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# NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT  
CENTRAL DISTRICT OF CALIFORNIA  
NORTHERN DIVISION

In re:	)	Case No. 9:15-bk-10528-PC
	)	
DOROTHY HANNAH HAMILBURG,	)	Chapter 11
	)	
	)	<b>MEMORANDUM DECISION</b>
	)	
	)	Date: July 25, 2016
	)	Time: 10:00 a.m.
	)	Place: United States Bankruptcy Court
	)	Courtroom # 201
Debtor.	)	1415 State Street
	)	Santa Barbara, CA 93101

This matter comes before the court on an objection by Dorothy Hannah Hamilburg (“Debtor”) to Claim # 15 filed by Donato Errico (“Errico”). The court, having considered the pleadings, evidentiary record, and argument of counsel, will allow Errico’s Claim # 15 as an unsecured non-priority claim in the amount of \$3,793,411, subject to adjudication of Debtor’s remaining defenses to Errico’s the claim,<sup>1</sup> based upon the following findings of fact and

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<sup>1</sup> See Exhibit 2, Debtor’s Motion Objecting to Donato Errico’s Proof of Claim (Claim No. 15) (“Debtor’s Claim Objection”) [Dkt. # 282], at 8: fn. # 1.

conclusions of law made pursuant to F.R.Civ.P. 52(a)(1),<sup>2</sup> as incorporated into FRBP 7052 and applied to contested matters in bankruptcy cases.

### I. STATEMENT OF FACTS

On March 16, 2015, Debtor filed her voluntary petition under chapter 11 of the Code in the above referenced case. Prior to the petition date, Errico had filed a complaint against Debtor in Case No. SC123821, Errico v. Hamilburg, in the Superior Court of California, County of Los Angeles, seeking damages for an alleged breach of a Remainder Interest Purchase Agreement between the parties dated February 19, 2015 (the “Errico Agreement”), specific performance of the Errico Agreement, and a declaratory judgment quieting title to the real property and improvements at 28926 Cliffside Drive, Malibu, California (the “Malibu Property”).<sup>3</sup> In her Schedule F, Debtor listed Errico as the holder of a contingent, disputed and unliquidated unsecured non-priority claim for damages for alleged breach of contract in an unknown amount.

On May 7, 2015, Debtor served a notice of the court’s deadline of June 16, 2015, to file a proof of claim in the case. On June 15, 2015, Errico filed Claim # 15 asserting an unsecured non-priority claim in the amount of \$9,333,830 based upon a “potential rejection” of the Errico Agreement by the Debtor. On November 18, 2015, Debtor moved for authority to reject the Errico Agreement as an executory contract pursuant to § 365(a). An order granting the motion was entered on December 14, 2015.

On April 4, 2016, Debtor filed a motion objecting to Errico’s Claim # 15 under § 502(b)(1) alleging that Errico’s claim for damages for rejection of the Errico Agreement should be disallowed for the following reasons:

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<sup>2</sup> Unless otherwise indicated, all “Code,” “chapter” and “section” references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1330. “Rule” references are to the Federal Rules of Bankruptcy Procedure (“FRBP”), which make applicable certain Federal Rules of Civil Procedure (“F.R.Civ.P.”). “LBR” references are to the Local Bankruptcy Rules of the United States Bankruptcy Court for the Central District of California (“LBR”).

<sup>3</sup> On March 18, 2015, Errico removed the action from state court pursuant to 28 U.S.C. § 1452(a) and FRBP 9027, and the case is now pending before this court under Adversary No. 9:15-ap-01024-PC (“Errico Litigation”).

- 1 1. Errico's calculation of damages allegedly resulting from Debtor's rejection of the
- 2 Errico Agreement is flawed; and
- 3 2. The Errico Agreement itself is, at best, an "agreement to agree" and is unenforceable
- 4 because it is uncertain and indefinite as to material terms, such as (a) the method of
- 5 calculating, and any limitations on Errico paying, the Debtor's capital gains; (b) the
- 6 nature and scope of the 'statutory duties and other disclosures' the Debtor was
- 7 required to make; and (c) any limitation on Errico paying the cost to trim an
- 8 overhanging tree.

9 Debtor's motion was supported by the declaration of Howard Grobstein ("Grobstein"), a  
10 certified public accountant, who testified that, in his opinion, Errico's damage calculation was  
11 deeply flawed and that Errico was not, in fact, damaged by the Debtor's rejection of the Errico  
12 Agreement.

13 On April 26, 2016, Errico responded in opposition to the Debtor's motion, and requested  
14 an evidentiary hearing on the value of his claim. Errico's response was supported by evidence,  
15 including the declarations of John Hekman ("Hekman"), Howard Muchnick ("Muchnick"), and  
16 Donald Fife ("Fife"). Hekman, an economist and real estate valuation consultant, testified that,  
17 in his opinion, Errico sustained damages attributable to rejection of the Errico Agreement in the  
18 amount of \$9,109,180. Debtor replied on May 13, 2016.

19 Having determined that Debtor had presented evidence sufficient to overcome the prima  
20 facie validity of Errico's Proof of Claim # 15, the court set the matter for an evidentiary hearing  
21 which commenced on July 26, 2016, and concluded on July 27, 2016. After hearing argument  
22 from counsel for Errico and Debtor, the matter was taken under submission.

## 23 II. DISCUSSION

24 This court has jurisdiction over this contested matter pursuant to 28 U.S.C. §§ 157(b) and  
25 1334(b). Debtor's objection to Errico's Claim # 15 is a core proceeding under 28 U.S.C. §  
26 157(b)(2)(A), (B) and (O). Venue is appropriate in this court. 28 U.S.C. § 1409(a).

1 A. Burden of Proof on Objection to Claim.

2 A proof of claim is deemed allowed unless a party in interest objects. 11 U.S.C. § 502(a).  
3 Absent an objection, a proof of claim constitutes prima facie evidence of the validity and amount  
4 of the claim under FRBP 3001(f). Lundell v. Anchor Constr. Specialists, Inc., 223 F.3d 1035,  
5 1039 (9th Cir. 2000). When a creditor has filed a proof of claim that complies with the rules,  
6 thereby giving rise to the presumption of validity, the burden shifts to the objecting party who  
7 must “present evidence to overcome the prima facie case.” U.S. v. Offord Fin., Inc. (In re  
8 Medina), 205 B.R. 216, 222 (9th Cir. BAP 1996). To defeat the claim, the objector must come  
9 forward with sufficient evidence and “show facts tending to defeat the claim by probative force  
10 equal to that of the allegations of the proofs of claim themselves.” Lundell, 223 F.3d at 1039,  
11 quoting In re Holm, 931 F.2d 620, 623 (9th Cir. 1991). “The objector must produce evidence  
12 which, if believed, would refute at least one of the allegations that is essential to the claim's legal  
13 sufficiency.” Lundell, 223 F.3d at 1040, quoting In re Allegheny Int'l, Inc., 954 F.2d 167, 173-  
14 74 (3d Cir. 1992). If the objector produces sufficient evidence to negate one or more of the  
15 sworn facts in the proof of claim, the burden reverts to the claimant to prove the validity of the  
16 claim by a preponderance of the evidence. Ashford v. Consol. Pioneer Mort. (In re Consol.  
17 Pioneer Mort.), 178 B.R. 222, 226 (9th Cir. BAP 1995), aff'd, 91 F.3d 151 (9th Cir. 1996),  
18 quoting Allegheny Int'l, 954 F.2d at 173-74. The ultimate burden of persuasion remains at all  
19 times on the claimant. Lundell, 223 F.3d at 1039; Holm, 931 F.2d at 623.

20 B. Standard for Determining Damages Resulting From Rejection of Executory Contract to  
21 Convey Real Property.

22 Section 365(g)(1) states, in pertinent part, that “the rejection of an executory contract . . .  
23 constitutes a breach of such contract . . . if such contract . . . has not been assumed under this  
24 section or under a plan confirmed under chapter 9, 11, 12, or 13 of this title, immediately before  
25 the date of the filing of the petition.” 11 U.S.C. § 365(g)(1). Paragraph 12.e. of the Errico  
26 Agreement states that the “Agreement shall be interpreted, enforced and governed in accordance  
27 with the laws of the State of California.”<sup>4</sup> Section 3306 of the California Civil Code states:

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28 <sup>4</sup> Exhibit 1, Proof of Claim # 15, at 18.

1 The detriment caused by the breach of an agreement to convey an estate in real  
2 property is deemed to be the price paid, and the expenses properly incurred in  
3 examining the title and preparing the necessary papers, the difference between the  
4 price agreed to be paid and the value of the estate agreed to be conveyed at the  
time of the breach, the expenses properly incurred in preparing to enter upon the  
land, consequential damages according to proof, and interest.

5 Cal.Civ.Code § 3306. “The plaintiff has the burden of proving his damage[, and] [t]he law is  
6 settled that he has the duty to minimize that damage.” Erler v. Five Points Motors, Inc., 249  
7 Cal.App.2d 560, 567 (1967). “No damages can be recoverable for a breach of contract which are  
8 not clearly ascertainable in both their nature and origin.” Cal.Civ.Code § 3301. See, e.g.,  
9 Landes Const. Co. v. Royal Bank of Canada, 833 F.2d 1365, 1373 (9th Cir. 1987) (“[C]ourts  
10 have been reluctant to admit evidence of lost profits for real estate ventures.”); Greenwich S.F.,  
11 LLC v. Wong, 190 Cal.App.4th 739, 754 (2010) (“Where ‘consequential damages’ or special  
12 damages are recoverable for breach of contract not involving breach of a real property purchase  
13 agreement, they may include lost profits, where such profits are the natural and direct  
14 consequence of the breach, where the amount of the lost profits can be established with  
15 reasonable certainty, and where the seller knew of the buyer’s intent to use the property for  
16 profit.” (emphasis added)).

17 C. The Errico Agreement Contains All Material Terms to be Enforceable.

18 Debtor claims that the Errico Agreement “is an unenforceable agreement to agree.”<sup>5</sup>  
19 According to Debtor, the Errico Agreement “leaves three material issues for future agreement:  
20 (1) the method of calculating, and any limitations on Errico paying, the Debtor’s capital gains;  
21 (2) the nature and scope of the ‘statutory and other disclosures’ the Debtor was required to make,  
22 which disclosures could have allowed Errico to back out of the deal; and (3) any limitation on  
23 Errico paying the cost to trim an overhanging tree, which apparently was sufficiently material to  
24 call out specifically in the [Errico] Agreement.”<sup>6</sup> Debtor points to paragraph 4.c.i which required  
25 Errico to pay Debtor’s capital gains as “calculated and limited as set forth on Exhibit 10” of the  
26 agreement, and paragraph 9 which required Debtor to make “the statutory and other disclosures

27 <sup>5</sup> Exhibit 2, Debtor’s Claim Objection, at 27:11-12.

28 <sup>6</sup> Id. at 27:12-18.

1 set forth in Exhibit 12.” It is undisputed that Exhibit 10 is missing entirely from the Errico  
2 Agreement, that Exhibit 12 is blank, and that Errico’s exposure for the total cost of trimming the  
3 overhanging tree was not limited in Exhibit 9 as contemplated in paragraph 4.b.iv of the  
4 agreement.

5 In Patel v. Liebermensch, the California Supreme Court stated that, with respect to a  
6 contract for the sale of real property, “[t]he material factors to be ascertained from the written  
7 contract are the seller, the buyer, the price to be paid, the time and manner of payment, and the  
8 property to be transferred, describing it so it may be identified.” 45 Cal.4th 344, 349 (2008)  
9 (citation omitted). The court explained that:

10 [T]he law does not favor but leans against the destruction of contracts because of  
11 uncertainty; and it will, if feasible, so construe agreements as to carry into effect  
12 the reasonable intentions of the parties if [they] can be ascertained.

13 An agreement for the purchase or sale of real property does not have to be  
14 evidenced by a formal contract drawn with technical exactness in order to be  
15 binding. Equity does not require that all the terms and conditions of the proposed  
16 agreement be set forth in the contract. The usual and reasonable conditions of  
17 such a contract are, in the contemplation of the parties, a part of their agreement.  
18 In the absence of express conditions, custom determines incidental matters  
19 relating to the opening of an escrow, furnishing deeds, title insurance policies,  
20 prorating taxes, and the like.

21 Id. at 349 (citations omitted); In sum, “[i]f the parties have concluded a transaction in which it  
22 appears that they intend to make a contract, the court should not frustrate their intention if it is  
23 possible to reach a fair and just result, even though this requires a choice among conflicting  
24 meanings and the filling of some gaps that the parties have left.” Larwin-Southern California,  
25 Inc. v. JGB Inv. Co., 101 Cal.App.3d 626, 641 (1979); see Ersa Grae Corp. v. Fluor Corp., 1  
26 Cal.App.4th 613, (1991) (“The contract will be enforced if it is possible to reach a fair and just  
27 result, even if, in the process, the court is required to fill in some gaps.”).

28 In this case, the Errico Agreement contains all material terms sufficient to be enforceable.  
The Errico Agreement identifies the seller, the buyer, the property to be transferred, the price to  
be paid, and the time and manner of payment. Although the total amount of capital gains taxes  
payable by Errico is not specified in Exhibit 10, the formula for calculating such capital gains

1 taxes is detailed in paragraph 4.c.i of the Errico Agreement. According to the evidence, the  
2 parties estimated that the cost to correct the overhanging tree was between \$15,000 and \$45,000  
3 and Errico was prepared to pay up to \$45,000 to trim the tree pursuant to paragraph 4.b.iv of the  
4 Errico Agreement. Furthermore, Debtor was the party responsible for making the disclosures  
5 required by paragraph 9, not Errico. The disclosures were for Errico's benefit, not Debtor's.  
6 Debtor cannot argue that the contract is not enforceable by Errico based on her own failure to  
7 make required disclosures. Neither omission of the disclosures in Exhibit 12 nor the cost of  
8 correcting the overhanging tree in Exhibit 9, standing alone or in combination, make the Errico  
9 Agreement materially incomplete or illusory.

10 D. Expert Testimony Regarding Damages Attributable to Debtor's Rejection of the Errico  
11 Agreement.

12 1. Expert Testimony.

13 Rule 702 of the Federal Rules of Evidence permits "[a] witness who is qualified as an  
14 expert by knowledge, skill, experience, training, or education [to] testify in the form of an  
15 opinion or otherwise if: (a) the expert's scientific, technical, or other specialized knowledge will  
16 help the trier of fact to understand the evidence or to determine a fact in issue; (b) the testimony  
17 is based on sufficient facts or data; (c) the testimony is the product of reliable principles and  
18 methods; and (d) the expert has reliably applied the principles and methods to the facts of the  
19 case. F.R.Evid. 702. A court need not accept an expert's opinion, even when the expert's  
20 testimony "is neither contradicted nor impeached." Lutz v. United States, 685 F.2d 1178, 1186  
21 (9th Cir. 1982). "T]he weight to be given expert . . . testimony is within the discretion of the  
22 trier of fact." Rains v. Flynn (In re Rains), 428 F.3d 893, 902 (9th Cir. 2005).

23 2. Errico's Expert Witnesses

24 Hekman, Errico's expert witness, testified on direct that, in his opinion, Errico's damages  
25 resulting from Debtor's rejection of the Errico Agreement totaled \$9,109,180.<sup>7</sup> Hekman is an

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26 <sup>7</sup> Exhibit E, Declaration of John Hekman in Support of Errico's Opposition to Motion Objecting  
27 to Proof of Claim ("Hekman Decl.") [Dkt. # 308], at 6:28.

1 economist with over 25 years of experience in real estate finance. He is a graduate of the  
2 University of Chicago, having received his MBA in Finance from there in 1971 and a Ph.D. in  
3 Economics in 1976. He was formerly an economist with the Federal Reserve and taught real  
4 estate finance at the University of North Carolina and University of Southern California. He has  
5 numerous publications and has testified extensively in state and federal litigation. On cross-  
6 examination, Hekman admitted that he was not an attorney, certified public accountant, or real  
7 estate appraiser, and that he was neither an expert in taxation nor an expert in valuing remainder  
8 interests.

9 Hekman testified that his opinion was based on his estimate of “the difference between  
10 the present value of Mr. Errico’s remainder interest in the [Malibu] Property as of February 19,  
11 2015, and the value of the consideration that was to be paid by Mr. Errico.”<sup>8</sup> First, Hekman  
12 determined that the present value of Errico’s remainder interest was \$14,419,832 as of February  
13 19, 2015, using the following methodology:

- 14 1. Hekman valued the Malibu Property in fee simple at \$13 million as of  
15 February 2015;
- 16 2. Hekman then determined that Debtor had a life expectancy in February 2015  
17 of 15 years based upon life expectancy tables at [www.ssa.gov](http://www.ssa.gov) and  
[www.cdc.gov](http://www.cdc.gov);
- 18 3. Hekman then estimated that the fair market value of the Malibu Property in  
19 fee simple would increase in value over the Debtor’s 15-year remaining  
20 lifetime to \$20.55 million, given at an annual growth rate of 3.1% derived  
from the Zillow Home Value Index for Malibu as of June 2015;
- 21 4. Hekman then applied a discount rate of 2.39%, which was the Applicable  
22 Federal Rate in February 2015, to the \$20.55 million figure to arrive at  
23 \$14,419,832 as the present value of Errico’s remainder interest on February  
24 19, 2015.<sup>9</sup>

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27 <sup>8</sup> Id. at 2:22-24.

28 <sup>9</sup> Id. at 4:14.



Next, Hekman determined that the total value of the consideration to be paid by Errico under the Errico Agreement for the remainder interest was \$5,310,692, which under his analysis consisted of the following components:

1. Consideration for the Transfer: Cash in the amount of \$1,097,741.<sup>10</sup>
2. Capital Gains Taxes: \$224,690 – Errico’s obligation under paragraph 4.c.i of the Errico Agreement to pay capital gains taxes on gains at closing calculated by applying a combined rate of 33.3% for federal and state capital gains taxes to \$674,746 (\$1,000,000, i.e., \$955,000 (Hekman’s total for the consideration specified in ¶¶ 4.a and 4.b.i through 4.b.v), plus \$45,000 to repair the overhanging tree, minus the Debtor’s tax basis of \$75,254 and the capital gains exclusion of \$250,000).
3. Operating Expenses of the Property: \$3,879,373 – The present value of Errico’s obligation under paragraph 4.c.ii.(1) of the Errico Agreement to pay \$20,788.51 a month to Debtor for a period of 15 years as reimbursement for the cost of operating the Malibu Property during the life estate, as increased periodically by 2.0% pursuant to such subparagraph and adjusted by applying a discount rate of 2.39%.
4. Property Insurance: \$46,653 – The present value of Errico’s obligation under paragraph 4.c.ii.(3) of the Errico Agreement to maintain property insurance on the Malibu Property during the life estate, calculated by using a \$3,000 annual premium, assuming a 2% annual increase for 15 years, and applying a 2.39% discount rate.
5. Property Taxes: \$62,235 – The present value of Errico’s obligation under paragraph 4.c.ii.(4) of the Errico Agreement to pay all property taxes on the

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<sup>10</sup> Hekman testified that the Errico Agreement required that the sum of \$3,097,741 be placed in escrow comprised of (a) a cash payment of \$1,097,741 (\$150,000 of which was to have been paid when the Errico Agreement was executed); and (b) a Closing Loan Note in the original principal sum of \$2,000,000 dated February \_\_, 2015, executed by Hannah Hamilburg and payable to Donato Errico, bearing interest at 2.39% per annum and payable in 360 monthly installments of \$7,788.51 each, beginning March 1, 2015. However, Hekman did not treat Errico’s \$2,000,000 loan to Debtor as “part of the consideration under the Remainder Agreement.” Id. at 5:1-2. Hekman testified that from the “\$3,097,741 which was to go into escrow, certain payments were to be made, including the payment of the first mortgage on the property with a balance of \$2,600,000, unsecured debts with a balance of \$205,000, \$150,000 for deferred maintenance projects on the property, and the cost (not specified) of correction of an overhanging tree.” Id. at 5:3-7. Hekman estimated the cost to correct the overhanging tree would not exceed \$45,000. Id. at 5:13.

1 Malibu Property during the life estate, calculated by using the 2015 taxes of  
2 \$4,002, assuming a 2% annual increase for 15 years, and applying a 2.39%  
3 discount rate.

4 Hekman concluded that “the economic loss to Mr. Errico from breach of the Remainder  
5 Agreement is \$14,419,832 less \$5,310,682,” for a total of \$9,109,180.<sup>11</sup>

6 Errico’s expert witnesses included Fife, a certified public accountant, and Muchnick, an  
7 attorney licensed to practice in the State of New York. Fife testified on direct that (1) “[t]he IRS  
8 Table S Factor is not used in valuing damages resulting from the breach of a contract to grant a  
9 remainder interest in real property[;]” (2) the IRS Table S Factor is inapplicable to valuing  
10 damages based on the loss of Mr. Errico’s remainder interest in the Debtor’s property[;]” and (3)  
11 “[i]nvestors in remainder interests do not use the Table S Factor in analyzing the value of a  
12 remainder interest that they are purchasing.”<sup>12</sup> He further testified on direct that “[t]he proper  
13 way to value Mr. Errico’s remainder interest is to take the current fair market value of the  
14 property, add to that the anticipated increase in value of the property during the estimated term of  
15 the life estate, subtract for any projected expenses paid by Mr. Errico over the term of the life  
16 estate (reduced to present value) and then discount that amount to present value using a  
17 customary figure for discounting to present value.”<sup>13</sup> However, Fife admitted on cross-  
18 examination that he had (1) never valued a remainder interest in real property; (2) no experience  
19 in valuing remainder interests; (3) never had an engagement involving a life estate until this case;  
20 (4) never served as a damages consultant in litigation involving a remainder interest until this  
21 case; (5) never been qualified to testify as an expert in litigation involving the issue of a  
22 remainder interest; and (6) never worked with any investors in any context regarding remainder  
23 interests. He further admitted that he was not an expert in calculating damages related to a

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24 <sup>11</sup> Id. at 6:28. The Hekman analysis is silent as to Errico’s obligation under paragraph 4.v. of the  
25 Errico Agreement to “deposit with Escrow the sum of . . . \$1,045,482.00 as partial consideration  
26 for the Remainder Interest.” Exhibit 1, at 14 (emphasis added).

27 <sup>12</sup> Exhibit G, Declaration of Donald Fife in Support of Errico’s Opposition to Motion Objecting  
28 to Proof of Claim (“Fife Decl.”), at 2:18-3:1.

<sup>13</sup> Id. at 3:4-8.

1 remainder interest, and had no experience at all in calculating damages relating to a remainder  
2 interest. He testified that he had not researched the use of IRS Table S by courts in valuing  
3 remainder interests, that his opinion that IRS Table S is inapplicable to valuing damages  
4 resulting from the breach of a contract to grant a remainder interest in real property was not  
5 based on any specific outside sources; and that he was not aware of any sources that state you  
6 cannot use IRS Table S for such purpose.

7 Muchnick testified on direct that “the way to determine such damages is to project the  
8 value of the [Malibu] Property to be obtained by Mr. Errico at the conclusion of the Debtor’s life  
9 estate, discount that amount to present value, and subtract the present value of costs to be  
10 incurred by Mr. Errico in purchasing the remainder.”<sup>14</sup> But on cross-examination, Muchnick  
11 testified that he did not perform a damage calculation independent of Hekman’s and that  
12 determining the amount of Errico’s damages resulting from Debtor’s rejection of the Errico  
13 Agreement was outside the scope of his engagement.

14 3. Debtor’s Expert Witness

15 Grobstein, Debtor’s expert witness, testified on direct that, in his opinion, Errico did not  
16 incur any damages attributable to Debtor’s rejection of the Errico Agreement.<sup>15</sup> Grobstein is a  
17 certified public accountant and certified fraud examiner. He is also certified in financial  
18 forensics by the American Institute of Certified Public Accountants. Grobstein received a  
19 Bachelor of Science from California State University, Northridge in 1994. He is currently a  
20 member of numerous professional organizations, including the California Receivers Forum,  
21 Association of Certified Fraud Examiners, American Bankruptcy Institute, California Society of  
22 Certified Public Accountants, and American Institute of Certified Public Accountants. On cross-  
23 examination, Grobstein admitted that he was not an expert on real estate valuation, including  
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25 <sup>14</sup> Exhibit F, Declaration of Howard Muchnick in Support of Errico’s Opposition to Motion  
26 Objecting to Proof of Claim (“Muchnick Decl.”), 5:23-26.

27 <sup>15</sup> Exhibit 5, Declaration of Howard Grobstein in Support of Debtor’s Motion Objecting to  
28 Donato Errico’s Proof of Claim (Claim No. 15) (“Grobstein Decl.”) [Dkt. # 285], at 6:27-28.

1 valuing remainder interests; but he did state that he had experience testifying as a summary  
2 witness concerning damage issues relating to real estate contracts.

3 Grobstein did not use the same methodology as Hekman to determine the value of the  
4 remainder interest in the Malibu Property that Errico sought to purchase under the Errico  
5 Agreement. Grobstein began by valuing the Malibu Property in fee simple at \$13 million as of  
6 February 2015. Grobstein then referred to Internal Revenue Service Bulletin: 2009-20 dated  
7 May 18, 2009, entitled “Use of Actuarial Tables in Valuing Annuities, Interests for Life or  
8 Terms of Years, and Remainder or Reversionary Interests.”<sup>16</sup> Using a 1.8% interest rate derived  
9 from IRS Rev. Ruling 2015-4 and the Debtor’s age of 72, Grobstein then applied a remainder  
10 factor of .80021 derived from IRS Table S to the Malibu Property’s fee simple valuation of \$13  
11 million to calculate the value of Errico’s remainder interest in the property at \$10,402,730.<sup>17</sup>

12 Next, Grobstein determined that the total value of the consideration to be paid by Errico  
13 for a remainder interest in the Malibu Property under the Errico Agreement through close of  
14 escrow was \$5,250,211,<sup>18</sup> which included the following:

- 15 1. Consideration for the Transfer: Cash in the amount of \$1,247,741  
16 (\$1,097,741 + \$150,000).<sup>19</sup>

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18 <sup>16</sup> Id. at 24.

19 <sup>17</sup> Id. at 3:14.

20 <sup>18</sup> Id. at 4:18. Grobstein’s calculations included two scenarios based on his interpretation of  
21 paragraph 4 of the Errico Agreement. Grobstein testified that, in his opinion, scenario # 1 “may  
22 be the more accurate estimation of Errico’s claim.” Exhibit 5, Grobstein Decl., 6:11-12. For  
23 purposes of this discussion, the court will focus on Grobstein’s scenario # 1 and give little, if  
any, weight to Grobstein’s scenario # 2.

24 <sup>19</sup> In contrast to the Hekman analysis, Grobstein does not reduce Errico’s obligation to make a  
25 \$1,047,741 payment into escrow by the \$150,000 payment due upon execution of the contract  
26 under paragraph 4.a. of the Errico Agreement. Moreover, the Grobstein analysis also does not  
27 appear to give full effect to the language in paragraph 4, which states that “Buyer will make a  
28 payment into escrow of \$1,097,741 (i.e., the aggregate of all of the expenses set forth in 4.b.i  
through 4.b.iv, minus \$2,000,000 as initial consideration (“Initial Consideration”). Exhibit 1, at  
13 (emphasis added).

2. Liquidation of Existing Mortgage Debt: \$2,601,257 – Errico’s obligation under paragraph 4(b)(i) of the Errico Agreement to pay existing debt secured by the Malibu Property as set forth in Exhibit 7.
3. Liquidation of Existing Unsecured Creditor Debt: \$205,731 – Errico’s obligation under paragraph 4.b.ii of the Errico Agreement to pay the unsecured debt listed in Exhibit 8.
4. Deferred Maintenance: \$150,000 – Errico’s obligation under paragraph 4.b.iii of the Errico Agreement to pay \$150,000 for the purpose of funding various improvement projects and deferred maintenance expenses on the Malibu Property.
5. Cost of Correcting Overhanging Tree: (Unknown) – Errico’s obligation under paragraph 4.b.iv of the Errico Agreement to pay the cost of correcting the overhanging tree.
6. Payment at Closing: \$1,045,482 – Errico’s obligation under paragraph 4.b.v to deposit at closing the sum of \$1,045,482 “as partial consideration for the Remainder Interest.”

Then Grobstein added the following post-closing expenses required to be paid by Errico under the Errico Agreement:

1. Capital Gains Taxes – Federal: \$3,314,583
2. Capital Gains Taxes – State: \$1,943,942
3. Operating Expenses of the Property: \$3,879,373
4. Property Taxes: \$2,505,266<sup>20</sup>

Grobstein concluded that “Errico’s total cost to purchase his remainder interest in the Malibu Property would have been \$16,893,473.”<sup>21</sup> Because the total cost of \$16,893,473 exceeded the

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<sup>20</sup> Unlike the Hekman analysis, Grobstein’s calculation assumes that the transaction would result in a reassessment of property taxes due to a change in ownership within the scope of California Revenue & Taxation Code § 60. Grobstein’s analysis also does not appear to include as post-closing consideration the present value of Errico’s obligation under paragraph 4.c.ii.(3) to maintain property insurance on the Malibu Property during the life estate.

<sup>21</sup> Exhibit 5, Grobstein Decl., 5:14.

1 \$10,402,730 value of the remainder interest sought to be purchased, Grobstein concluded that  
2 Errico was not damaged as a result of Debtor's rejection of the Errico Agreement.<sup>22</sup>

3 E. Court's Analysis and Determination of Errico's Damages for Debtor's Rejection of the Errico  
4 Agreement.

5 1. Relevant Portions of the Errico Agreement

6 Paragraph 4 of the Errico Agreement entitled "Consideration for Transfer," states in  
7 pertinent part:

8 In consideration of Life Estate Entity's sale, transfer, assignment and conveyance  
9 of the Remainder Interest to Buyer, Buyer will make a payment into escrow of  
10 \$1,097,741 (i.e., the aggregate of all of the expenses set forth in 4.b.i through  
11 4.b.iv, minus \$2,000,000 as initial consideration ("Initial Consideration").  
12 Additionally, Buyer will extend a loan to Life Estate Entity ("Closing Loan"),  
pursuant to a note ("Closing Loan Note") substantially in the form set forth as  
Exhibit 6 hereto. . . From the Initial Consideration, Escrow shall pay all of the  
following to or on behalf of Seller:

13 a. Payment at Contract Execution. Upon execution of this Agreement by  
14 the parties, Buyer shall deposit with Escrow the sum of one hundred  
15 fifty thousand dollars (\$150,000).

16 b. Payments to be Made by Buyer Contemporaneously with the Closing.  
17 Contemporaneously with the Closing, Buyer shall make each of the  
following payments to Seller or on Seller's behalf:

18 i. Liquidation of Existing Mortgage Debt. Various mortgage  
19 creditors are owed sums by Seller, which debts are secured by  
20 security interests in the Property. Such mortgagors, their  
addresses and the approximate amount they are owed are set  
21 forth as Exhibit 7 hereto. Contemporaneously with the  
Closing, Escrow shall pay the full pay off amounts of each  
22 such mortgage creditor and obtain a full reconveyance of the  
security interest in the Property from such creditors and, for the  
23 benefit of Seller, shall obtain a full release of all such debt  
from each of the enumerated creditors, respectively.

24  
25 ii. Liquidation of Enumerated Unsecured Creditors of Seller.  
26 Various unsecured creditors are owed sums by Seller. Such  
creditors, their addresses and the approximate amount they are  
27 owed are set forth as Exhibit 8 hereto. Contemporaneously

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28 <sup>22</sup> Id. at 5:20-23.

with the Closing, Escrow shall pay the full pay off amounts to each such creditor and obtain for the benefit of Seller, a receipt and release of all such debt from each such enumerated creditor, respectively.

iii. Payment for Deferred Maintenance. Contemporaneously with the Closing, Buyer shall pay Life Estate Entity one hundred and fifty thousand dollars (\$150,000) for the purposes of funding various improvement projects and deferred maintenance expenses at the Property, including, but not limited to, the repair of the roof, the replacement of doors and windows, correction of any plumbing issues, correction and/or removal of the overhanging tree at the property, desirable upgrades to the guesthouse facility and/or various gardening initiatives. Anything to the contrary notwithstanding, Seller shall have complete and absolute discretion regarding the maintenance and improvement projects undertaken, including whether or not any particular project or improvement is pursued, the identity of any contractors employed, the sums to be paid and the manner in which such work will be undertaken.

iv. Cost of Correction of Overhanging Tree. The Buyer shall pay the cost of correcting the overhanging tree in an amount of not to exceed the tree trimming estimate set forth as Exhibit 9 hereto.

v. Payment. Contemporaneously with the Closing, Buyer shall deposit with Escrow the sum of one million forty-five thousand, four hundred and eighty-two dollars (\$1,045,482.00) as partial consideration for the Remainder Interest.<sup>23</sup>

Paragraph 4.c.i of the Errico Agreement, entitled Payment of Capital Gains Taxes on Closing, further provided:

On or before April 15, 2016, Buyer will pay all of Seller's capital gains resulting from this transaction, such amount to be calculated and limited as set forth on Exhibit 10, annexed hereto. As such term is used in Subparagraph 4.c.i, capital gains will mean the difference between Seller's cost basis and the consideration received by Seller from Buyer pursuant to Subparagraphs 4.a and 4.b.i through 4.b.v., above; provided, however, that in calculating Seller's cost basis in the Property, Seller shall use her best efforts to show a cost basis of as close to \$1,000,000 as possible using legal fees, deferred maintenance, and upgrade and maintenance costs paid and other credits and in such efforts Seller shall receive credit for the \$250,000 exclusion from gain for the sale of Seller's principal

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<sup>23</sup> Exhibit 1, at 13-14.

1 residence pursuant to 26 U.S.C. § 121. Seller shall cooperate fully with Buyer's  
2 efforts to handle the capital gains treatment in the most efficient manner  
possible.<sup>24</sup>

3 Finally, paragraph 4.c.ii of the Errico Agreement, entitled Ongoing Payment Obligations of  
4 Buyer, states in pertinent part:

5 (1) Operating Expenses of the Property. On the first day of each month Buyer will reimburse  
6 the Life Estate Entity for all costs of operating the Property during the preceding month,  
7 including but not limited to all utilities (including gas, water, power, sewage, telephone,  
8 internet and the monthly amount the Life Estate Entity is obligated to pay Buyer on the  
Closing Loan Note), maintenance expenses and physical repairs (including septic  
9 maintenance), gardening, tree-trimming and housekeeping; provided that Buyer shall not  
be required during any one period to reimburse Seller for expenses exceeding the  
10 Expenditure Sum Limit (as such term is hereinafter defined); provided further that sums  
not reimbursed in any given period because such sums exceed the Expenditure Sum  
11 Limit, may be reimbursed in other periods in which the Expenditure Sum Limit has not  
been reached. The "Expenditure Sum Limit" shall be an amount which equals  
12 \$20,788.51 per month in the first month of the Agreement and is increased on each  
anniversary date thereafter by 2.0% of the Expenditure Sum Limit payable in the month  
13 immediately preceding such anniversary date. Any sums paid by Buyer as  
14 reimbursement to the Life Estate Entity for Operating Expenses of the Property shall be  
treated as expenses of the Buyer directly to the vendor therefor and Buyer. . .

15 (3) Annual Property Insurance Payments. During the term of the Life Estate hereunder,  
16 Buyer shall maintain an all-risks property insurance policy issued by a company having  
17 at least an A-rating from either A.M. Best, Standard & Poor's or Moody's Investors  
Service (hereinafter "Insurance Policy"). Such Insurance Policy shall insure for the full  
18 replacement value of the improvements on the Property. In the event of any insured  
casualty with respect to the improvements on the Property occurring during Seller's life,  
19 all insured proceeds shall be paid to Life Estate Entity and shall be utilized by Life Estate  
Entity to pay for such improvements. In the event of any condemnation of all or part of  
20 the Property during Seller's life, such proceeds shall be payable as follows: Life Estate  
Entity shall receive an amount from such condemnation proceeds equal to the fair market  
21 rental value of the Property (determined as of the date of condemnation) over her  
remaining life expectancy. The remainder of the proceeds shall be payable to Buyer.  
22 Notwithstanding the condemnation, Seller's obligations to Buyer under the Closing Loan  
Note and Buyer's obligation to pay to Seller the Expenditure Sum Limitation shall  
23 continue.

24 (4) Property Tax Payments. During the term of the Life Estate hereunder, Buyer shall pay,  
25 before delinquency, all property taxes on the Property (including any increases for  
26 reassessment or other assessments) imposed by the County or other taxing authorities.

27  
28 <sup>24</sup> Id. at 15.



1 The Buyer shall deliver to Seller at the address stated below copies of paid tax and  
2 assessment receipts within 45 days after the due date.<sup>25</sup>

3 2. Value of the Remainder Interest

4 Prior to this case, neither Hekman nor Grobstein had experience calculating the value of a  
5 remainder interest for purposes of determining damages attributable to rejection of an executory  
6 contract for the sale of an interest in real property. Hekman did not cite any court authority,  
7 learned treatise, or other authoritative source in support of his methodology. Errico's opposition  
8 states that "California law has specifically recognized in valuing remainder interests, an assumed  
9 rate of return on the investment, e.g., the anticipated increase in value of the property over the  
10 course of the life estate, should be considered[,]”<sup>26</sup> citing Estate of Malpas, 7 Cal.App.4th 1901  
11 (1992). Malpas, however, stands for the simple proposition that estate taxes must be allocated  
12 between the life estate and remainder under California Probate Code § 20113. Id. at 1904. In  
13 dicta, the court in Malpas noted “that for various purposes (including death taxation) life estates  
14 and remainder interests in any given asset may be separately valued at any point in time, on the  
15 basis of life expectancy and an assumed rate of return on investment, and that the sum of their  
16 values will equal the value of the asset at that time.” Id. 1908. In support of its observation,  
17 however, the Malpas court did not cite any authority other than the IRS's actuarial tables that  
18 accompany its regulation entitled “Valuation of annuities, interests for life or term of years, and  
19 remainder or reversionary interests” which appears at 26 C.F.R. § 20.2031-7. Id.

20 Section 7520(a) of the Internal Revenue Code states that “[f]or purposes of this title, the  
21 value of any annuity, any interest for life or a term of years, or any remainder or reversionary  
22 interest shall be determined – (1) under tables prescribed by the Secretary, and (2) by using an  
23 interest rate (rounded to the nearest 2/10ths of 1 percent) equal to 120 percent of the Federal  
24 midterm rate in effect under section 1274(d)(1) for the month in which the valuation date falls.”

25 \_\_\_\_\_  
26 <sup>25</sup> Id. at 15-16.

27 <sup>26</sup> Exhibit 7, Creditor Donato Errico's Opposition to Motion Objecting to Proof of Claim (Claim  
28 No. 15); Memorandum of Points and Authorities in Support Thereof (“Errico's Opposition”)  
[Dkt. # 295], at 14:10-12.

26 U.S.C. § 7520(a). With respect to the interest rate required by § 7520(a)(2), Revenue Ruling 2015-4 Table 5 effectuates § 1274, “contains the federal rate for determining the present value of an annuity, an interest for life or for a term of years, or a remainder or a reversionary interest for purposes of section 7520[.]” and states that the “[a]pplicable federal rate of interest for determining the present value of an annuity, and interest for life or a term of years, or a remainder or reversionary interest” for March 2015 was 1.8%. Rev.Rul.2015-4, 2015 WL 685700 (March 15, 2015). With respect to the table specified under § 7520(a)(1), the IRS’s final regulations entitled “Use of Actuarial Tables in Valuing Annuities, Interests for Life or Terms of Years, and Remainder or Reversionary Interests” contains the appropriate actuarial tables to be used to value a life estate, remainder, or other interest for purposes of income taxes, estate taxes, or gift taxes as of a date on or after May 1, 2009. See 76 FR 495780-01, 2011 WL 3468798 (August 10, 2011). Table S, which lists the “Single Life Remainder Factors Applicable On or After May 1, 2009,” prescribes the use of a remainder factor of .80021 when the age of the life tenant is 72 and applicable interest rate is 1.8%.<sup>27</sup>

IRS actuarial tables have been used by bankruptcy courts to divine the value of interests in property, including life estates, remainders, and tenancies by the entireties, for purposes other than federal income, estate and gift taxation. See, e.g., Pletz v. United States, 221 F.3d 1114, 1119 (9th Cir. 2000) ( affirming the district court’s decision to uphold a bankruptcy court’s order denying chapter 13 plan confirmation based on a valuation of the Debtor’s interest in property held jointly with his wife as tenants by the entireties using joint-life actuarial tables); In re Murray, 318 B.R. 211, 215 (Bankr. M.D.Fla. 2004) (valuing the IRS’s secured claim on property held by Debtors as tenants by the entireties with reference to joint life actuarial tables.”); Matter of Reardon, 10 B.R. 697, 700 (Bankr. D. Conn. 1981) (applying “actuarial tables employed by the Internal Revenue Service to arrive at values of life estates and remainder interests” to conclude that judicial lien did not impair Debtor’s homestead exemption in a remainder interest).

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<sup>27</sup> Under the regulation, the Table S Factor remained .80021 when applying an interest rate of 1.8% and an age of 72 whether the valuation was for purposes of federal income tax [26 C.F.R. § 1.642(c)(6)], federal estate taxes [26 C.F.R. § 20.2031-7], or federal gift taxes [26 C.F.R. §§ 25.2512-5; 25.7520-1].

1 Using the 1.8% interest rate prescribed by IRS Rev. Ruling 2015-4 and the Debtor's age  
2 of 72, Grobstein applied the appropriate remainder factor of .80021 derived from IRS Table S to  
3 the Malibu Property's fee simple valuation of \$13 million to calculate the value of Errico's  
4 remainder interest in the property at \$10,402,730. Based on the foregoing, the court will adopt  
5 Grobstein's calculation to fix the value of the remainder interest in the Malibu Property which  
6 Errico sought to purchase under the Errico Agreement at \$10,402,730.

7 3. No Reassessment of Property Taxes on Malibu Property

8 Paragraph 4.c.ii(4) of the Errico Agreement requires Errico to pay "all property taxes on  
9 the [Malibu] Property (including any increases for reassessments or other assessments) imposed  
10 by the County or other taxing authorities" during the term of the life estate.<sup>28</sup> Debtor and Errico  
11 disagree on the issue of whether the transaction contemplated by the Errico Agreement will  
12 constitute a "change in ownership" under California Revenue & Taxation Code § 60, and trigger  
13 a reassessment of property taxes on the Malibu Property. Hekman believes that the transaction  
14 will not trigger a reassessment and testified that the present value of Errico's obligation under  
15 paragraph 4.c.ii(4) is \$62,235 calculated by using the 2015 taxes of \$4,002, assuming a 2%  
16 annual increase for 15 years, and applying a 2.39% discount rate. On the other hand, Grobstein,  
17 who opined that the transaction will result in a reassessment of property taxes, testified that the  
18 present value of Errico's property tax obligation is \$2,505,366 using as a starting point 1.1% of  
19 the sales price of \$13,000,000.

20 The Constitution of the State of California provides that county assessors may reassess  
21 taxes due on real property only when said property is "purchased, newly constructed, or a change  
22 in ownership has occurred . . . ." Cal. Const., art. XIII A, § 2(a). "Change in ownership," as used  
23 in the California Revenue & Taxation Code, means "a transfer of a present interest in real  
24 property, including the beneficial use thereof, the value of which is substantially equal to the  
25 value of the fee interest." Cal. Rev. & Tax. Code § 60. A change in ownership, as defined in §  
26 60, includes, but is not limited to . . . [a]ny vesting of the right to possession or enjoyment of a  
27 remainder or reversionary interest that occurs upon the termination of a life estate or other

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28 <sup>28</sup> Exhibit 1, at 16.

1 similar precedent property interest . . . .” Cal. Rev. & Tax. Code § 61(g). A change in  
2 ownership does not include either of the following:

3 1. “[a]ny transfer between an individual . . . and a legal entity . . . , that results  
4 solely in a change in the method of holding title to the real property and in which  
5 proportional ownership interests of the transferors and transferees, whether  
6 represented by stock, partnership interest, or otherwise, in each and every piece of  
real property transferred, remain the same after the transfer.” Cal. Rev. & Tax.  
Code § 62(a)(2).

7 2. “[a]ny transfer by an instrument whose terms reserve to the transferor an  
8 estate for years or an estate for life.” Cal. Rev. & Tax. Code § 62(e).

9 Under paragraph 3 of the Errico Agreement, Errico was to receive a remainder interest in  
10 the Malibu Property through a structured transaction involving a “Life Estate Entity” and two  
11 separate and contemporaneous transfers of an interest in the Malibu Property at closing: (1)  
12 Debtor’s transfer of a fee simple interest in the Malibu Property to the Life Estate Entity (the  
13 “First Transfer”); and (2) the Life Estate Entity’s transfer of a remainder interest in the Malibu  
14 Property to Errico (the “Second Transfer”). The court does not believe that either the First  
15 Transfer or the Second Transfer will trigger a reassessment of taxes on the Malibu Property.

16 With respect to the First Transfer, Debtor formed “28926 Cliffside Drive LLC,” a limited  
17 liability company, which was designated the “Life Estate Entity” under the Errico Agreement.  
18 The First Transfer required Debtor to transfer the Malibu Property to 28926 Cliffside Drive LLC  
19 in fee simple at closing. The Limited Liability Company Agreement of 28926 Cliffside Drive  
20 LLC (“Operating Agreement”) designates Debtor as its sole equity member and prohibited the  
21 admission of additional members. Debtor’s interest in the Malibu Property after the transfer  
22 would have been proportional to her interest in the Malibu Property immediately before the  
23 transfer. Errico is named as an “Independent Manager” in the Operating Agreement. The  
24 Independent Manager is appointed by the sole member and must discharge the duties set forth in  
25 § 10 of the Operating Agreement. As Independent Manager, Errico is not a member under the  
26 Operating Agreement, could not become a member of the limited liability company, and would  
27 not have received a beneficial interest in the Malibu Property as a result of the First Transfer. In  
28 his capacity as Independent Manager, Errico would have had the right under § 5(c) to become a

1 “Special Member” but only “[u]pon the occurrence of any event that caused the Member to cease  
2 to be a member of the Company” and even in that capacity would have “no interest in the profits,  
3 losses and capital of the Company and . . . no right to receive any distributions of Company  
4 assets.”<sup>29</sup> Section 9(d)(iv) of the Operating Agreement authorized Errico, as Independent  
5 Manager, “to execute and file on behalf of the Company a quitclaim deed transferring the  
6 [Malibu] Property from the Company to Donato Errico or his assign” upon the death of the  
7 Company’s sole equity member, the Debtor.<sup>30</sup> Because Debtor would have retained her  
8 proportional interest in the Malibu Property and Errico would have received no beneficial  
9 interest in the Malibu Property under the First Transfer, the court believes that the First Transfer  
10 would have been exempt under California Revenue & Taxation Code § 62(a)(2) and would not  
11 have triggered a reassessment of property taxes on the Malibu Property.

12 With respect to the Second Transfer, the Life Estate Entity was to convey to Errico by  
13 Remainder Interest Deed (Life Estate Reservation) all right, title and interest in the Malibu  
14 Property with the Life Estate Entity reserving a life estate. Under the terms of the deed, the Life  
15 Estate Entity was to have “full ownership, possession and use of the [Malibu Property], as well  
16 as the rents, revenues and profits generated by the property during the term of [Debtor’s] natural  
17 life, subject to Grantee’s Current Interests” as defined in the Errico Agreement.<sup>31</sup> Paragraph 2 of  
18 the Errico Agreement stated that “[d]uring the life of the Seller, Seller shall have the right to  
19 complete, continuous and exclusive use of the [Malibu] Property subject to ‘Buyer’s Current  
20 Interests,’” which limited Errico access to the Malibu Property only for the following: (1)  
21 permission to park a vehicle in a designated location at the property; (2) permission to maintain a  
22 small cabana near that parking area suitable for the maintenance and storage of his surfing  
23 equipment; (3) permission to have access to the beach abutting the property; and (4) permission

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25  
26 <sup>29</sup> Exhibit 1, at 24.

27 <sup>30</sup> Id. at 26.

28 <sup>31</sup> Id. at 44.

1 to have two (2) beach access keys for the beach area.<sup>32</sup> Because the terms of the deed from the  
2 Life Estate Entity to Errico reserved to the transferor an estate for life, the court believes that the  
3 Second Transfer falls squarely within the exemption provided under California Revenue &  
4 Taxation Code § 62(e) and would not have triggered a reassessment of property taxes on the  
5 Malibu Property.

6 In sum, the court will adopt Hekman's calculation of \$62,235 as the present value of  
7 Errico's obligation under paragraph 4.c.ii(4) of the Errico Agreement to pay property taxes on  
8 the Malibu Property during the term of the life estate for purposes of determining the amount of  
9 damages attributable to Debtor's rejection of the agreement.

10 4. Consideration Due at Close of Escrow

11 Hekman and Grobstein presented conflicting calculations regarding to total consideration  
12 due at closing. To the sum of \$1,097,741 appearing in paragraph 4, Grobstein added the  
13 \$150,000 due under paragraph 4.a upon execution of the Errico Agreement. Hekman did not.  
14 Moreover, the sum of \$1,097,741 appearing in paragraph 4 purports to be a total of the amounts  
15 due under subparagraphs 4.b.i through 4.b.iv, but the figure can only be construed as an estimate  
16 because the amounts in subparagraphs 4.b.i through 4.b.iv were not yet fixed by Exhibits 7, 8  
17 and 9. Unsecured claims were added to Exhibit 7 and the \$45,000 cost to trim the overhanging  
18 tree had not been included in Exhibit 9. The aggregate of all expenses set forth in paragraphs  
19 4.b.i through 4.b.iv is \$3,001,988, less \$2,000,000 equals \$1,001,988. The court agrees with  
20 Hekman that the \$150,000, which was to be paid upon execution of the Errico Agreement is  
21 subsumed in this figure as part of the Initial Consideration. To this amount, however must be  
22 added the payment of \$1,045,482 due at closing under paragraph 4.b.v., for a total of \$2,047,740.

23 5. Consideration Due After Close of Escrow

24 Paragraph 4.c.i of the Errico Agreement defines capital gains as "the difference between the  
25 Seller's cost basis and the consideration received by Seller from Buyer pursuant to  
26 Subparagraphs 4.a and 4.b.i through 4.b.v."<sup>33</sup> The court has recalculated the amount of capital

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27 <sup>32</sup> Id. at 13.

28 <sup>33</sup> Id. at 15.

gains taxes resulting from the transaction on the total consideration paid through closing as \$573,588 by applying a combined rate of 33.3% for federal and state capital gains taxes to \$1,722,486 (\$2,047,740 minus the Debtor's tax basis of \$75,254 and the capital gains exclusion of \$250,000).

The court disagrees with Grobstein's conclusion that the transaction would constitute a change in ownership under California Tax and Revenue Code § 60, triggering an increase in future property taxes.

Finally, the court adopts Hekman's calculations regarding Errico's post-closing ongoing obligations regarding the payment of operating expenses, property taxes, and property insurance during the life estate pursuant to paragraphs 4.c.ii(1), (3) and (4) of the Errico Agreement.

#### 6. Amount of Claim

Based on the foregoing, the court determines that Errico's claim for damages attributable to Debtor's rejection of the Errico Agreement is \$3,793,141, calculated as follows:

<u>Value of Remainder Interest</u>		\$10,402,730
<u>Consideration Due at Close of Escrow</u>		
Existing Mortgage Debt [¶ 4.b.i]	\$2,601,257	
Unsecured Debt [¶ 4.b.ii]	205,731	
Deferred Maintenance [¶ 4.b.iii]	150,000	
Trim Overhanging Tree [¶ 4.b.iv]	<u>45,000</u>	
Subtotal	\$3,001,988	
Less	<u>2,000,000</u>	
		1,001,988 <sup>34</sup>
Payment at Closing [¶ 4.b.v]		<u>1,045,482</u>
Total		2,047,470

#### Consideration After Close of Escrow

Capital Gains Taxes [¶ 4.c.i]	\$ 573,588
Operating Expenses [¶ 4.c.ii(1)]	3,879,373
Property Insurance [¶ 4.c.ii(3)]	46,653
Property Taxes [¶ 4.c.ii(4)]	<u>62,235</u>

<sup>34</sup> This figure includes the deposit of \$150,000 paid upon execution of the contract pursuant to paragraph 4.a of the Errico Agreement.

1 Total 4,561,849

2 Recapitulation

3 Value of Remainder Interest \$10,402,730  
4 Consideration Due at Close of Escrow -2,047,470  
5 Consideration Due After Close of Escrow -4,561,849

6 Total Claim \$ 3,793,411


7 III. CONCLUSION

8 For the reasons stated, Debtor's motion objecting to Errico's Claim # 15 will be granted,  
9 and Errico will be allowed an unsecured non-priority claim in the reduced amount of \$3,793,411,  
10 subject to adjudication of the Debtor's remaining defenses to Errico's claim in this case.<sup>35</sup>

11 A separate order will be entered consistent with this memorandum decision.

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24 Date: August 11, 2016

  
Peter H. Carroll  
United States Bankruptcy Judge

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28 <sup>35</sup> See footnote # 1, infra.