana, 46601.

MEMORANDUM OF DECISION

At South Bend, Indiana, on March 4, 2004.

On July 23, 2003, the court granted Samuel Mercantini's Motion for Summary Judgment on his Request for Allowance and Payment of Administrative Expense. On December 15, 2003, the court conducted an evidentiary hearing on the amount of administrative rent allowed to the creditor. After hearing the witnesses and reviewing the evidence presented, the court took the matter under advisement.

Jurisdiction

Pursuant to 28 U.S.C. § 157(a) and Northern District of Indiana Local Rule 200.1, the United States District Court for the Northern District of Indiana has referred this case to this court for hearing and determination. After reviewing the record, the court determines that the matter before it is a core proceeding within the meaning of § 157(b)(2)(B) over which the court has jurisdiction pursuant to 28 U.S.C. §§ 157(b)(1) and 1334. This entry shall serve as findings of fact and conclusions of law as required by Federal Rule of Civil Procedure 52, made applicable in this proceeding by Federal Rules of Bankruptcy Procedure 7052 and 9014. Any conclusion of law more properly classified as a factual finding shall be deemed a fact, and any finding of fact more properly classified as a legal conclusion shall be deemed a conclusion of law.

Background

The plaintiff Securities Investor Protection Corporation (“SIPC”) was appointed Trustee for the liquidation of Spectrum Investment Services, Inc. under the Securities Investor Protection Act, 15 U.S.C. § 78aaa *et seq.* (“SIPA”). The Spectrum assets to be liquidated included the real and personal property of Spectrum, located at 410 Lincolnway East, Mishawaka, Indiana. The creditor Samuel Mercantini had sold the Mishawaka property by land contract to the defendant Mary L. Sanders, President of Spectrum, on November 7, 1995, for \$240,000. Mercantini received payments from Sanders until December 2000, when she disappeared. SIPC, as Trustee, moved into the Spectrum premises on or about January 17, 2001. Mercantini asserted that he had received no payment from SIPC during its occupancy. He claimed entitlement to the fair rental value of those premises for the period that SIPC utilized the real estate, from January 17, 2001, through May 17, 2002. He contended that the reasonable fair market rental value of the premises SIPC occupied was \$10.00 per square foot for the basement and first floors, plus expenses of taxes, insurance and utilities. His claim for administrative expense included \$53,328.00 in fair market rent and \$11,203.80 in expenses.

The position taken by SIPC is that the appropriate time period for the rental is January through August 2001. It explained that the personal property of Spectrum was sold and removed from the real estate by August 2001, and SIPC no longer was in the building. SIPC also apprised the court that it had offered to pay Mercantini the same amount Sanders had paid monthly under the land contract; he had countered with a request of \$10 a square foot. In the view of SIPC, the \$10 amount was excessive and inappropriate. An appraiser of the property had told SIPC that the rental amount should be \$4.80 a square foot. It asked the court to consider both the fair market value of the rent and the time period for which rent must be paid.

The Mishawaka real estate at issue is an 1860 restored Victorian brick building on the St. Joseph River. It is a two-story building with a finished basement. A business, Environmental Solutions, rented the second floor of the building, which measured 1200 square feet. It paid \$600 a month in rent and covered its own utilities. SIPC occupied the ground floor and the basement, a total of 4,406 square feet of office space. The basement was improved and refinished as office space; it is not as elegant as the first floor offices, however, which are decorated with elegant wall paper and chandeliers. Mercantini, the legal owner of the real estate, testified at the hearing that the building meets the historical preservation standards but is not on the Historical Register. He stated that SIPC paid no rent and covered the utilities for only the first month. Mercantini proffered a list of the bills – for utilities, insurances, taxes, and other expenses – that he paid during the period from February 2001 through May 2002. He has not been reimbursed for those bills, which total \$11,536.64, he stated.

Two experts testified concerning the fair rental value of the Mishawaka property. The creditor's expert witness was Richard Doolittle, a real estate broker who has been a partner and principal broker at Grubb & Ellis, Cressy & Everett, since 1984. He manages the brokerage operation of the company and supervises commercial rentals. A graduate of Indiana University, he has been a licensed realtor since 1971, with a real estate office in downtown Mishawaka from 1971 through 1984. He is the past president of the Mishawaka Business Association, owns commercial real estate in Mishawaka, and has lived in the downtown area, as well.

Doolittle testified that he is familiar with 410 Lincolnway East and with the real estate in downtown Mishawaka generally. Doolittle had examined the real estate, viewing the property and assessing its general condition for leasing. He then compared in detail eight other properties in the market place, three of which were in downtown Mishawaka. He described their locations, their square footage, their rents, what costs are included in the rent, and which buildings had closely held leases. Based on his examination of the building and his first-hand knowledge of downtown Mishawaka, he gave his opinion that the lease value of the Mishawaka real estate was between \$6.50 and \$7.25 per square foot, with the tenant paying all the costs for utilities, taxes, janitorial services, grounds fees, and other expenses. He stated that such a value was a fair range for the rent during the period from January 2001 through May 2002. He explained that his figures were an average of the values of each of the two floors available for commercial use. He also gave two other valuation opinions. First, he stated that a gross lease, for which the landlord is responsible for the taxes and other costs of maintaining an older building, would be around \$10 a square foot or more. Second, he testified that the rental of that property if it was used only for storage would be much lower, but he made clear that the building was not meant to be used for commercial storage.

The second expert to testify, on behalf of SIPC, was real estate appraiser and broker Bernard F. Diedrich. He works at the Appraisal Group, Inc., as a real estate consultant and appraiser, specializing in commercial, investment and industrial appraising. Having earned a master's degree and having taken numerous realtor and appraiser courses, Diedrich has been licensed as a broker since 1970 and as a Certified General Appraiser since 1991. He appraised the Mishawaka property on July 9, 2001. He saw the premises and reviewed comparable rented office space in Mishawaka which were of similar age, location, and condition. Based on his review of the comparables, he formed an opinion, using the direct sales comparison approach, that the fair rental of this property, at that time, would be \$4.80 per square foot plus expenses. He also formed the opinion that the value of the property itself, as of July 9, 2001, was \$270,000. He believed that a rental of \$10.00

a square foot, plus costs, was excessive. Assuming that the building was used for commercial office space, he opined that the reasonable rental value should be \$2,333 per month for the entire building. The \$600 rental paid by the subtenant Environmental Solutions should be subtracted, he stated.

On cross examination, Diedrich acknowledged that he had appraised the property in 1985 for Mercantini. In that appraisal, he valued the first floor at \$10 a square foot, the second floor at \$8 a square foot, and the basement at \$6 a square foot, with the tenants responsible for their pro rata share of the expenses. The court overruled the Trustee's objection to the admission of evidence concerning the 1985 appraisal. It found that an assessment of the same building by the same appraiser was relevant and that the sixteen-year passage of time went to the weight of the evidence. Diedrich stated that the 1985 valuation of the building, based on those figures, was \$246,900. The value as of January 2001 was around \$270,000. He further testified that no one would look at a 1985 appraisal to determine what would be fair appraisal in 2001. In his opinion, the 1985 appraisal had no relevance today.

When Mercantini again took the stand, he conceded that SIPC offered him the same monthly payments that the defendant Mary Lou Sanders would have paid to him. He noted that the amount remaining on the land contract was \$214,236.93 and, with accrued interest, the total owed was \$245,000. He stated that the present value of the property, in his estimation as the owner, was \$250,000 to \$260,000. He claimed that there was no equity left in the property: If he sold it for \$245,000, the expenses of the sale would use whatever equity was left in the property. He acknowledged that SIPC did not object to his motion for relief from the stay. However, he was required to go to state court to get possession of the property because SIPC had refused to give him access to the building without a state court order. Mercantini admitted that the accepted remedy, after receiving relief from the stay, was to turn to state court for relief, but stated that SIPC could have abandoned the premises to him without a state court order.

Discussion

Section 503(b)(1)(A) of the Bankruptcy Code authorizes payment of actual, necessary costs of preserving the estate. The SIPA incorporates § 503 of the Bankruptcy Code and requires that a SIPA proceeding be treated like a chapter 7 bankruptcy case. *See In re Lloyd Secs., Inc.*, 75 F.3d 853, (3d Cir. 1996). The statutory authority under SIPA for advancing administrative expenses to the trustee is found at 15 U.S.C. § 78fff-3(b).¹ *See SIPC v. Ambassador Church Finance/Development Group, Inc.*, 788 F.2d 1208, 1212 (6th Cir.), *cert. denied*, 479 U.S. 850 (1986). Under the SIPA, the SIPC fund is required to pay administrative expenses incurred in the liquidation “to the extent that the debtor is unable to provide reimbursement.” *SIPC v. BDO Seidman, L.L.P.*, 222 F.3d 63, 71 (2d Cir. 2000) (citing 15 U.S.C. § 78fff-3(b)). “In light of the fact that Congress has mandated that SIPC shall advance administrative costs and expenses to the extent the debtor cannot, the trustee has a heavy burden in making an argument in equity contrary to what the statute provides.” *In re G.V. Lewellyn & Co., Inc.*, 140 B.R. 502, 508 (Bankr. S.D. Iowa 1992). The trustee has been held liable for administrative rent from the date of bankruptcy until the date the trustee vacated the premises completely. *See In re Buttonwood Secs., Inc.*, 349 F. Supp. 273, 278 (S.D Calif. 1972) (citing cases).

In its Memorandum of Decision of July 23, 2003, the court determined that Mercantini’s claim for administrative rent was allowed under § 503(b)(1)(A).

It is the finding of this court that Mercantini, who provided the Spectrum property for the Trustee’s use and control for sixteen months, should be paid a reasonable rent for its possession of the Mishawaka real estate.

R. 41 at 11-12 (citing cases). The court set a separate hearing to determine the reasonable amount of administrative rent.

¹ 15 U.S.C. § 78fff-3(b) provides that “SIPC shall advance to the trustee — . . . (2) to the extent the general estate of the debtor is not sufficient to pay any and all costs and expenses of administration of the estate of the debtor and of the liquidation proceeding, the amount of such costs and expenses.”

The Trustee asks first that the court find that SIPC occupied the Spectrum premises from January 17, 2001, only through August 2001, rather than through May 17, 2002. It explained that the personal property of Spectrum was sold and removed from the real property by August 25, 2001, and that SIPC no longer was in the building after that date. The court finds that SIPC did not abandon the Mishawaka property to Mercantini in August 2001, even if it had removed the Spectrum personal property from the real estate. It maintained continuous control and possession of the property and denied Mercantini access to it until after he was granted relief from the automatic stay and had obtained a Judgment for Possession and Cancellation of Land Contract in the St. Joseph Circuit Court. Only then, in May 2002, did SIPC turn over control of the real estate to Mercantini. The court having found, in its Memorandum of Decision of July 23, 2003, that the Trustee had use and control of the Spectrum property for sixteen (16) months, it now finds, after consideration of the Trustee's arguments and evidence, that the possession time is *res judicata* and that SIPC incurred an administrative expense for its rental value for sixteen months.

The court next considers the rental value of the property as commercial office space in downtown Mishawaka. It has before it the opinions of reasonable fair market rental rates given by two highly reputable, seasoned real estate experts. SIPC's expert, Mr. Diedrich, was a Certified General Appraiser who testified that, in his expert opinion, on July 9, 2001, the rental value of the Spectrum property was \$4.80 per square foot. Mercantini's expert, Mr. Doolittle, was a licensed real estate broker who testified that, in his expert opinion, between January 2001 and May 2002, the rental value of the Spectrum property was between \$6.50 and \$7.25 per square foot. Both experts were credible and informative. Mr. Diedrich, in his report, proffered four rental comparables and stated that the Spectrum property was "most similar to comparable 4 in use and size." Pl. Ex. F at 81. At the hearing, however, he discussed the sales comparables rather than the rental comparables, and focused on the appraised market value of the building. Mr. Doolittle, in his report, proffered eight leased comparables and fourteen sold comparables. He stated expressly that his report was "intended to reflect Property

Value as it relates to the local and regional real estate market,” and was not an appraisal. Cr. Ex. 2 at 2. At the hearing, Mr. Doolittle discussed the comparables used to obtain the lease value of the Spectrum building. He compared the location of various comparable properties, their square footage, and their lease rates. He pointed out that some lease rates include utilities, taxes, insurance, janitorial costs and grounds care, and others leave those costs to the tenant. He noted two closely held leases. The court was provided much more information about the comparisons of various downtown office buildings in Mishawaka and South Bend from Mr. Doolittle than from Mr. Diedrich.

The court finds that Mr. Doolittle’s more detailed information about the Lincolnway building and the other comparable leased properties was persuasive. Mr. Doolittle was personally familiar with the leased office real estate being valued and had a personal interest in downtown Mishawaka business real estate. The court found that his commercial knowledge of the Mishawaka downtown area gave added insight and credibility to his testimony and gave him the edge as an expert.

The court finds that the reasonable fair market rental value for the space of 4,406 square feet (the space occupied by SIPC) in the building at 410 Lincolnway East is \$6.50 per square foot. The monthly rent therefore is \$2,386.58, and the total rent for the sixteen months in which SIPC used and possessed the Mishawaka property is \$38,185.28. The court also finds that part of the costs and expenses of administration of this SIPC estate are the reimbursable expenses of utilities, taxes, and building upkeep, which Mercantini listed as \$11,536.64. Congress requires, by statute, that the administrative rent and expenses, in the total sum of \$49,721.92 in this case, are to be paid by SIPC to the extent the debtor cannot pay. *See* 15 U.S.C. 78fff-3(b)(2). No one challenges the fact that Mary Lou Sanders, the debtor’s president and owner, has disappeared with investor funds and that the debtor Spectrum is unable to pay. The court therefore determines that the administrative rent and expenses of the claimant Samuel Mercantini, in the total amount of \$49,721.92, shall be advanced to the claimant by the trustee.

Conclusion

After considering all the evidence and arguments of counsel, the court now grants the Request for Allowance and Payment of Administrative Expense of Samuel Mercantini in the amount of \$49,721.92. It finds that the trustee of SIPC is liable for the reasonable value of SIPC's use and occupancy of the real estate at 410 Lincolnway East in Mishawaka, Indiana, for the time period from January 17, 2001, through May 17, 2002. The court approves Samuel Mercantini's claim for administrative rent in the amount of \$38,185.28 and for reimbursable expenses in the amount of \$11,536.64.

Therefore, it is ordered that the Trustee remit to Samuel Mercantini the sum of \$38,185.28 for administrative rent and \$11,536.64 in expenses from January 17, 2001 through May 17, 2002.

SO ORDERED.

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HARRY C. DEES, JR., CHIEF JUDGE
UNITED STATES BANKRUPTCY COURT