

FOR PUBLICATION



**UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA**

In re

ROBERT W SWEITZER,

Debtor.

Case No. LA 04-18590 TA

Chapter 7

**MEMORANDUM OPINION RE DEBTOR'S
MOTION TO AVOID LIEN**

This case requires a determination of the meaning of “gross annual income” as used in California’s statute regarding homesteads for debtors over 55 years of age.

Debtor filed a motion under 11 U.S.C. 522(f)(1) to avoid the judicial lien of Liner, Yankelevitz, Sunshine & Regenstreif, LLP (“Liner”). Liner timely filed an opposition and request for a hearing on the motion. Debtor in his motion alleges that Liner’s lien impairs his homestead exemption, which Debtor claims is \$150,000 pursuant to California Code of Civil Procedure § 704.730(a)(3)(C), which provides:

“(a) The amount of the homestead exemption is one of the following:...(3) One hundred fifty thousand dollars (\$150,000) if the judgment debtor or spouse of the judgment debtor who resides in the homestead is at the time of the attempted sale of the homestead any one of the following:...(C) A person 55 years of age or older with a gross annual income of not more than

1 fifteen thousand dollars (\$15,000) or, if the judgment debtor is married, a gross annual income,
2 including the gross annual income of the judgment debtor's spouse, of not more than twenty
3 thousand dollars (\$20,000) and the sale is an involuntary sale.”

4 Liner argues that Debtor is only eligible for a \$75,000 exemption because he does not meet the income
5 limitation in Cal. Civ. Proc. § 704.730(a)(3)(C) for the \$150,000 exemption, and therefore Liner’s lien
6 does not impair Debtor’s homestead exemption. The Court agrees with Liner, and for the reasons
7 discussed below, Debtor’s motion is denied.

8 Debtor listed the real property commonly known as 420 Middlebury Court, Claremont,
9 California (the “Property”) on his Schedule A at a value of \$350,000, and claimed an exemption of
10 \$150,000 therein under Cal. Civ. Proc. § 704.730(a)(3)(c) on his Schedule C. In his schedules and
11 motion, Debtor asserts that a senior lien of \$194,763.09 encumbered the Property, with the Liner lien,
12 in the amount of \$92,157.36, in second position. No timely objection to the exemption was filed. The
13 net proceeds of the post-petition sale of the Property in the sum of \$84,628 were deposited with the
14 Bankruptcy Court by stipulated order entered May 16, 2005, with the rights of the parties to the
15 proceeds to await determination by the Court on Debtor’s motion. It appears from the record that the
16 amount deposited into the Court is net of the undisputed amount of homestead, i.e. \$75,000, and that
17 the first lienholder does not continue to claim any part of the proceeds. There is a reference to an
18 arithmetic disagreement between Debtor and Liner about the amount of the first lien. The Court
19 assumes that the first lien has already been paid in full, but if there remains any claim of the first
20 lienholder, the parties will do the arithmetic regarding dividing the remaining proceeds after
21 satisfaction of the first mortgage and payment of the undisputed portion of the exemption (\$75,000)
22 in accordance with this decision.

23 The main issue is whether Debtor is entitled to a homestead exemption in the amount of only
24 \$75,000, or in the amount of \$150,000. Liner argues that the highest possible exemption amount in
25 any case would be \$125,000 as this was the highest amount allowed under Cal. Civ. Proc. § 704.730
26 in December 2001, the date of levy of the writ of attachment to which Liner’s judgment lien then
27 relates back under state law. Cal. Civ. Proc. § 704.965. Since the statute was not amended to increase
28 the exemption until 2003, the claim to a \$150,000 exemption is wrong under any analysis. Debtor

1 does not refute this argument.

2 In order to determine the amount of Debtor's homestead exemption, this Court must determine
3 whether Debtor is entitled to offset his share of losses of the S corporation, Enterprise Ventures, Inc.,
4 reported as \$35,775 in his 2004 tax return. If Debtor is entitled to offset his share of these losses in
5 determining "gross annual income" under Cal. Civ. Proc. § 704.730 then Debtor had no "gross annual
6 income" but only a net loss for 2004 and, presumably, would qualify for the enhanced exemption.
7 This Court, however, believes Debtor should not be entitled to offset his share of the S corporation
8 losses, and only the lesser exemption of \$75,000 is appropriate in this case.

9 Although no objection to Debtor's claimed exemption was received, this Court must still
10 consider the exemption claim on its legal merits. Although exemptions are determined as claimed by
11 the debtor absent timely objection, even if the exemption is not otherwise supported in law (see *Taylor*
12 *v. Freeland & Kronz*, 503 U.S. 638, 112 S.Ct. 1644 (1992)), the Ninth Circuit Bankruptcy Appellate
13 Panel has determined that this does not govern a lien holder's ability to defend in a lien avoidance
14 action, such as the case at bar. *Morgan v. Federal Deposit Insurance Corp. (In re Morgan)*, 149 B.R.
15 147, 152 (9th Cir. BAP 1993).

16 Debtor argues that he qualifies for the larger exemption found at Cal. Civ. Proc. §
17 704.730(a)(3)(c) because, as of the date of the petition, he was over 55 and he and his spouse had a
18 "gross annual income" of less than \$20,000. Debtor's declaration, which was filed with the motion,
19 provides: "On the filing date, I was married and over the age of fifty-five (55) years. In the calendar
20 year 2004 up to the filing date, the gross income for both my spouse and I was less than \$20,000..."
21 However, from Liner's opposition and Debtor's own 2004 tax returns, it appears that wages paid in
22 2004 alone were at least \$30,008. A twelve month period is clearly the appropriate measure for
23 determining a Cal. Civ. Proc. § 704.730(a)(3)(c) exemption, and Debtor cannot rely on the
24 happenstance of a filing early in the calendar year to enhance his exemption. *In re Goldman*, 70 F.3d
25 1028, 1029 (9th Cir. 1995). The parties seem to assume that 2004 is the appropriate twelve month
26 period, even though most of this period was post-petition. Since the evidence submitted by Liner and
27 extrapolation from Schedule I income suggest that the income earned in earlier periods was probably
28 even higher, which twelve month period is used is not material to the outcome of this motion. Since

1 the parties focused on 2004, so will the Court.

2 Unfortunately, there is very little authority interpreting “gross annual income” as that term is
3 used in Cal. Civ. Proc. § 704.730. Debtor cites to *Shelly v. Kendall (In re Shelly)*, 184 B.R. 356, 358
4 (9th Cir. BAP 1995) *affd.* 109 F.3d 639 (9th Cir. 1997). The debtors in *Shelly* owned a retail store. The
5 chapter 7 trustee brought a motion to limit the debtors homestead exemption because he claimed their
6 “gross income” based on gross receipts exceeded \$20,000. *Id.* at 357. The court held that the debtors’
7 gross income would be the income from their sole proprietorship reduced by the expenses of that
8 company. The court reasoned that when a person owns a business, gross receipts are not the correct
9 measure of income. The court felt that to hold otherwise would discriminate against sole proprietors.
10 *Id.* at 360. However, *Shelly* is distinguishable and its holding does not compel a decision in favor of
11 Debtor on these facts. Debtor seems to argue that *Shelley* stands for the proposition that “gross annual
12 income” is the functional equivalent of “adjusted gross income” as used for computing taxes, i.e.,
13 wages, salaries, etc. or other income *less* the variety of possible deductions appearing at lines 12-21
14 of the IRS 1040 form, including NOL carryover, and losses on partnerships and S corporations. This
15 argument is a vast overreading of *Shelley*. Indeed, the *Shelley* court held that “gross income” was a
16 malleable concept and “should not convey the same definite and inflexible significance under all
17 circumstances and wherever used. It is a term whose construction and meaning depends on the
18 context of the subject matter.” (citations omitted) *Id.* at 359. *See also, In re Kaura*, 211 F.3d 1273
19 (9th Cir. 2000); *In re Faber*, 78 B.R. 934, 935 (Bankr. S.D. Iowa 1987).

20 In *Shelly*, it made perfect sense that “gross annual income” should mean gross receipts *less*
21 costs of goods sold because the debtors operated a retail merchandising establishment conducted as
22 a sole proprietorship. Certainly in such a context, gross receipts are not meaningful in determining
23 “income” unless cost of goods sold is first deducted. The debtor who spends more in a year to acquire
24 the inventory than he realizes on sale has no “income.” But, the court notes that in other contexts
25 “gross income” has been defined very differently, such as in a service business other than mining,
26 manufacturing and merchandising, where gross income equals gross receipts. *See, e.g. Guy F.*
27 *Atkinson Co. Of California and Subsidiaries v. Commissioner of Internal Revenue*, 82 T.C. 275, 298
28 (1984), citing *Hahn v. Commissioner*, 30 T.C. 195 (1958) *affd.* 271 F.2d 739 (5th Cir. 1959).

1 Moreover, in the *Hahn* case, where the taxpayer was engaged in operating a blacksmith and welding
2 shop, “gross income” was determined on a gross receipts basis, without deduction of cost of goods
3 sold, because the taxpayer was “*primarily* engaged in repairing, plows, trailers...” *Hahn, supra* at 196-
4 197 (emphasis added). Similarly, In *In re Faber, supra*, the debtor was not permitted to deduct “costs
5 of operation” in the trucking segment of his business to reduce his gross non-farming income to less
6 than half of his annual income so as to qualify as a “family farmer” under Chapter 12. The *Faber*
7 court held the trucking income was primarily from the rendering of services and, therefore, deduction
8 of the expenses from gross receipts was improper in determining “gross income” under what is now
9 11 U.S.C. § 101(18)(A). Therefore, it is appropriate to determine the *primary* source of Debtor’s
10 income, and, if it was from rendering of services, deductions from gross receipts should not be
11 allowed.

12 The parties do not provide the Court with any evidence explaining what was the business of
13 the S Corporation, Enterprise Ventures, Inc. or whether Debtor’s share of its 2004 losses comprised
14 a majority or minority of Debtor’s gainful efforts on a time-spent basis for that year, although the
15 Court notes from the California 2004 return that Debtor was only a 15% owner of the stock. There
16 is very little evidence in the record, but what appears (such as W-2 forms) persuades the Court that
17 Debtor’s gross annual income was primarily from services he rendered to Pepperdine University and
18 Claremont College as a consultant or professor.

19 Although there is little guidance from California case law or legislative history citing Cal. Civ.
20 Proc. § 704.730, there are other sources which may provide guidance and which persuade the Court
21 that deduction of costs should not diminish gross receipts in determining “gross annual income” in our
22 context. For example, California Family Code Section 4058, governing child support obligations,
23 defines “annual gross income” in a variety of ways but makes a distinction between income based on
24 commissions, salaries and royalties under subsection (a)(1) from “income from the proprietorship of
25 a business, such as gross receipts from the business reduced by expenditures required for the operation
26 of the business...” under subsection (a)(2). Moreover, the statute has been interpreted to exclude
27 unrealized appreciation of assets such as equity in a parent’s residence, in the definition of “annual
28 gross income.” See e.g. *In re Marriage of Henry*, 126 CA. 4th 111, 119 (2005). Clearly, “annual

1 NOTICE OF ENTRY OF JUDGMENT OR ORDER
2 AND CERTIFICATE OF MAILING
3

4 TO ALL PARTIES IN INTEREST LISTED BELOW:

5 You are hereby notified that a judgment or order entitled: MEMORANDUM O RE DEBTOR'S
6 MOTION TO AVOID LIEN was entered on 10-13-05.

7
8 I hereby certify that I mailed a true copy of the order or judgment to the persons
9 and entities listed below on 10-13-05.

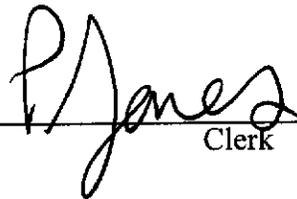
10
11 David A. Tilem
12 Brian D. Wirsching
13 Law Offices of David A. Tilem
14 500 North Brand Blvd., Suite 460
15 Glendale, California 91203

16 Leslie A. Cohen
17 Enid M. Colson
18 Liner Yankelevitz Sunshine & Regenstreif LLP
19 1100 Glendon Avenue, 14th Floor
20 Los Angeles, California 90024

21 David A. Gill
22 Chapter 7 Trustee
23 2029 Century Park East, Third Floor
24 Los Angeles, California 90067

25 DATED 10-13-05

26
27
28
By _____


Clerk