

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF:)
)
1504 HARNEY ASSOCIATES, L.P.,) CASE NO. BK96-82476
)
DEBTOR) CH. 11

MEMORANDUM

Hearing was held on March 3, 1997, on a motion for relief filed by Firemen's Insurance Company of Newark, New Jersey. Appearances: Robert Gonderinger for the debtor, Alan Solow and Eric Lindquist for Fireman's Insurance Company, and Jerry Jensen for the U.S. Trustee. This memorandum contains findings of fact and conclusions of law required by Fed. Bankr. R. 7052 and Fed. R. Civ. P. 52. This is a core proceeding as defined by 28 U.S.C. § 157(b)(2)(A) and (G).

Background

The Chapter 11 debtor in this case, 1504 Harney Associates, L.P., (the debtor) currently operates the Radisson Redick Tower Hotel (the Hotel) in Omaha, Nebraska. The debtor obtained the real and personal property which constitutes the Hotel on October 1, 1996 from Diversified Historic Investors V (Diversified). The debtor was formed on April 12, 1994 and is a Nebraska Limited Partnership. Diversified is the debtor's general partner and owns 99 percent of the debtor. The remaining one percent is owned by Dover Historic Investors V, the general partner of Diversified.

Firemen's Insurance Company of Newark, New Jersey (Firemen's) holds a mortgage and security interest in the hotel pursuant to a mortgage, assignment of leases and rents, security agreement and fixture financing statement dated November 1, 1994. Firemen's became involved with Diversified in a project involving the Hotel in 1987. The project utilized \$6.5 million of Nebraska Investment Finance Authority (NIFA) bonds, and Firemen's provided a guarantee for a fee of \$800,000. Diversified was the owner of the project and made a cash contribution of approximately \$2 million.

In 1994, Firemen's advanced \$200,000 to cover the costs of refunding the bonds at a lower interest rate, and negotiated the refunding with NIFA using Norwest Bank as bond underwriter. Before the bonds were due to mature on November 1, 1996, Firemen's, Diversified, and Norwest agreed to extend the maturity of the bonds, but NIFA refused. When the bonds matured, Firemen's advanced under its guarantee.

The debtor was created in 1994 when Diversified was involved in the refunding discussions. Diversified believed that the best way to secure alternative financing was to have the hotel operated in a single asset, single purpose entity. According to the debtor, when NIFA refused to extend the maturity of the bonds in 1996, Diversified was required to seek alternative financing, and the property was transferred to the debtor in order to facilitate Diversified's attempt to refinance the bond indebtedness. As a result of the inability to refinance the indebtedness, the debtor filed its petition for reorganization under Chapter 11 on November 4, 1996.

As of the date of filing, the debtor's obligations to Firemen's were in excess of \$6 million. Firemen's has provided evidence from an appraiser that the value of the Hotel is \$3.1 million, and the debtor has provided evidence from an appraiser that the value of the Hotel is \$4 million. In either case, Firemen's is an undersecured creditor.

After the filing of the petition, Firemen's consented to the debtor's use of cash collateral in November and December of 1996, and again in January 1997. However, Firemen's filed its motion for relief from the automatic stay or for dismissal of the case on February 10, 1997.

Decision

As the Hotel is not declining in value and is necessary for an effective reorganization, Firemen's motion for relief from the automatic stay is overruled. In addition, the debtor's petition was not filed in bad faith, and, accordingly, Firemen's motion to dismiss is overruled.

Discussion

Firemen's seeks relief from the automatic stay under both 11 U.S.C. § 362(d)(1) and (d)(2) and also seeks a dismissal of the debtor's case under 11 U.S.C. § 1112(b).

I. Motion for Relief from the Automatic Stay

Section 362(d) provides in part as follows:

(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay --

(1) for cause, including the lack of adequate protection of an interest in property of such party in interest;

(2) with respect to a stay of an act against property under subsection (a) of this section, if --

(A) the debtor does not have an equity in such property; and

(B) such property is not necessary to an effective reorganization . . .

11 U.S.C. § 362(d). Firemen's contends that it is entitled to relief from the stay under § 362(d)(1) because it is not being adequately protected from a threatened decrease in the value of the Hotel. It also contends that it is entitled to relief under § 362(d)(2) because the debtor lacks equity in the property and, as there can be no effective reorganization, the property is not necessary for such a purpose.

A. Lack of Adequate Protection

A secured creditor lacks adequate protection if the value of its collateral is declining as a result of the automatic stay. 11 U.S.C. § 361. Although adequate protection is not defined in the code, section 361 provides three examples of what can constitute adequate protection: periodic payments, replacement liens, or such other relief that is the indubitable equivalent of the creditor's interest. Id.

Although 11 U.S.C. § 362(g)(2) places upon the debtor-in-possession the ultimate burden of proving that the creditor is

being adequately protected, the moving party bears the initial burden of production, and must produce enough evidence to make out a prima facie case before the debtor will be required to rebut the evidence produced and bear the burden of persuasion. Sonnax Indus., Inc. v. TRI Component Products Corp. (In re Sonnax Indus., Inc.), 907 F.2d 1280, 1285 (2d Cir. 1990); In re Eatman, 182 B.R. 386, 390 (Bankr. S.D.N.Y. 1995); In re Elmira Litho, Inc., 174 B.R. 892, 902 (Bankr. S.D.N.Y. 1994); In re Planned Sys., Inc., 78 B.R. 852, 859-60 (Bankr. S.D. Ohio 1987); In re Brown, 78 B.R. 499, 502 (Bankr. S.D. Ohio 1987).

What constitutes a prima facie case for relief from stay turns on the grounds upon which relief from stay is sought. Where, as here, cause for relief from stay is grounded upon an alleged decline in value of the creditor's collateral along with a failure by the debtor to offset such decline by periodic cash payments or some other form of adequate protection, the movant must establish a prima facie case supporting this asserted cause for relief from the automatic stay. Such a prima facie case may include: (1) a showing of an obligation owing by the debtor to the creditor; (2) a valid security interest as to which relief from stay is sought; and (3) the cause justifying relief from stay, in this case a decrease in the value of the [collateral] securing debtor's obligation to the movant combined with the failure on the part of the debtor to provide adequate protection of the movant's interest in the [collateral].

Planned Sys., 78 B.R. at 860.

In this case, there is an obligation owing from the debtor to Firemen's, and Firemen's holds a valid security interest in the property of the debtor. However, while Firemen's has provided evidence as to the value of the collateral at the time of the petition, there is no evidence that the value is in any way declining. In fact, Firemen's appraiser specifically stated in an affidavit that "[t]he value of the Hotel, as is the case with real estate generally, is inherently uncertain. Further, given the particular market conditions involving the Hotel . . . the value of the Hotel is inherently volatile and there is a possible risk of decline in

the value of the Hotel in the foreseeable future." (Emphasis supplied).

Firemen's argues that the mere possibility of a decline in value is enough to require that its interest in the Hotel be adequately protected. However, case law indicates otherwise, and the cases relied on by Firemen's are distinguishable from the case at bar.

In Elmira Litho, the court did state that a creditor, in order to establish a prima facie case under § 362(d)(1), must prove a decline or a threat of decline in the value of its collateral. Id. at 902. However, the court noted that such threats of a decline in value included the failure to maintain property insurance on the collateral or the failure to keep the property in a good state of repair. Id. at 902 n.9. See, In re Pinto, 191 B.R. 610, 612 (Bankr. D.N.J. 1996) (Noting that a threat of decline exists when there is a failure to maintain property insurance or failing to provide for real property taxes); In re Gallegos Research Group, 193 B.R. 577, 584 (Bankr. D. Colo. 1995) (Although the court stated that the measure of adequate protection may be determined by the anticipated decrease in the value of the collateral during the bankruptcy case, the court went on to note that "creditors are entitled to adequate protection only to the extent that the value of the property securing their claim diminishes . . ."); In re Jones, 189 B.R. 13, 15 (Bankr. E.D. Okla. 1995) (Noting that a threat of decline includes failure to maintain property insurance).

These types of threats to the value of a creditor's interest in collateral are serious enough to warrant some form of adequate protection. If a debtor does not pay real estate taxes, the taxing authority may levy on the collateral, thereby reducing the value of the secured creditor's interest. If the debtor does not maintain insurance on the collateral, a calamity could destroy the value of the creditor's interest entirely. However, the mere possibility that the collateral may, at some point, decline in value is not enough of a threat to warrant adequate protection. If such were the case, every creditor holding an interest in property would be entitled to adequate protection, as there almost always will be a threat that given certain circumstances, the value of the property will decline.

The types of legitimate threats described above are not present in this case. Firemen's has not produced any evidence showing that the value of the Hotel is depreciating, that the debtor has failed to pay property taxes or failed to maintain insurance, that the debtor has failed to keep the property in a good state of repair, or "any other facts tending to evidence a lack of adequate protection." Brown, 78 B.R. at 503. Firemen's has thereby failed to establish a prima facie case for a lifting of the stay. Accordingly, Firemen's is not entitled to relief from the stay pursuant to § 362(d)(1).

B. Lack of Equity and Necessary for an Effective Reorganization

"The secured creditor who seeks relief from the automatic stay under § 362(d)(2) must demonstrate (1) the amount of its claim, (2) that its claim is secured by a valid, perfected lien in property of the estate, and (3) that the debtor lacks equity in the property." Elmira Litho, 174 B.R. at 900. Following the establishment of a prima facie case, the debtor must prove that the collateral is necessary for an effective reorganization or rebut the evidence presented by the moving party. Id. at 901.

In this case, Firemen's has made out a prima facie case. Accordingly, the debtor must show that the collateral is necessary to an effective reorganization.

What this requires is not merely a showing that if there is conceivably to be an effective reorganization, this property will be needed for it; but that the property is essential for an effective reorganization that is in prospect. This means . . . that there must be "a reasonable possibility of a successful reorganization within a reasonable time."

United Savings Ass'n v. Timbers of Inwood Forest Assoc., Ltd., 484 U.S. 365, 375-76, 108 S. Ct. 626, 632, 98 L. Ed. 2d 740 (1988).

From the evidence presented at the hearing on this motion, and from a review of the case file, it is apparent that there is a reasonable possibility of a reorganization within a reasonable time. The debtor has already filed both a disclosure statement and a plan of reorganization. The plan

calls for, among other things, a cash infusion of approximately \$1 million by Diversified.

Firemen's has objected to this plan, arguing that it violates that absolute priority rule of 11 U.S.C. § 1129(b)(2)(B) and that there is no Eighth Circuit authority for the type of "new value" plan proposed by the debtor. However, there is such authority. See, Anderson v. Farm Credit Bank (In re Anderson), 913 F.2d 530 (8th Cir. 1990); In re Kramer, 96 B.R. 972 (Bankr. D. Neb. 1989).

As there is a reasonable possibility of a reorganization within a reasonable time, and it is clear that there can be no reorganization without the Hotel, Firemen's is not entitled to relief from the stay pursuant to § 362(d)(2).

II. Motion to Dismiss

Firemen's has moved to dismiss this case pursuant to 11 U.S.C. § 1112(b). That section provides in part:

Except as provided in subsection (c) of this section, on request of a party in interest . . . and after notice and a hearing, the court may convert a case under this chapter to a case under chapter 7 of this title or may dismiss a case under this chapter, whichever is in the best interest of creditors and the estate, for cause . . .

11 U.S.C. § 1112(b). The section goes on to provide a nonexclusive list of ten factors which constitute cause. Although bad faith is not one of the enumerated factors, a court may dismiss a case for cause if the court finds that the debtor has filed its Chapter 11 petition in bad faith. First Nat'l Bank v. Kerr, 908 F.2d 400 (8th Cir. 1990).

The Eighth Circuit has stated that before a case may be dismissed for bad faith pursuant to § 1112(b), there must be a pattern of concealment, evasion, and direct violations of the Bankruptcy Code or court order which clearly establishes an improper motive. Id. at 404. No such conduct is present in this case, let alone a pattern of it. Accordingly, dismissal of this case is unwarranted.

Separate journal entry to be entered.

DATED: March 28, 1997

BY THE COURT:

/s/ Timothy J. Mahoney
Timothy J. Mahoney
Chief Judge

Copies faxed by the Court to:

GONDERINGER, ROBERT 390-9221
LINDQUIST, ERIC 392-0816

Copies mailed by the Court to:

Alan Solow, Esq., 55 East Monroe St., Suite 3700,
Chicago, IL 60603
United States Trustee

Movant (*) is responsible for giving notice of this journal entry to all other parties (that are not listed above) if required by rule or statute.

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FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF:)	
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1504 HARNEY ASSOCIATES, L.P.,)	CASE NO. BK96-82476
)	A
<u>DEBTOR(S)</u>)	CH. 11
)	Filing No. 66, 85
Plaintiff(s))	
vs.)	<u>JOURNAL ENTRY</u>
)	DATE: March 28, 1997
<u>Defendant(s)</u>)	HEARING DATE: March 3,
)	1997

Before a United States Bankruptcy Judge for the District of Nebraska regarding Motion for Relief filed by Firemen's Insurance Company of Newark, New Jersey; Resistance by Debtor.

APPEARANCES

Robert Gonderinger, Attorney for debtor
Alan Solow and Eric Lindquist, Attorneys for Firemen's Insurance Company
Jerry Jensen, Attorney for U.S. Trustee

IT IS ORDERED:

Motion for relief from automatic stay and motion to dismiss are denied. See memorandum entered this date.

BY THE COURT:

/s/ Timothy J. Mahoney
Timothy J. Mahoney
Chief Judge

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