

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION**

IN RE:	§	
	§	
COBALT INTERNATIONAL ENERGY, INC., ET AL.	§	Chapter 11
	§	
Reorganized Debtors.	§	Case No. 17-36709
	§	
	§	(Jointly Administered)
	§	

**RESPONSE AND REQUEST FOR ABSTENTION OF CYPRESS-FAIRBANKS
INDEPENDENT SCHOOL DISTRICT AND HARRIS COUNTY TO MOTION OF
NADER TAVAKOLI, ACTING SOLELY AS PLAN
ADMINISTRATOR, FOR ENTRY OF AN ORDER DETERMINING 2018 AD
VALOREM TAX LIABILITIES PURSUANT TO 11 U.S.C. § 505**
(Docket #1241)

**To the Honorable Marvin Isgur,
United States Bankruptcy Judge:**

NOW COMES, Harris County in its own right and the following entities for which it collects: Harris County Department of Education, Harris County Flood Control District, Harris County Hospital District, Lone Star College System, Port of Houston Authority, and Harris County Emergency Services District #9 (collectively, “**Harris County**”) and Cypress-Fairbanks Independent School District (“**Cy-Fair ISD**”) (together with Harris County, the “**Taxing Authorities**”), secured creditors in the above-numbered and styled bankruptcy case, and file this *Response and Request for Abstention to Motion of Nader Tavakoli, Acting Solely as Plan Administrator, for Entry of an Order Determining 2018 Ad Valorem Tax Liabilities Pursuant to 11 U.S.C. § 505*, stating as grounds therefore the following:



1. On December 14, 2017, (the “**Petition Date**”), Cobalt International Energy, Inc. and certain of its affiliates (the “**Debtors**”) filed voluntary petitions for relief under Chapter 11 of the United States Bankruptcy Code (the “**Bankruptcy Code**”).

2. On April 5, 2018, the Court entered its Order Confirming the Fourth Amended Joint Chapter 11 Plan (the “**Plan**”) of Cobalt International Energy, Inc. and its affiliated debtors (collectively, the “**Debtors**”). Pursuant to the Plan and Confirmation Order, Nader Tavakoli (the “**Plan Administrator**”) was charged with acting for the Debtors to resolve disputed claims, make distributions pursuant to the Plan, and administer the Plan.

3. On or about January 31, 2019, the Plan Administrator filed a Motion for Entry of an Order Determining the 2018 Ad Valorem Tax Liabilities Pursuant to 11 U.S.C. § 505 (the “**Motion**”). The Debtors request the Court determine the fair market value of certain personal property (the “**Personal Property**”) located at 6401 North Eldridge Parkway, Houston, Texas 77074 (the “**Eldridge Location**”) and 920 Memorial City Way, Suite 100, Houston, Texas 77024 (the “**Memorial City Location**”).¹ The Taxing Authorities object to such relief and ask the Court to abstain from deciding the merits of the Motion.

FACTS

4. The Taxing Authorities are units of local government in the State of Texas which possess the authority under the laws of the state to assess and collect ad valorem taxes on real and personal property. The Harris County Appraisal District (“**HCAD**”) is

¹ The Plan Administrator has reserved his right to modify his Motion to include other locations with personal property. The Taxing Authorities similarly reserve their right to amend or modify their objection to incorporate and raise any defenses it may have in regards to any arguments or allegations the Plan Administrator may assert.

a separately established governmental agency under the laws of the State of Texas that possesses the authority to assess the value of real and personal property as well as grant any exemptions related to such property. HCAD is a separate and distinct governmental entity that is unrelated to Harris County. Upon information and belief, HCAD, although the party responsible for determining and defending values pursuant to state law, was not given notice of this matter.

5. Contemporaneously with the filing of this Motion, the Plan Administrator alleges that he filed a Personal Property Correction Motion with HCAD in accordance with section 25.25(d) of the Texas Property Tax Code for the Personal Property (the “**Correction Motion**”).²

6. On or about March 28, 2018, Harris County filed administrative proof of claim number 416 in the estimated amount of \$225,574.87³ for taxes assessed against the Debtors’ personal property for tax year 2018. Harris County has filed an amended administrative proof of claim in the amount of \$237,805.72 to reflect the actual 2018 tax amounts and accrued post-penalties and interest. Harris County’s claim consists of the following personal property accounts:

Account #	Amount	Location
2163136	\$ 53,724.13	Memorial City Location
2067878	\$ 44,657.78	Eldridge Location
2250551	\$ 425.78	660 Greens Parkway
2080312	\$ 18,992.37	10222 Sheldon Rd
2080313	\$119,238.88	9518 E. Mount Houston
2293922	\$ 766.78	13460 Lockwood Rd.

² The Taxing Authorities have not been able to verify whether the Correction Motion was filed and if filed, whether it was timely.

³At the time Harris County filed its administrative proof of claim, the 2018 appraisal and tax rolls were not certified.

7. On or about March 28, 2018, Cy-Fair ISD filed administrative proof of claim number 417 in the estimated amount of \$47,283.05 for 2018 taxes assessed against the Debtor's personal property at the Eldridge Location. Cy-Fair ISD has filed an amended administrative proof of claim in the amount of \$80,820.43 to reflect the actual 2018 tax amounts and accrued post-petition penalties and interest.

RESPONSE AND REQUEST FOR ABSTENTION

A. Abstention

8. The Taxing Authorities respectfully request the Court to exercise its power of discretionary abstention. Discretionary abstention in bankruptcy cases is governed by 28 U.S.C. §1334(c)(1), which provides, in pertinent part, the following:

“...nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title.”

9. In a recent case, the bankruptcy court abstained from determining a debtor's tax liability owed to Harris County, stating that “[s]ection 505(a)(1) permits, but does not require, the bankruptcy court to determine a debtor's tax liability. It provides that the ‘court *may* determine the amount or legality of any tax, any fine or penalty relating to a tax, or any addition to a tax,’ whether or not such tax has been previously assessed or paid.” *In re CM Reed Almeda 1-3062, LLC*, 2016 WL 3563148, at *3 (Bankr.D.Nev. May 31, 2016)(emphasis in the original), *aff'd*, 2:13-BK-19117, 2017 WL 1505215 (9th Cir. BAP Apr. 26, 2017). As the Nevada bankruptcy court pointed out, the discretionary aspect of this statute has been noted by several courts. *Id.* at FN 71, *citing*

Central Valley AG Enterprises v. United States, 531 F.3d 750, 764 (9th Cir. 2008)(§ 505(a)(1) “is a permissive empowerment” rather than a “mandatory directive.”); *In re Luongo*, 259 F.3d 323,330 (5th Cir. 2001)(“The bankruptcy court’s ability to abstain is premised on Congress’ use of the word ‘may’ in § 505.”); *In re New Haven Projects Ltd. Liability Co.*, 225 F.3d 283, 288 (2nd Cir. 2000)(“we interpret the verb ‘may’ in 11 U.S.C. § 505(a)(1) as vesting the bankruptcy court with discretionary authority to redetermine a debtor’s taxes.”); *In re Breakwater Shores Partners, L.P.*, 2012 WL 1155773, at *2 (“the exercise of jurisdiction under § 505 is discretionary with this Court.”); *In re Gordon*, 2011 WL 3878356, at *5 (Bankr.S.D.N.Y. Aug. 30, 2011)(“As the verb ‘may’ indicates, the Court’s ability to determine a debtor’s tax liability is discretionary.”); *In re Galvano*, 116 B.R. 367, 372 (Bankr.E.D.N.Y. 1990)(§505 is discretionary, and “the Court may decline to review a debtor’s tax liability.”)

10. The issue presented by this case goes far beyond mere mathematical calculation or even determination of tax liability. The Plan Administrator is essentially asking the Court to impose a different methodology – in this instance, a **fire sale** valuation methodology – or standard for valuing the Personal Property for local tax purposes.⁴ Rather than use the valuation methodology mandated by state law and applied by HCAD to other similar properties in the area in which the Personal Property lies, the Plan Administrator proposes a different standard based upon an auction liquidation value. The Personal Property in question was valued in a similar manner as all

⁴ Section 23.01(b) of the Texas Tax Code provides, “[t]he market value of property shall be determined by the application of generally accepted appraisal methods and techniques. If the appraisal district determines the appraised value of a property using mass appraisal standards, the mass appraisal standards must comply with the Uniform Standards of Professional Appraisal Practice. The same or similar appraisal methods and techniques shall be used in appraising the same or similar kinds of property. However, each property shall be appraised based upon the individual characteristics that affect the property’s market value, and all available evidence that is specific to the value of the property shall be taken into account in determining the property’s market value.” Tex. Tax Code Ann. § 23.01(b).

other property of the same or similar nature. By seeking to impose a different standard in contravention of HCAD's established practices, the Plan Administrator is intentionally putting at issue the uniformity of assessment of taxes. Several courts have held that in instances where the uniformity of local assessment is at issue, it is proper for bankruptcy courts to abstain from hearing the matter. Absent a showing by the Plan Administrator that HCAD did not use the same method for valuing all similar property in Harris County, Harris County asks the Court to abstain from determining these taxes in the interest of preserving uniformity of assessment.

11. Abstention is warranted where the uniformity of assessment is placed in question. In reading the Motion, not only is the valuation of the property put in question but also the underlying methodology applied. It is apparently the Plan Administrator's hope that this Court will not follow Texas law and the appraisal method used by HCAD, but will instead apply some other method which will result in the unequal apportionment of taxes within Harris County. Harris County's property taxation scheme is called into question and, in such cases, abstention is appropriate. "As noted by Harris County, many courts have found abstention to be appropriate when uniformity of assessment is at issue." *In re CM Reed Almeda 1-3062, LLC*, 2016 WL 3563148, at *10. "In the context of section 505, abstention is often used where the uniformity of assessment is an issue." *ANC Rental Corp. v. Dallas County*, 316 B.R. 153, 159 (Bankr. D. Del. 2004); *In re Metromedia Fiber Network*, 299 B.R. 251, 281 - 283 (Bankr.S.D.N.Y. 2003) (fair allocation of the cost of government among the tax base must be a product of local decision making and depends more on uniform standards for assessing value than on an ideal calculation). If the Personal Property is valued using a different method than other

similarly situated property, it could create havoc and set precedent for valuing such property into the future. When a Bankruptcy Court redetermines taxes pursuant to 11 U.S.C. § 505, it must apply substantive applicable non-bankruptcy law. *In re Fairchild Aircraft Corp.*, 124 B.R. 488, 492-93 (Bankr. W.D. Tex. 1991); *Metromedia Fiber Network*, 299 B.R. at 270; *In re CM Reed Almeda 1-3062, LLC* 2016 WL 3563148 at *9 (The Debtor has to show that “its suggested approach to valuation is consistent with Texas law, which the court must apply if it were to consider the 505 Motion”). This encompasses not only the law concerning the method of valuation but also the type of evidence which may be considered. “Each tax authority must enjoy and apply a uniformity of assessment within its tax jurisdiction.” *In re Cable & Wireless U.S.A., Inc.*, 331 B.R. 568, 578 (Bankr. D. Del. 2005).

12. It is clear that where uniformity of assessment is at issue, Bankruptcy Courts may exercise their right to abstain within their discretion. *New Haven Projects Ltd. Liability Co.*, 225 F.3d 283 at 287-88; *Metromedia Fiber Network*, 299 B.R. 251. *See also In re Elantic Telecom, Inc.*, 2005 WL 3781715, Case No. 04-36897-DOT (Bankr. E.D. Va. Dec. 2, 2005)(bankruptcy court abstained in part because tax issue was a local issue better resolved by the state).

13. There are six factors usually considered when determining whether to abstain in a proceeding seeking relief under 11 U.S.C. § 505(a). Those factors are (1) the complexity of the issues to be decided; (2) the need to administer the bankruptcy case in an orderly and efficient manner; (3) the burden on the court’s docket; (4) the length of time which would be required for trial and decision; (5) the asset and liability structure of the debtor; and (6) any prejudice to the debtor and potential prejudice to the taxing

authorities. *New Haven Projects*, 225 F.3d at 289. Each of these factors weighs in favor of the Taxing Authorities.

Factor 1: The complexity of the issues to be decided

14. The issues to be decided are fact specific and involve solely issues of Texas state law. The Taxing Authorities are not the party which sets values and maintains valuation records so evidence on these matters must be sought from HCAD. The Plan Administrator argues that this first factor weighs in favor of the Court exercising jurisdiction because this “Court is routinely called upon to value real and personal property in many different contexts.” Motion at ¶ 15, p. 8. While it is true that bankruptcy courts are routinely called upon to value real and personal property, those are situations where there is no other forum to determine value, i.e. the bankruptcy court is the only forum to value assets for purposes of, for example, 11 U.S.C. § 362 and plan confirmation issues under chapters 11, 12 and 13. Moreover, those are situations without other, controlling, law. In this instance, though, there is a complete statutory framework provided under the Texas Property Tax Code to do the very thing the Plan Administrator is asking this court to do. More importantly, the Debtors claim to have availed themselves of the state law protest procedures by filing their Correction Motion.

Factor 2: The need to administer the bankruptcy case in an orderly and efficient manner

15. The Plan Administrator has not demonstrated that this Court’s determination of the value of the Personal Property is needed for an orderly and efficient administration of the estate. Since the Plan has already been confirmed, there is no pressing need to bring certainty to the amount of property taxes so as to be able to forecast distribution amounts to other creditors. In fact, the asset purchase agreements

for the sale of the Debtors' assets are all dated March 2018. The Plan was confirmed in April 2018. It is evident that if the Plan Administrator truly needed the value of the Personal Property determined, he would not have waited almost a year to seek such relief. Further, the current tax liability for the Personal Property is less than \$350,000.00, which pales in comparison to the over half a billion dollars the Debtors received for the sale of their assets. This fact is further evidence that a determination of the value of the Personal Property is not needed by this Court for an orderly and efficient administration of the estate.

Factors 3 and 4: The burden on the court's docket, and the length of time which would be required for trial and decision

16. Instead of burdening this Court's docket, there already exists a state law forum, which the Plan Administrator has already availed himself of, that could determine the value in an efficient manner. Further, if the Court did not abstain, the Taxing Authorities anticipate that it would need to do discovery not only on the Debtors but also on HCAD. This would ultimately require a trial date well in the future. As the Court noted in *In re CM Reed Almeda 1-3062, LLC*, "because there is a review process available to the Debtor in Texas, 'it seems most appropriate that the debtor in chapter 11 proceed with the systems already in place' for determining its state tax liability, 'rather than substituting this court for that process.' 2016 WL 3563148 at *9 (*quoting In re the Village at Oakwell Farms, Ltd.*, 428 B.R.372, 375 (Bankr.W.D.Tex. 2010)).

Factor 5: The asset and liability structure of the debtor

17. A tax determination by this Court is not essential for the Plan Administrator to discharge his duties under the Plan especially given the asset and liability structure of the Debtors. The taxes owed on the Personal Property currently total

less than \$350,000. As already indicated, the Debtors sold their assets for over half a billion dollars. This is not a case wherein distributions to other creditors is predicated solely on a reduced tax liability.

Factor 6: Prejudice to the debtor and potential prejudice to the taxing authorities

18. There is prejudice to the Taxing Authorities if this court determined the 2018 taxes. There exists a state law procedure and forum for the Debtors to raise valuation issues. The Taxing Authorities are unduly burdened by having to litigate valuation matters, which are far outside its scope of ordinary operations. Moreover, the Taxing Authorities would be forced to defend actions taken by another entity, HCAD. The Plan Administrator argues that if this Court were to abstain from determining the 2018 ad valorem taxes, there would be a detriment to the estates as a result of a gross tax overpayment. There is no prejudice to the Debtors if this Court were to abstain for the simple fact that the Plan Administrator has already taken steps with HCAD to reduce the value on the Personal Property. The case would be different if the Debtors were without a forum where they could obtain review of its assessment.

19. For the foregoing reasons, the Taxing Authorities respectfully request the Court to abstain from determining the 2018 taxes on the Personal Property

B. The Assessed Market Value for the Personal Property Should Not be Reduced Because Fair Market Value Should not Be Based on Auction Value

20. The Plan Administrator correctly argues that all taxable property must be appraised at its market value as of January 1. The cases the Plan Administrator cites do not address property that was being sold as part of a distressed sale, as routinely occurs in bankruptcy cases such as the instant case. In the bankruptcy context, fair market value does not mean fire sale value. In *Cable & Wireless USA, Inc.*, the court stated that “to

use the sale of the assessed property or like property to determine the property's value for tax assessment purposes, the sale must be a normal, fair, arm's-length transaction between parties who are willing, but not forced to sell or buy." 331 B.R. at 579. In the instant case, there certainly were buyers who were not forced to buy but a case can certainly be made that the Debtors were forced to sell. The court further stated that "'Fair Market Value' means neither panic value, auction value, speculative value, nor a value fixed by depressed or inflated prices. In fact, a market may be established only where there are willing sellers and buyers in substantial numbers." *Id.*

1. Memorial City Location

21. It is unclear from the Motion when the Debtors marketed the sale of the Personal Property at the Memorial City Location but several asset purchase agreements were executed in March 2018. The Debtors filed their personal property rendition with HCAD on April 9, 2018 wherein the Debtors listed the estimated value of their Personal Property at \$7,904,885. **HCAD accepted** the \$7.9 value provided by the Debtors and certified the appraisal rolls at that value. Now, almost a year later, the Plan Administrator is asserting that the \$7.9 value – a value that was provided by the Debtors to HCAD – is excessive and should be reduced. Because the Plan Administrator has already filed a Correction Motion with HCAD to address what he perceives to be an excessive valuation, this Court should abstain to allow HCAD to review the evidence and appraise the Personal Property in accordance with their appraisal methodology.

2. Eldridge Location

22. The Plan Administrator states that most of the Personal Property at the Eldridge Location was acquired by Total E&P USA, Inc. and Statoil Gulf of Mexico,

LLC (the “Buyers”). As set forth in the Motion, the asset purchase agreement between the Debtors and the Buyers provides that the Buyers are responsible for the 2018 ad valorem taxes. While the Motion states that the Debtors sold the remaining personal property left at the Eldridge Location, it is unclear if the remaining personal property was of a de minimus amount. Since the bulk of the Personal Property was sold to the Buyers who assumed the 2018 tax liability, this Court should abstain from determining the 2018 tax liability on the basis that most of the benefit from such a reduction would benefit a third party who does not have standing to otherwise protest the value of the Personal Property. *See In re Hinsley*, 69 Fed.Appx. 658 (5th Cir. 2003) (where Trustee abandoned the property prior to the motion for redetermination under 505, it “cannot be said that bankruptcy issues will predominate in the requested valuation” and that the beneficiaries of the reduction of the tax liability is not the estate). Because there would be little to no benefit to the estate, the Court should abstain from determining the 2018 tax liability.

C. Should the Court Decline to Abstain The Motion Should be Continued

23. In the event the Court declines to abstain from hearing the merits of the Motion, the Taxing Authorities request that the hearing on the Motion be continued and that the Plan Administrator be required to make HCAD a party to the Motion. HCAD is a necessary party to this case. The principal function of HCAD under state law is to determine the assessed value of real and personal property. The Taxing Authorities only levy and collect taxes, or issue refunds; they do not value property for tax purposes and have no control over HCAD. The Plan Administrator directly attacks the assessed value of the Personal Property upon which the tax debt was assessed. Any reduction in the assessed value directly impacts the claims of the Taxing Authorities. All evidence

regarding the valuation of the property for the tax year in question, including any self-reporting forms, formal/informal appeals, and agreements as to value is kept and controlled by HCAD. The presence of HCAD is necessary in this case so that it may address the determination of assessed value and to determine whether the Plan Administrator may be granted any of the relief requested. With the involvement of HCAD, a just determination of value can be made in accordance with state law.

RESERVATION OF RIGHTS AND DEFENSES

24. The Taxing Authorities reserve the right to amend its response to the Motion to incorporate any further arguments and/or to assert any defenses.

WHEREFORE, based upon the foregoing, the Taxing Authorities respectfully request the Court to abstain from deciding the merits of the Motion and that it grant the Taxing Authorities such other and further relief, at law or in equity, as is just.

Dated: February 21, 2019

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned does hereby certify that a true and correct copy of the foregoing was served upon the entities listed below by either electronic court filing or by email on February 21, 2019.

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