

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEBRASKA

IN RE:)
)
JERRY DIBBERN and VERNA DIBBERN,)
)
Debtors.)

BK 84-1701
CV 85-0-747

ORDER

FILED
DISTRICT OF NEBRASKA

JUN 5 1986

William L. Olson, Clerk

By _____ Deputy

This matter is before the Court on appeal from an order of the United States Bankruptcy Court for the District of Nebraska entered on July 3, 1985. The Bankruptcy Court found that the Federal Land Bank's interest was not adequately protected as required under 11 U.S.C. § 363. The Bankruptcy Court held that the debtors-in-possession should be prohibited from using two tracts of land that serve as collateral until they provided the Federal Land Bank with one or more forms of adequate protection as provided by 11 U.S.C. § 361 in an amount equivalent to the decline in the value of the collateral, or \$191,805.00.

FACTS

The essential facts of this appeal are not in dispute. The appellants (debtors) are husband and wife and are debtors-in-possession under a Chapter 11 proceeding filed June 19, 1984. The debtors operate a grain farm and cattle feeding operation in Wood River, Nebraska.

On August 24, 1979, the debtors borrowed \$526,700.00 from the Federal Land Bank of Omaha (Bank) secured by a mortgage on a 160-acre tract (Tract 1). On May 19, 1980, debtors borrowed \$602,600.00 from the same institution secured by a mortgage on a separate 300-acre tract (Tract 2). On the date of Bankruptcy filing there was due to the Bank on Tract 1 the sum of \$623,769..

with interest accruing at \$235.19 per day, and on Tract 2 the sum of \$646,420.02 with interest accruing at \$210.17 per day. No payments on these notes have been made since the date of filing.

- On or about January 15, 1985, pursuant to 11 U.S.C. § 363(e) the Bank filed a motion to prohibit debtors from using the collateral described as Tract 1 and Tract 2. The Federal Land Bank did not file a request for relief from the stay pursuant to 11 U.S.C. § 362. The debtors filed a plan and disclosure statement. The Bank objected to the disclosure statement. The Bank's objection was sustained with leave to file an amended disclosure statement. The Bank is the only significant creditor in these proceedings.

On the date of filing, June 19, 1984, the value of Tract 1 was \$640,200.00. The Federal Land Bank debt was \$623,769.55. On the date of filing the value of Tract 2 was \$510,510.00 and the debt was \$646,420.02. On the day of the hearing, the value of Tract 1 was \$524,342.00 and the value of Tract 2 was \$418,312.00. The value of the Federal Land Bank collateral declined from June, 1984, to June, 1985.

The decline in value of the Federal Land Bank's interest in Tract 1 was \$99,427.00, the difference between the debt on date of filing and the land value on date of hearing. The debt on date of filing was \$623,769.55 and the land value on the date of hearing was \$524,342.00.

The Bankruptcy Court found that since the Federal Land Bank was undersecured on Tract 2 on the date of filing, the interest which the Federal Land Bank has a right to be protected was the difference between its maximum allowable secured claim (which is equal to the land value for Tract 2 on date of filing), \$510,510.00 and the land value on date of hearing \$418,132.00. This decline in value is \$92,368.00.

The Bankruptcy Court found the total protectible decline in value from date of filing to be \$191,805.00. The Bankruptcy Court found that the value of collateral would continue to decline during the 1985 crop year.

After a review of the facts and applicable law, the Court finds the order of the Bankruptcy Court should be reversed and the case remanded for further proceedings.

DISCUSSION

The purposes of a business reorganization under Chapter 11 are to "relieve the debtor of its prepetition debts, to free cash flow to meet current operating expenses, and ultimately to permit the debtor 'to restructure a businesses' finances so that it may continue to operate, provide its employees with jobs, pay its creditors, and product a return for its stockholders.'" In re Martin, 761 F.2d 472, 475 (8th Cir. 1985) quoting In re American Mariner Industries, Inc., 734 F.2d 426, 431 (9th Cir. 1984) quoting H.R. Rep. No. 595 at 220, 1978 U.S. Code Cong. & Ad. News at 6179. The filing of a petition in Chapter 11 "operates as an automatic stay, which prevents creditors from enforcing their

liens against the property of the Bankruptcy estate and removing collateral that may be essential to the reorganization plan. 11 U.S.C. § 362(a)." In re Martin, 761 F.2d at 475.

The Bank in this instance moved for adequate protection under 11 U.S.C. § 363(e). That statute provides:

Notwithstanding any other provision of this section, at any time, on request of an entity that has an interest in property used, sold, or leased, or proposed to be used, sold, or leased, by the trustee, the court shall prohibit or condition such use, sale, or lease as is necessary to provide adequate protection of such interest. In any hearing under this section, the trustee has the burden of proof on the issue of adequate protection.

11 U.S.C. § 363(e).

In In re Martin, 761 F.2d at 474, the Eighth Circuit discussed the concept of adequate protection as that term is used in the Bankruptcy Code. The Court wrote:

The concept of adequate protection was designed to 'insure that the secured creditor receives the value for which he bargained.' S. Rep. No. 989, 95th Cong., 2d Sess. 53, reprinted in 1978 U.S. Code Cong. & Ad. News 5787, 5839 (Emphasis added); see also H.R. Rep. No. 595, 95th Cong., 2d Sess. 339, reprinted in 1978 U.S. Code Cong. & Ad. News 5963, 6295. Congress explicitly stated that value was to be considered a flexible concept 'to permit the courts to adapt to varying circumstances and changing modes of financing' and that such matters '[to be] left to case-by-case interpretation and development.' H.R. Rep. No. 595 at 339, 1978 U.S. Code Cong. & Ad. News at 6295; see also S. Rep. News No. 989 at 54, 1978 U.S. Code Cong. & Ad. News at 5840. Because Congress intended that value was to be determined on a case-by-case basis, that which is designed to protect value, i.e., adequate protection, must also be determined on a case-by-case basis, permitting the debtors maximum flexibility in structuring a

proposal for adequate protection. In re
American Mariner Industries, Inc., 734 F.2d
426, 435 (9th Cir. 1984).

Id. at 474.

- In determining the kind and quantity of adequate protection to be afforded the Bank, the Court must be mindful that the Bank sought adequate protection under 11 U.S.C. § 363, not 11 U.S.C. § 362 which concerns granting relief from the automatic stay in order to effect foreclosure.

Section 363 is most often used to provide adequate protection for the use of cash collateral, inventory or personal property, not real property. Section 362 generally is used to provide adequate protection for a creditor's interest in real property.

Section 363 functions to protect a creditor's interest that may be impaired through the use [emphasis added] of the collateral. See 11 U.S.C. § 363. See, e.g., In re Bermac, 445 F.2d 367 (3d Cir. 1971); In re Yale Express Systems, Inc., 384 F.2d 990 (2d Cir. 1967); H.R. Rep. No. 95-595, at 339-340, 1978 U.S. Code Cong. & Ad. News 6296; S. Rep. 95-989, 1976 U.S. Code Cong. & Ad. News 5840 (concept exposed in In re Bermac and In re Yale Express Systems, Inc. codified in Bankruptcy Code). It is Section 362 that protects the creditor from damage incurred by the stay preventing the creditor from foreclosing on the collateral. 11 U.S.C. §§ 361(1) and 362.

The evidence presented to the Bankruptcy Court focused on the diminution of value due to economic circumstances as opposed to any deterioration caused by use. No cases have been found that

allow a creditor to proceed under section 363(e) for adequate protection for diminution of the value of real property collateral due to economic circumstances as opposed to protection for the use of the property. This is not the proper use of 11 U.S.C. § 363(e). The use by the debtors, i.e., cultivation of the land, resulted in little, if any, identifiable loss. The decline in value was caused by economic factors during the imposition of the 11 U.S.C. § 362 stay. 11 U.S.C. § 361(1) clearly delineates that adequate protection must be offered to the extent that the "stay" under Section 362 affects value. As a practical matter, to determine that a creditor is entitled to adequate protection under Section 363 for the use of land in an amount equivalent to the economic depreciation of the land values from the time of filing the petition to the date of the hearing in Bankruptcy Court would most often paralyze the effort to reorganize, as in this case. Therefore, the Bank in order to protect its interest in the land should have proceeded under 11 U.S.C. § 362.¹

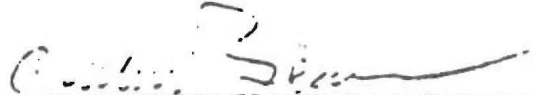
Accordingly,

IT IS ORDERED that the order of the Bankruptcy Court should be and hereby is reversed and the case is remanded for further proceedings consistent with this opinion.

DATED this 5th day of ~~May~~
June, 1986.

¹ See *In re Briggs Transportation Co.*, 780 F.2d 1339 (8th Cir. 1985) (recent discussion of concept of adequate protection and the concept of the benefit of the bargain).

BY THE COURT:


C. ARLEN BEAM, CHIEF JUDGE
UNITED STATES DISTRICT COURT