

Distressed Real Estate and Bankruptcy



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Distressed Real Estate and Bankruptcy

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GOOD FAITH AND REAL ESTATE
CHAPTER 11 CASES

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I. Dismissal for the Lack of Good Faith

A. Bankruptcy Code Section 1112(b)(1) and the Good Faith Test



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B. Objective-Subjective Test is Employed to Determine Bad Faith

United States Court of Appeals for the Second Circuit case

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C. *Single Asset Bad Faith Cases*

The following are *indicia of bad faith*:

- The debtor has a single asset;
- The debtor has few unsecured creditors;
- The debtor's asset is in foreclosure;
- The Chapter 11 case is a two-party dispute;

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D. The Creditor's Ability to Block Any Plan Indicates a Bad Faith Filing

In order to confirm a plan of reorganization that is not 100% there must be at least one impaired class that votes in favor of the plan of reorganization. 11 U.S.C. § 1129(a)(10).

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E. The New Debtor Syndrome

The new debtor syndrome is when assets are transferred to a new entity on the eve of bankruptcy so that the new entity can file and obtain the benefit of the automatic stay.

Indicia of the new debtor syndrome.

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F. Serial Chapter 11 Cases

Serial Chapter 11 cases are multiple Chapter 11 cases. In Northtown Realty Co., L.P., 215 B.R. 906 (Bankr. E.D.N.Y. 1998) the late Chief Judge Duberstein dismissed a Chapter 11 case. The court thought that under Bankruptcy Code Section 1127 it was impermissible to modify a substantially consummated plan of reorganization.

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G. Dissolved Corporations and Partnerships

If a dissolved corporation files for Chapter 11, then the Chapter 11 case can be dismissed for bad faith. *In re Cinole, Inc.*, 339 B.R. 40 (Bankr. W.D.N.Y. 2006). *In Cinole the court dismissed the debtor's Chapter 11 case because of bad faith.*

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H. Summary

A threshold issue that must be addressed is whether the Chapter 11 case was filed in good faith. The related question is whether the debtor has the ability to confirm a plan of reorganization.

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BANKRUPTCY AND REAL ESTATE: THE USE OF CASH COLLATERAL



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I. **Definition of Cash Collateral**

Bankruptcy Code Section 363(a) defines “cash collateral” as follows:

In this section, "cash collateral" means cash, negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents whenever acquired in which the estate and an entity other than the estate have an interest

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II. Use of Cash Collateral

Bankruptcy Code Section 363(c)(2) governs the use of “cash collateral” and states:

The trustee may not use, sell, or lease cash collateral under paragraph (1) of this subsection unless--

(A) each entity that has an interest in such cash collateral consents; or

(B) the court, after notice and a hearing, authorizes such use, sale, or lease in accordance with the provisions of this section.

11 U.S.C. § 363(c)(2).

Adequate Protection And The Use of Cash Collateral

Bankruptcy Code Section 363(e) authorizes a bankruptcy court to permit the use of cash collateral if the secured creditor is adequately protected. 11 U.S.C. § 363(e).

Determination of Secured Status

Under *Butner v. U.S.*, 440 U.S. 48 (1979) property rights in bankruptcy cases are determined by nonbankruptcy law. The Supreme Court has stated:

Property interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding.

Cash Collateral Decisions

A pertinent case is *In re Miller*, 133 B.R. 882 (Bankr. N.D. Ohio 1991). There, the court ruled that the debtor was not entitled to use cash collateral because there was not an agreement between the debtor and mortgagee and there was no court approval for the use of cash collateral.

Procedure for Using Cash Collateral

Federal Rule of Bankruptcy Procedure 4001(c) governs the procedure for obtaining cash collateral orders.

SINGLE ASSET REAL ESTATE
CASES AND CHAPTER 11



Definition of Single Asset Real Estate Case

Bankruptcy Code Section 101(51B)

Bankruptcy Code Section 101(51B) defines a single asset real estate case.

II. Bankruptcy Code Section 362(d)(3) and Single Asset Real Estate Cases

A. Cases Interpreting Bankruptcy Code Section 362(a)(3)

**SERIAL BANKRUPTCY FILERS
AND THE AUTOMATIC STAY
IN REAL ESTATE BANKRUPTCY CASES**



The Scope of the Automatic Stay

A. Bankruptcy Code Section 362(a)

Bankruptcy Code Section 362(a) sets forth the acts that are stayed when a bankruptcy petition is filed. 11 U.S.C. § 362(a).

The Scope of the Automatic Stay and Real Estate

Any recognizable interest of the estate will be afforded protection by the automatic stay.

In re Reinhardt, 209 B.R. 183, 185 (Bankr. S.D.N.Y. 1997). The automatic stay should be interpreted broadly. *In re Draper*, 237 B.R. 502, 505 (Bankr. M.D. Fla. 1999).

The Co-Debtor Stay and Bankruptcy Code Section 362(c)(3)

Bankruptcy Code Section 1301(a) provides for a co-debtor stay for individuals that have guaranteed a consumer debt of a Chapter 13 debtor. 11 U.S.C. § 1301(a). Bankruptcy Code Section 362(c)(3) has no impact on the co-debtor stay. *In re Lemma*, 393 B.R. 299, 304 (Bankr. E.D.N.Y. 2008).

Bankruptcy Code Section 105(a) and a Discretionary Stay

Some courts have held that Bankruptcy Code Section 105(a), the “all writs” statute, can be employed to issue a discretionary stay if a debtor fails to obtain the adjudication of its Bankruptcy Code Section 362(c)(3) within the applicable 30-day period. *In re Franzese*, 2007 B.R. 2083650 (Bankr. S.D.Fla. 2007).

Bankruptcy Code Section 362(c)(4)

Bankruptcy Code Section 362(c)(4) governs automatic stay in bankruptcy cases in which the debtor has had two cases dismissed within the last year.

**BANKRUPTCY CODE SECTION 362(d):
MODIFICATION OF THE AUTOMATIC
STAY IN BANKRUPTCY REAL
ESTATE CASES**



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I. *Introduction to Bankruptcy Code Section 362(d)*

A mortgagee will seek to modify the automatic stay so that it can either commence or continue with its foreclosure proceeding. Bankruptcy Code Section 362(d) governs modification of the automatic stay. 11 U.S.C. §362(d).



362(d)(1): Modification of the Automatic Stay for Cause

A. Bad Faith

Bankruptcy Code Section 362(d)(1) provides that the automatic stay may be modified for “cause.” 11 U.S.C. § 362(d)(1). Bankruptcy Code Section 362(d)(1) does not define what constitutes “cause.” *In re Ridge View Farm, LLC*, 2012 WL 6137690 at 7 (Bankr.N.D.N.Y. 2012).

Bankruptcy Code Section 362(d)(2)

Under Bankruptcy Code Section 362(d)(2), both prongs of the statute must be satisfied before the stay will be modified. *In re YL West 87th Holdings I LLC*, 423 B.R. 421, 427 (Bankr. S.D.N.Y. 2010). Bankruptcy Code Section 362(g) places the burden of proof on the issue of the lack of equity on the movant, and the burden of proof on all the other issues is placed on the party opposing relief. 11 U.S.C. § 362(g).

Bankruptcy Code Section 362(d)(4): In Rem Relief

An important Bankruptcy Code provision that was intended to combat abusive serial bankruptcy filings is Bankruptcy Code Section 362(d)(4). *In re Blair*, 2009 WL 5203738 at 4 (Bankr. E.D.N.Y. 2009). Bankruptcy Code Section 364(d)(4) authorizes *in rem* relief. 11 U.S.C. § 362(d)(4).

**BANKRUPTCY CODE SECTION 364(d):
POST-PETITION FINANCING IN REAL
ESTATE BANKRUPTCY CASES**

Introduction to Bankruptcy Code Section 364

Bankruptcy Code Section 364 governs the issuance of credit to a debtor-in-possession.

11 U.S.C. §§ 364(c) & (d).

Bankruptcy Code Section 364(c)

Bankruptcy Code Section 364(c)(1) authorizes a debtor-in-possession to incur debt on a super-priority basis with priority over all administrative and super priority debt. 11 U.S.C. § 362(c)(1). Bankruptcy Code Section 364(c)(2) authorizes the granting of a lien on unencumbered property to secure post-petition financing. 11 U.S.C. § 362(c)(2).

Bankruptcy Code Section 364(d)(4) and Super Priority Liens

Introduction to Bankruptcy Code Section 364(d)(4)

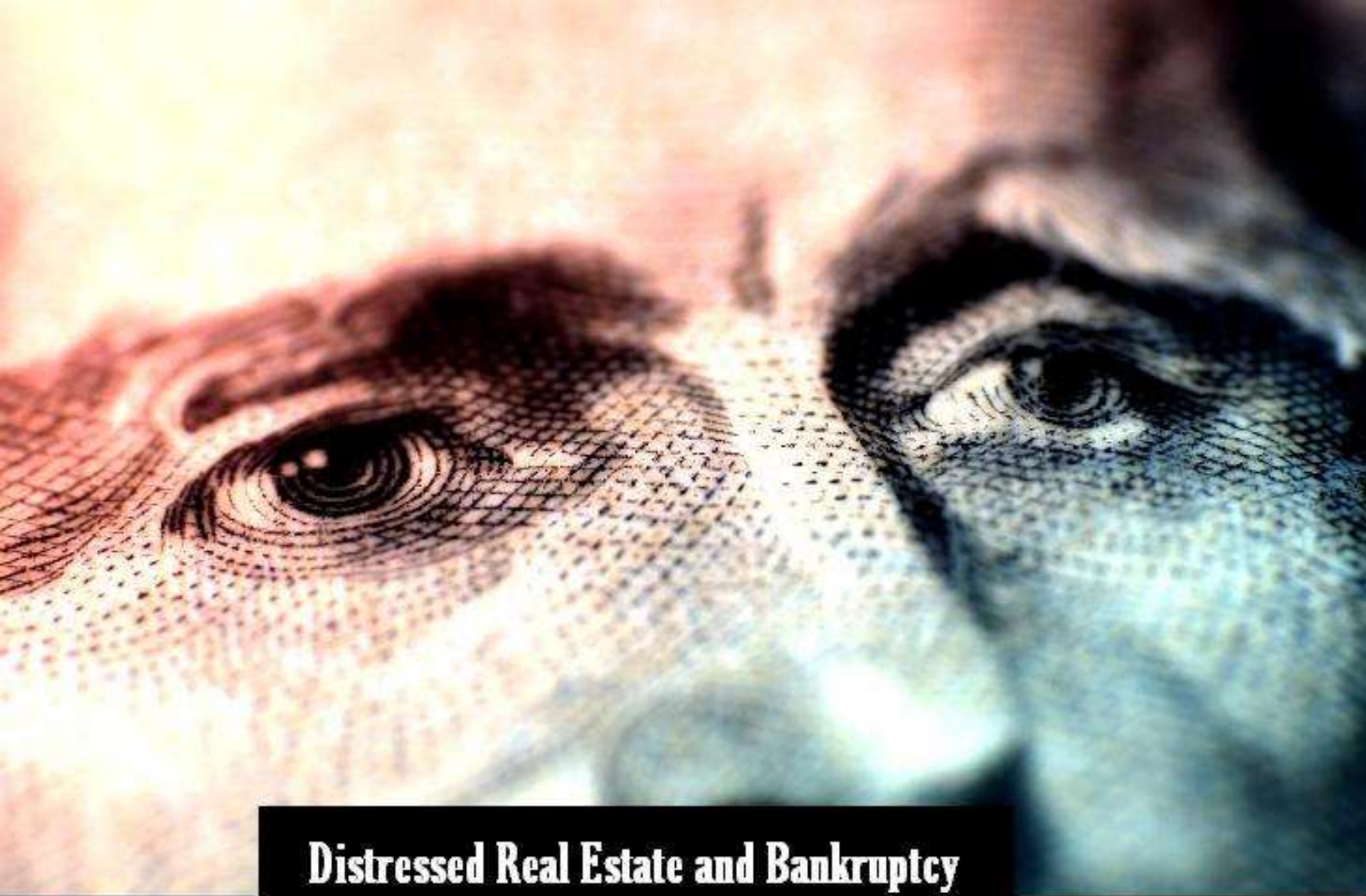
Bankruptcy Code Section 364(e): Safe Harbor for Good Faith Lenders

Bankruptcy Code Section 364(e) protects post-petition lenders who have extended credit in good faith.

(e) The reversal or modification on appeal of an authorization under this section to obtain credit or incur debt, or of a grant under this section of a priority or a lien, does not affect the validity of any debt so incurred, or any priority or lien so granted, to an entity that extended such credit in good faith, whether or not such entity knew of the pendency of the appeal, unless such authorization and the incurring of such debt, or the granting of such priority or lien, were stayed pending appeal. 11 U.S.C. § 364(e).

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V. *The Procedure for Obtaining Credit:* **Federal Rule of Bankruptcy Procedure** **4001(c)**



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