IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEBRASKA

IN RE:	)	BK 84-542
	)	
JERRY L. STEVENS and	)	BK 84-0-412
CYNTHIA J. STEVENS,	)	
	)	
	)	ORDER
Debtor.	)	

This matter is before the Court on appeal from a final order of the Bankruptcy Court, dated June 14, 1984, sustaining appellee's request for relief from the automatic stay in appellants' Chapter 11 proceeding. Relief was granted with regard to the following property: one, 1288' Model 2071 Electric Valley Center Pivot Irrigation System, and 3300 feet of 8 inch Kroy pipe.

Debtor-appellants are Chapter 11 farmers in possession of the irrigation equipment listed above. They acquired possession of this equipment from creditor-appellee, Trans Union Leasing Corporation (Trans Union), by executing an agreement on June 28, 1976, which purports on its face to be a 126 month lease. Debtors allegedly defaulted on the agreed payments. Thereafter, on or about September 19, 1983, Trans Union filed a replevin action in state district court for recovery of the equipment. Following a replevin hearing on December 8, 1983, the district court held that Trans Union was entitled to possession pending trial on the merits.

On March 19, 1984, prior to levy on the property, debtors filed for bankruptcy under Chapter 11, seeking to reorganize their farming business. Thereafter, on May 16, 1984, Trans Union filed a complaint for relief from the automatic stay, alleging inter

alia that the debtors have no equity or interest in the equipment other than mere possession. Attached to its complaint were copies of the lease, state court petition and an affidavit in replevin.

The Bankruptcy Court set the matter for hearing and ordered that evidence be presented by affidavits. At the hearing on June 12, 1984, Trans Union offered in support of its motion an order of replevin signed by the Judge of the District Court of Perkins County, Nebraska, which granted possession of the equipment to Trans Union pending trial. Trans Union argued that, "This is a mere lease situation, the debtors having no equity or ownership interest, . . . Trans Union's interests are not being adequately protected due to the large arrearages and lack of any payments." Record at 2-3. In opposition to the motion, debtors offered their personal affidavits,[1] an affidavit of Dean Knaub[2] (owner of a center pivot irrigation systems business), and a certified copy of the order of replevin, issued December 9, 1983. Debtors argued that Trans Union had failed to prove (1) that it was entitled to

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[1] In his affidavit, debtor Jerry Stevens states inter alia that (1) he is the owner of the irrigation equipment, having purchased the pivot for $29,700.00 and the pipe for $5,610.00 from Trans Union on Jure 28, 1976, (2) the equipment is necessary to permit an effective reorganization, (3) he has maintained the equipment in good operating condition and will continue to do so, (4) the maximum decrease in value of the equipment is $300.00 per year, and (5) he is willing to make installments to cover any reduction in value.

[2] The affidavit of Dean Knaub states that the present value of the equipment totals approximately $14,000.00 and that the equipment would decrease in value approximately $300.00 per year for the next 8 years.

relief "simply by the introduction of the court order of replevin," or (2) that this was a mere lease situation. Record at 7.

At the close of arguments, the Bankruptcy Court sustained Trans Union's motion for relief, stating:

> The order for replevin signifies that the moving party, Trans Union Leasing, has a special property interest in this equipment as opposed to a general unsecured creditor who has no special property interest in any specific property, and the specific property is held by the debtor under lease and not claim, I gather, of ownership.

Record at 8. With reference to the debtors' offer to make payments to cover any reduction in value, the Court stated, "[The lessor's] hope of some time in the future receiving adequate protection is not the same thing as required by the statute which requires that the adequate protection be present now. It is not, in my view. The motion is sustained." Id.

DISCUSSION

On appeal, the Bankruptcy Court's findings of fact are not to be set aside unless clearly erroneous. The district court is not bound, however, by the Bankruptcy Court's conclusion of law. See Matter of American Beef Packers, Inc., 457 F. Supp. 313 (D. Neb. 1978); Bankr. Rule 8013, U.S.C.A. (West 1984).

On appeal, debtors argue that the Bankruptcy Court erred in sustaining Trans Union's motion for relief from the automatic stay. Specifically, they raise the following three issues: (1) whether the Bankruptcy Court committed procedural error by limiting the admission of evidence at the hearing to affidavits;

(2) whether the Bankruptcy Court erred in finding that debtors had no equity in the equipment, i.e., that the equipment was held under lease and not sale; and (3) whether debtors made a sufficient showing that the equipment was necessary to an effective reorganization and that Trans Union was adequately protected.

I.

With regard to debtors' first assignment of error, the Court finds that no procedural error was committed. Bankruptcy Rule 9017, 11 U.S.C., provides, "The Federal Rules of Evidence and Rules 43, 44 and 44.1 F.R.Civ.P. apply in cases under the Code." Applicable here is Rule 43(e), which provides:

> (e) Evidence on Motions. When a motion is based on facts not appearing of record the court may hear the matter on affidavits presented by the respective parties, but the court may direct that the matter be heard wholly or partly on oral testimony or deposition.

Fed. R. Civ. P. 43(e) (Emphasis added).

The Bankruptcy Court clearly had the authority to hear this matter by affidavit, pursuant to Rule 43(e). While debtors had a right to be heard, see Bankruptcy Rules 4001 and 9014, they were not necessarily entitled to present oral testimony at the hearing. See World Brilliance Corp. v. Bethlehem Steel Co., 342 F.2d 362, 366 (2d Cir. 1965).

II.

With reference to debtors' second and third assignments of error, the Court looks to 11 U.S.C. § 362(d), which governs relief from the automatic stay:

> (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; or
>
> (2) with respect to a stay of an act against property, 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).

> For the purposes of determining relief from stay matters, the two tests provided for in § 362(d)(1) and (2) are alternative tests, and . . . a party need establish only one of the alternatives to support its claim for relief. Once a secured creditor has proven the debtor's lack of equity in the property, and the debtor has failed to prove necessity of the property for an effective plan, relief may be granted without any requirement that other cause, such as lack of adequate protection, be established by the creditor. If the debtor seeks to prove that adequate protection has been or can be afforded the secured creditor, the debtor must also allege and establish reasons why that being true, the court should deny relief from stay.

First Connecticut Small Business Investment Co. v. Ruark, 7 B.R. 46, 49 (Bankr. D. Conn. 1980). Accord, In Re Olson, No. 84-0-440, slip op. at 5 (D. Neb.. Mar. 1, 1985).

Under 11 U.S.C. § 362(g), Trans Union has the burden of proving that debtors have no equity in the equipment in question and debtors bear the burden of proof with regard to establishing the necessity of the equipment to an effective reorganization.

Debtors' second assignment of error is that the Bankruptcy Court erred in finding that they had no equity in the equipment, i.e., that the property was held under lease and not sale. Whether the transaction here actually constituted a lease or a security interest under the Bankruptcy Code depends upon applicable state or local law. In re Francis, 42 B.R. 763, 765 (Bank. E.D. Mo. 1984); Matter of Elliott, 18 B.R. 602, 603 (Bankr. D. Neb. 1982).

Section 1-201(37) of the Nebraska Uniform Commercial Code defines "security interest" as:

> [A]n interest in personal property . . . which secures payment or performance of an obligation. . . . Unless a lease . . . is intended as security, reservation of title thereunder is not a 'security interest' . . . . Whether a lease is intended as security is to be determined by the facts of each case; however, (a) the inclusion of an option to purchase does not of itself make the lease one intended for security, and (b) an agreement that upon compliance with the terms of the lease the lessee shall become or has the option to become the owner of the property for no additional consideration or for a nominal consideration does make the lease one intended for security.

Neb. Rev. Stat. U.C.C. § 1-207(37) (Reissue 1980) (emphasis added). See Gibreal Auto Sales, Inc. v. Missouri Valley Machinery Co., 186 Neb. 763, 186 N.W.2d 719, 721 (1971). As correctly noted by the Bankruptcy Court in Matter of Elliott, 18 B.R. at 604,

> The intent to which U.C.C. § 1-201(37) refers is of the objective and not the subjective variety, with a possible exception where both parties subjectively intended the lease as security. Neither the presence nor the absence of the option to purchase is conclusive, except with respect to the type of option described in clause (b). Ibid., p.2. See also 1 Gilmore, Security Interests in Personal Property, § 11.2, pp. 338-9.

To determine the objective intent of the parties, the Court must look to the content of the document and to the factual setting of the transaction, as well as to the subsequent treatment of the agreement by the parties. See In Re Air Vermont, Inc., 44 B.R. 440, 443 (Bankr. D. Vt. 1984), and cases cited therein. Factors considered by courts of other jurisdiction include whether

> (a) the lessor is merely a seller or financier in 'lessor's clothing';
> (b) the lease period approximates the useful life of the property leased;
> (c) the aggregate rentals called for under the purported lease far exceed the original value of the property;
> . . .
> (e) the lessee assumes most or all of the legal incidents of ownership (payment of taxes, bearing risk of loss or damage to the property, etc.), and
> (f) the lessor, upon default, has the right to accelerate all future rentals due under the agreement.

In re Francis, 42 B.R. at 765.

Based upon the record before this Court, it appears that the Bankruptcy Court relied primarily, if not solely, upon the state court order of replevin in concluding that the transaction here was a lease and that debtors had no equity. The Bankruptcy Court made no reference to the fact that such order was merely a preliminary order of possession pending trial on the merits. The Court also made no reference to the facts surrounding the transaction, the subsequent treatment of the agreement by the parties, the terms of the purported lease or the debtors' claim of purchase.

The record here is insufficient to support the Bankruptcy Court's conclusion that this was a mere lease situation and that debtors had no equity. This Court must, therefore, conclude that the Bankruptcy Court erred in so finding. This Court expresses no opinion, however, as to whether the transaction was in fact a lease or a sale. That determination is for the Bankruptcy Court to decide on remand.

III.

In addition to the issue of equity, on remand the Bankruptcy Court must consider whether the equipment in this instance is necessary to debtors' effective reorganization.

As previously noted, debtors have the burden of proof on this issue. See 11 U.S.C. § 362(g). Inherent in debtors' burden of proof is the need to establish that reorganization is feasible. See, e.g., In re Clemmons, 37 B.R. 712, 719 (Bankr. W.D. Mo. 1984); In re Besler, 19 B.R. 879, 884 (Bankr. D. S.D. 1982);

Matter of Terra Mar Associates, 3 B.R. 462, 464 (Bankr. D. Conn. 1980). However, a debtor's bare assertion that the subject property is necessary to survival, without more, is insufficient to carry that burden. Matter of Discount Wallpaper Center, Inc., 19 B.R. 221, 222 (Bankr. M.D. Fla. 1982).

The Court notes that in In Re Francis, 42 B.R. 763, 767 (Bankr. E.D. Mo. 1984), the bankruptcy court considered a similar situation involving a purported lease of irrigation equipment and a debtor's claim that such equipment was necessary to an effective Chapter 11 reorganization of his farming business. In that case the court concluded that the equipment was necessary for an effective reorganization and that section 362(d)(2), being in the disjunctive, provided no basis for relief from the automatic stay.

Whether or not the irrigation equipment in the present case is necessary to debtors' effective reorganization is a question, in the first instance, for the Bankruptcy Court to make. There being no reference to the necessity of this equipment by the Court on the record, this issue is also remanded for the Bankruptcy Court's determination.

Accordingly,

IT IS ORDERED that the Bankruptcy Court's order of June 14, 1984, sustaining appellee's request for relief from the automatic stay, is reversed and the case is hereby remanded to the Bankruptcy Court for further proceedings in accordance with this Memorandum.

DATED this 13th day of March, 1985.

BY THE COURT:

C. Arlen Beam

C. ARLEN BEAM
UNITED STATES DISTRICT JUDGE