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Obtaining Adequate Protection: An Analysis Pertaining to Real Estate Projects

BY J. ERIC WISE AND MATTHEW K. KELSEY

This article discusses adequate protection in the context of partially completed real estate projects. In particular, we consider whether and to what extent the increase in value of a prepetition secured creditor's collateral that results from further construction, or the completion of construction, may be a potential source of value for a debtor attempting to rehabilitate its business while in Chapter 11. If postpetition accretion in the value of the project can be a source for adequate protection of the prepetition secured creditor, the debtor could use this value to support the debtor's use of cash collateral, obtaining priming postpetition financing under sections 363 or 364(d) of the Bankruptcy Code, or the continued imposition of the automatic stay under section 362 of the Bankruptcy Code.

A. What is Adequate Protection?

To understand adequate protection in the narrow context of a real estate project, it will be helpful to first look at adequate protection broadly. At the outset of most Chapter 11 cases, secured creditors focus their attention on obtaining adequate protection against the diminution in value of their collateral resulting from the debtor's use of that collateral. Adequate protection is an attempt to resolve potential Fifth Amendment constitutional issues¹ presented by business reorganization cases that are at least as old as the Bankruptcy Act of 1898.² Congress' bankruptcy power³ is limited by the Fifth Amendment property protections under the "due process" clause.⁴ Creditors cannot be deprived of their property without due process of law.⁵

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A security interest is an interest in property. If Congress sought to preserve the rights of a secured creditor without any impairment or limitation, Congress would have permitted the secured creditor to enforce its security interest and to have that security interest retain its ranking to the same extent it would retain that ranking under applicable nonbankruptcy law.⁶ Without the powers to bar secured creditors from enforcing their liens and to use collateral in a case, it would not be possible for a debtor to reorganize in a great many cases.⁷ Accordingly, if Congress were too strict in protecting a secured creditor's interest in property under the Fifth Amendment, the bankruptcy power of Congress would be severely curtailed. A strict view would essentially permit only laws along the lines of a moratorium on the rights of unsecured creditors and would limit gravely a debtor's ability to rehabilitate its business.

A debtor's first need is often liquidity, and few debtors have unencumbered cash to finance their own restructuring. Debtors need to obtain the necessary liquidity in a bankruptcy proceeding from the use of cash collateral or postpetition credit. As a practical matter, many debtors would not be able to obtain postpetition credit without priming prepetition liens on the debtor's property. To enable debtors to use cash collateral and obtain postpetition credit by means of priming prepetition liens, without abridging the secured creditor's constitutional rights, sections 363(e) and 364(d) of the Bankruptcy Code require the holder of a lien or interest in such property be provided adequate protection of its interest.⁸ Adequate protection protects a secured creditor from a decline in the value of its interest in collateral during the pendency of the bankruptcy case.⁹ At the same time, it provides a debtor with options, despite having granted liens on its key assets prepetition. Were this flexibility not included in the Bankruptcy Code, a prepetition secured creditor having a lien on key assets could become the sole source of the debtor's liquidity during the case, and this would greatly shift bargaining power to the prepetition secured creditor.

Thus, in balancing, on the one hand, the demands of the Fifth Amendment to protect a property owner's due process rights, and, on the other hand, the policy for the protection of the ability of a debtor to rehabilitate itself, Congress chose to provide a secured creditor with "adequate protection" as a proxy for due process (and, in cases of total deprivation, just compensation).¹⁰ In so doing, Congress protected other creditor constituencies from adverse action by secured creditors. By requiring adequate protection for secured creditors as a basis for withholding the

enjoyment of certain rights, the Bankruptcy Code reconciles the property interests and constitutional rights of the secured creditor with those of the debtor and the unsecured creditors.

Given the constitutional ground of “adequate protection” to protect a secured creditor’s interest in property from a decrease in value of an interest in collateral due to the action of Sections 362, 363 and 364 of the Bankruptcy Code, the Bankruptcy Code does not give bankruptcy courts discretion as to *whether* a secured creditor is entitled to adequate protection.¹¹ A bankruptcy court does, however, have broad latitude as to what might constitute adequate protection and what method is appropriate for determining the value of an interest in collateral or the adequacy of the protection.¹² Section 361 of the Bankruptcy Code sets forth the following nonexclusive means by which adequate protection may be provided:

When adequate protection is required under section 362, 363, or 364 of this title of an interest of an entity in property, such adequate protection may be provided by—

- (1) requiring the trustee to make a cash payment or periodic cash payments to such entity, to the extent that the stay under section 362 of this title, use, sale, or lease under section 363 of this title, or any grant of a lien under section 364 of this title results in a *decrease in the value* of such entity’s interest in such property;
- (2) providing to such entity an additional or replacement lien to the extent that such stay, use, sale, lease, or grant results in a *decrease in the value* of such entity’s interest in such property; or
- (3) granting such other relief, other than entitling such entity to compensation allowable under section 503(b)(1) of this title as an administrative expense, as will result in the realization by such entity of the *indubitable equivalent* of such entity’s interest in such property.¹³

In addition to cash payment and the granting of replacement liens on assets, a bankruptcy court can grant any number of forms of relief to serve as adequate protection.¹⁴ Where adequate protection granted in a case proves insufficient to compensate a secured creditor for this diminution in value, section 507(b) of the Bankruptcy Code allows a secured creditor an administrative expense claim to the extent of the excess

diminution in value.¹⁵ Notably, an administrative expense claim under section 507(b) of the Bankruptcy Code is given priority over all other administrative claims arising under section 507(a)(2) of the Bankruptcy Code. In other words, this “superpriority” claim is senior in distribution priority to all other “actual, necessary cost and expense of preserving the estate” under section 503(b).¹⁶ This administrative expense claim serves as a “statutory fail-safe system in recognition of the ultimate reality that protection previously determined the ‘indubitable equivalent’ ... may later prove inadequate.”¹⁷

When determining whether a proposed protection is adequate, the principal considerations for the bankruptcy court are (1) the change in value of *an interest* in collateral (as opposed to *the collateral itself*)¹⁸ and (2) the provision of something equivalent to its decrease in value.¹⁹ A bankruptcy judge has wide latitude because valuations are “determined on a case by case basis.”²⁰ Value is “intended to have broad scope in the context of providing adequate protection to secured creditors.”²¹ The debtor should be prepared to substantiate with evidence the sources and extent of value in the particular case.²²

B. How do Courts Value the Protection That Is Due to a Secured Creditor?

Because adequate protection is meant to protect a secured creditor’s interest in the collateral, there is a valid argument that the secured creditor’s interest is only the value that would be realized if the collateral were liquidated by the secured creditor under applicable nonbankruptcy law.²³ Arguments can be made that the court may take account of market and other conditions changing over time, and that values change depending on when measured. The value protected should be the present value of the creditor’s interest.²⁴ Case law, however, has not finally resolved the question of the time when the value being protected by “adequate protection” is measured.²⁵

There is, nevertheless, a thread of consensus among bankruptcy courts about the timing of the valuation of the secured creditor’s interest in the debtor’s property. One point in time for measuring value for determining adequate protection is the petition date.²⁶ Another point in time is the date on which a request for adequate protection is made, on the ground that Fifth Amendment due process rights, and *a fortiori* adequate protection rights, may be waived.²⁷ For example, a secured creditor that waits six months into the case to demand adequate protection of its interest may be found to waive its right to adequate protection based

on a value as of the petition date. Such a creditor may only be entitled to adequate protection based on its interest in the collateral (and whether the value of that interest is declining) at the time of its demand. Thus, determining the extent of any diminution in value of an interest in collateral requires two valuations of the interest at different points in time first, either at the petition date or the date on which a secured creditor requests adequate protection, and second, at the time of confirmation or other final resolution of the secured creditor's interest in the case.²⁸

Calculating diminution in value for adequate protection purposes, the court must compare the value of the collateral as of the initial relevant time (i.e., the petition date or the date of demand) with the value as of the final relevant time (i.e., confirmation or the effective date of the Chapter 11 plan).²⁹ The determination of what is to be provided as adequate protection is made at the time of that initial determination. But the determination as to whether there has been a diminution in value is made at the later date of final resolution. A bankruptcy court has broad discretion in determining the method for valuation of collateral for purposes of establishing whether there has been a diminution in value.³⁰

What is the appropriate valuation? For the bankruptcy court to determine what valuation method is appropriate, the “proposed disposition or use of the collateral is of paramount importance to the valuation question … the appropriate standard for valuing collateral must depend upon what is to be done with the property—whether it is to be liquidated, surrendered, or retained by the debtor.”³¹ If the case were to conclude with a reorganization of the debtor, rather than a liquidation, the secured creditor may be entitled to a diminution claim equal to the difference between what that creditor receives pursuant to the plan and the going concern value of his interest in collateral at the relevant initial time (i.e., the petition date or the date of demand) even though the secured creditor may not have had the ability to realize the value of his interest in collateral on a going concern basis at the relevant initial time.³² The appropriate determination of what constitutes adequate protection requires the analysis of all relevant facts.³³ There is room for argument.

The challenges facing a bankruptcy court when valuing collateral for the purpose of determining diminution can be seen in the following illustration. Suppose a secured creditor has a lien on substantially all of the assets of an operating company. Suppose the assets on the petition date constituting collateral have a going concern value of \$100 million and a liquidation value of \$70 million, and the allowed claim of the prepetition secured creditor is \$90 million. The debtor obtains \$20

million in postpetition financing secured by a priming lien on the encumbered property postpetition under section 364(d) of the Bankruptcy Code. If the bankruptcy court accepts the argument that the value of the interest in collateral on the petition date is liquidation value, the secured creditor has suffered no diminution in value of its interest in collateral (i.e., the reorganization date value of \$100 million less \$20 million is greater than petition date value of \$70 million). But if the bankruptcy court accepts an argument that the value of the interest in collateral on the petition date is a going concern value of \$100 million, the secured creditor has suffered a \$10 million diminution in value (i.e., the reorganization date value of \$100 million less \$20 million is \$80 million, which is exceeded by the allowed secured claim of \$90 million). The challenges facing a bankruptcy court when determining diminution in value are further complicated by risks and mitigating circumstances relating to changes in markets, asset depreciation and other factors that change over time.

The possibilities for what might constitute “adequate protection” of a secured creditor’s interest in the debtor’s property are many, depending on the nature of the restructuring. In cases where a secured creditor has a lien on all assets, current payment of interest from the liquidation financing might represent value equal to the diminution in value.³⁴ Where there are unencumbered assets, as there are in most cases, the back-stop superpriority administrative expense claim under section 507(b) might serve its role as a failsafe protection. But what if there are no material unencumbered assets to pay this potential 507(b) claim?

C. Adequate Protection in the Context of Projects

Analysis of adequate protection in the context of financing of a project, as distinguished from adequate protection in the context of a going concern business, has unique features. Leading cases regarding adequate protection in real estate projects are *In re 495 Cent. Park Ave. Corp.*,³⁵ *In re Swedeland Development Corp. (U.S. v. Geniviva)*,³⁶ and *In re YL West 87th Holdings I LLC*.³⁷ *YL WL West 87th* arguably stands for the proposition that “the preferred test in determining whether priming of a senior lien” is the existence of an equity cushion.³⁸ *Central Park* and *Swedeland* are often cited as support for opposite propositions, absolutes as to whether adequate protection is appropriate, or not appropriate, in all cases for bankruptcy financed build-out of a project. The cases, however, may be reconciled.³⁹

A project represents a capital asset in the process of construction. This asset does not (typically) generate income until completion. Until it becomes an income-generating asset, the project's theoretical value as an income generating asset is discounted by two uncertainties: (1) the uncertainty of the cost of completion of the assets, which may go up or down, and (2) the uncertainty of the stream of income that the asset will produce. Both of these uncertainties decrease over time as the project approaches completion, with the speculative risk associated with the completion of the project moving to zero at the time of completion. Thus, one valuation could be the present value of anticipated future revenues less the amount of further expenditures required to achieve those revenues discounted to expected value by the uncertainties. The other possible valuation is based upon raw land value less demolition costs. At the risk of pointing out the obvious, if the value of the latter exceeds the value of the former, no restructuring should occur.

Project completion also involves the addition of new value and new assets. That is, projects during build-out may involve continual accession to the existing collateral and mixing of collateral. For example, the completion of a 15-unit condominium when 10 units are completed will involve the construction of five units. The five units constructed postpetition can be said to represent a postpetition asset under section 552(a) of the Bankruptcy Code, i.e., a postpetition asset, and not proceeds, products, offspring or profits of prepetition collateral under section 552(b) of the Bankruptcy Code.⁴⁰ As such, the five additional units might constitute an increase in value of the asset sufficient to serve as adequate protection for a primed prepetition lien holder, although the question may arise as to how are they to be valued separately. Assuming that units 11 to 15 are synergistic with units one to 10, the value of one to 10 should increase as a result of the further completion of the condominium project, and the value of units 11 through 15 would be greater than their cost of construction.⁴¹

In *Central Park*, the court evaluated adequate protection arguments in the context of a Manhattan apartment building. The *Central Park* court found that the additional value from the completion of the project provided adequate protection to the existing secured creditor whose security interest was primed. In particular, the *Central Park* court cited the higher rental value of the units upon the restoration of the building. *Central Park*, however, is often cited to support the proposition that "The money spent for improvements will be transferred in value."⁴²

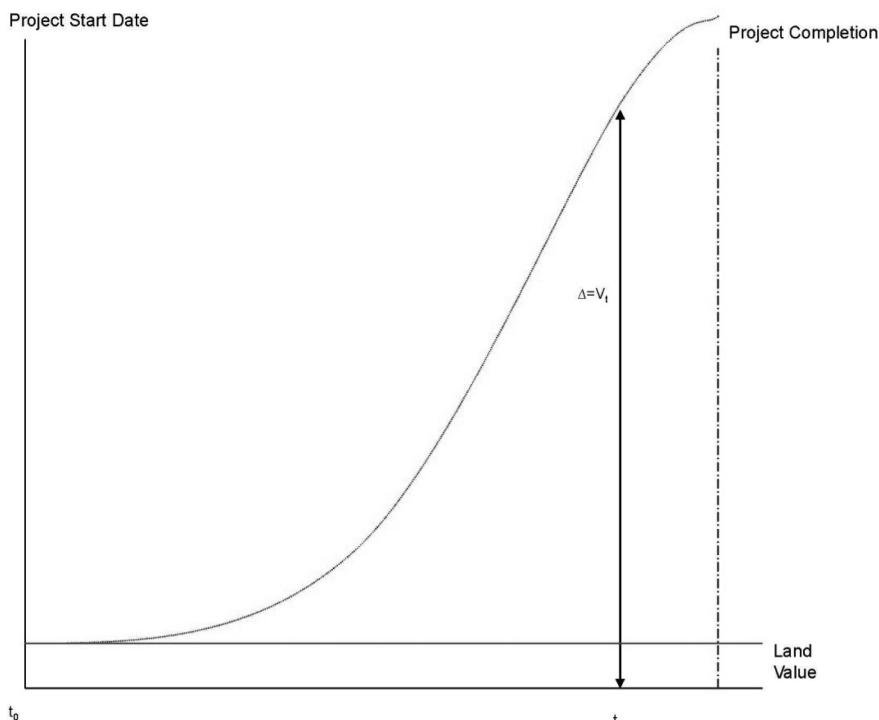
By contrast, *Swedeland* involved a 508-acre golf course development in Sussex County, New Jersey, the development of which had been ongoing for at least four years. The *Swedeland* court found that the projected increase in value in the project derived from additional development of the golf course did not constitute adequate protection because the debtor's projections were speculative and reflected only the hopes and beliefs of the debtor, rather than any certainty of outcome. Accordingly, the *Swedeland* court declined to ascribe any meaningful increase in value of the project from continued construction. *Swedeland* found that the potential increase in value (given the uncertainty of achieving this increased value) was not sufficient to protect the secured creditor from the diminution in value of that creditor's collateral that would have resulted from further construction of the project.

Swedeland also attempts to distinguish *Central Park*, noting that, in *Central Park*, some additional value above the projected increase in the value of the collateral property protected the senior lien holder's interest.⁴³ Many believe that *Swedeland* stands for the proposition that there is no basis for ever providing adequate protection based on value accretion in the project derived from further development. Indeed, *Swedeland* itself contains express *dicta* that "continued construction based on projections and improvements to the property does not alone constitute adequate protection."⁴⁴

Despite the apparent tension between the cases, *Central Park* and *Swedeland* can be viewed as decisions standing for fundamentally the same proposition, namely, that speculative risk must be taken into account when determining the increase in value from continued construction. Synthesized in this way, *Swedeland* stands for the proposition that when the speculative risk is sufficiently high, the projected increase in value resulting from additional expenditures on the project is discounted. This discount, if great enough, can render the projected increase in value an insufficient basis for adequate protection. Similarly, *Central Park* stands for the proposition that when speculative risk is sufficiently low, the increase in value resulting from the additional expenditures is a basis for adequate protection. In this light, *Swedeland* and *Central Park* embody the same principle applied to different facts. In addition to its logical strength, this reconciliation of *Swedeland* and *Central Park* promotes a fundamental policy of the Bankruptcy Code, which is the rehabilitation and reorganization of an enterprise, preserving value and employment by providing a debtor with an opportunity to rehabilitate a project so long as the speculative risks in the accretion of value are not too great.

Swedeland and *Central Park* have other implications based on patterns of change in value over time corresponding to change in uncertainty over time. In a previous article,⁴⁵ we supposed that a real estate project can be said to have speculative, transitional and nonspeculative phases as the risk of the failure of the project declines as completion approaches. At the outset, a real estate project is raw land. Once project construction begins, the uncertainties of project cost and final project revenues are at their greatest, and the expected value discount to the present value of the future stream of income is also at its greatest. At a certain point, however, uncertainties of project cost and final project revenues begin to decrease as actual (as opposed to budgeted or projected) construction costs come into view and future income becomes more predictable as market conditions become more certain and sales have occurred. This shift in value over time can be depicted as a curve resembling a flattened "S" as shown in Figure 1. Figure 1 is just an example, as each project asset can be expected to be unique.

Figure 1



If a liquidity crisis occurs and insolvency proceeding commences different times “ t ” along that curve, the project’s viability has different characteristics. Early on, it may be impossible to provide financing that increases the value of the project by an amount greater than the amount of the financing. As the speculative risk of the project declines, however, it becomes more likely for the debtor to obtain additional financing—even on a priming basis—where the increase in the value of the project exceeds the amount of the new financing.

There are practical challenges to a debtor using value accretion in a project resulting from postpetition improvements as a basis for the provision of adequate protection to a secured creditor. For instance, a certain amount of the increase in the value of the project may be attributable to the increase in value of real estate and improvements existing on the petition date. But the real estate and improvements that existed on the petition date are collateral of the prepetition secured creditor. It may not be possible to rebut arguments that the increase in value of such real estate and improvements is “profits” and “products” of prepetition collateral for the benefit of the prepetition secured creditor under section 552(b)(1) of the Bankruptcy Code. Consequently such value may not properly be available as adequate protection without relief based on the equities.⁴⁶ Also, an increase in the secured creditor’s prepetition collateral resulting from postpetition improvements would obviate the need for adequate protection (which can only be for diminution in value of the prepetition collateral). And further, whether there has been an increase or diminution in prepetition collateral cannot be known until the final disposition of the collateral giving rise to a second measuring date.⁴⁷

Despite this apparent difficulty there may yet be ground for providing adequate protection through a replacement lien on unencumbered property. As the debtor adds new labor and new physical assets to the project, a portion of the increase in value of the project is attributable to postpetition assets. That is, the increase in value directly attributable to the accession of postpetition physical assets and labor and the increase in this postpetition value—“profits” and “products” of new postpetition value—are new value on which a replacement lien may be meaningfully placed.

We have found it helpful to give arithmetic expression to these changes in value based on the total value as a proportion of the prepetition and postpetition value inputs. If the value of the collateral petition date is “ Y ” and the value of additional development at any time “ t ” is “ Z_t ”, and

the value of the project at time "t" is " V_t ", then at any time the portion of asset value in which the prepetition lender has an interest on account of its prepetition security interest can be expressed as follows:

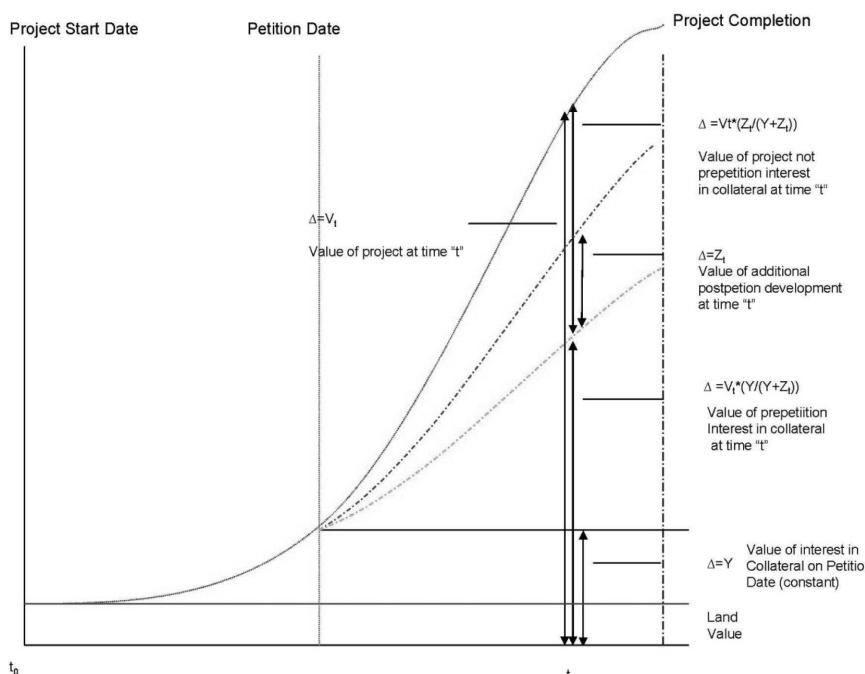
$$V_t * (Y/(Y+Z_t))$$

Similarly at any time "t" the portion of the asset value in which the prepetition lender does not have an interest on account of its prepetition security interest can be expressed as follows:

$$V_t * (Z_t/(Y+Z_t))$$

The asset value in which the prepetition lender does not have an interest on account of its prepetition lien is available to serve as adequate protection through a replacement lien.⁴⁸ If V_t is increasing rapidly because of the decline in speculative risk, then it is possible (and, in some cases, probable) that there is sufficient value to serve as adequate protection from a potential the decline in value to the prepetition lender in order to support a priming lien (or use of cash collateral). Figure 2 illustrates the point showing a hypothetical value curve of a project incorporating the references used in the formulae above.

Figure 2



The sufficiency of adequate protection in such context requires a careful factual analysis of projections and risk based on expert testimony and other evidence. Bankruptcy courts are left to make a factual determination as to whether the certainty of the success of the project (or conversely the discount of the risk of failure) implies sufficient value of the additional collateral created by continued project development for adequate protection.⁴⁹ One challenge for valuation experts may be identifying the point at which speculative risk begins to decline rapidly causing valuation to rise quickly as the project moves towards completion.⁵⁰ Further, unstable markets and uncontrollable variables add complexity to a finding of adequate protection through projected increases in collateral property alone.⁵¹ Where a project possesses indicia of certainty, such as identified buyers, adequate historical data or likely future events, a finding of adequate protection from a replacement lien on unencumbered assets in the form of the accretive value created by the development of the project could be consistent with *Swedeland* and *Central Park* alike.

Where the circumstances are such that a debtor cannot readily identify facts supporting the certainty of value of project completion, the test may be whether there is an equity cushion in the existing asset.⁵² While courts have been in some circumstances been reluctant to find adequate protection where an equity cushion exists but is small or may be subject to decline,⁵³ it is also possible that several sources of adequate protection might be considered together, such as equity cushion plus increase (or prevention of decrease, which is arguably the same thing) in value.

Single asset real estate projects present additional issues because Congress has made significant concessions to single asset real estate lenders. Specifically, section 101 of the Bankruptcy Code provides:

The term ‘single asset real estate’ means real property constituting a single property or project, other than residential real property with fewer than 4 residential units, which generates substantially all of the gross income of a debtor who is not a family farmer and on which no substantial business is being conducted by a debtor other than the business of operating the real property and activities incidental.⁵⁴

If a debtor qualifies as “single asset real estate”, or “SARE”, section 362(d)(3) of the Bankruptcy Code provides that a secured creditor, upon request, be granted relief from the automatic stay unless, within 90 days following the after the entry of an order for relief or 30 days

after the court determines that the debtor is a SARE, the debtor has filed a plan of reorganization that has a reasonable possibility of being confirmed within a reasonable time or the debtor has commenced monthly payments in an amount equal to interest at the applicable nondefault rate of interest on the value of the creditor's interest in the collateral.⁵⁵ If a SARE determination is made, adequate protection must include an analog of adequate protection in the form of cash payment of interest or a realistic and facially confirmation Chapter 11 plan needs to be on file.

Given these heightened protections to a secured creditor in the SARE context, the question becomes determining whether a particular debtor qualifies as a SARE. The definition speaks for itself in many respects. The question arises, however, whether a semi-completed project with an income-producing adjunct is in fact a SARE. For example, a semi-completed resort project with a golf course and restaurant may not be a SARE depending on the scale of such activities.⁵⁶ By contrast, other mixed-use projects, like a real estate development wherein, in addition to developing and selling property, the debtor also was in the business of purchasing other property, planning and constructing homes, marketing and selling homes, and maintaining developed properties, have been considered SARE under the Bankruptcy Code.⁵⁷

In conclusion, while there are acknowledged challenges to obtaining postpetition financing to complete an unfinished project in Chapter 11, these challenges are not necessarily insurmountable. Indeed, as demonstrated, the leading case law is subject to interpretation and synthesis and does not, therefore, create a bright-line rule that holds that increased value of a project over time cannot serve as a basis for adequate protection. Rather, whether such increased value is sufficient for adequate protection should be considered on a case-by-case basis, with focus on the extent of the risk related discount for increased value. Viewing adequate protection in this way in the context of bankruptcy project finance cases can give, under the appropriate circumstances, a project debtor an opportunity to complete project construction and ensure that all holders of claims and interests enjoy the benefit of their bargains.

Notes

1. See generally 2 Collier on Bankruptcy 361-62 (Matthew Bender ed., 15th ed. 2010). See also U.S. v. Security Indus. Bank, 459 U.S. 70, 103 S. Ct. 407, 74 L. Ed. 2d 235, 9 Bankr. Ct. Dec. (CRR) 1071, 7 Collier Bankr. Cas. 2d (MB) 629, Bankr. L. Rep. (CCH) P 68875, 35 U.C.C. Rep. Serv. 1 (1982).

2. Adequate protection is embodied in the now defunct Bankruptcy Act of 1898 in Section 77B.

3. U.S. Const. art. I.
4. U.S. Const. amend. V.
5. Wright v. Union Cent. Life Ins. Co., 311 U.S. 273, 279, 61 S. Ct. 196, 85 L. Ed. 184 (1940); see also Continental Illinois Nat. Bank & Trust Co. of Chicago v. Chicago, R.I. & P. Ry. Co., 294 U.S. 648, 680, 55 S. Ct. 595, 79 L. Ed. 1110 (1935). In addition, the Fifth Amendment takings clause prohibits the taking of a creditor's property for public use without just compensation. See Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555, 602, 55 S. Ct. 854, 79 L. Ed. 1593, 97 A.L.R. 1106 (1935).
6. Stratton v. New, 283 U.S. 318, 321, 51 S. Ct. 465, 75 L. Ed. 1060 (1931).
7. Continental Illinois, 294 U.S. at 680.
8. The legislative history is clear that the purpose of adequate protection "is to insure that the secured creditor receives in value essentially what he bargained for." Cong., 2d Sess at 53 (1978).
9. In re Alycan Interstate Corp., 12 B.R. 803, 7 Bankr. Ct. Dec. (CRR) 1123, 4 Collier Bankr. Cas. 2d (MB) 1066 (Bankr. D. Utah 1981); Grundy Nat. Bank v. Tandem Min. Corp., 754 F.2d 1436, 12 Collier Bankr. Cas. 2d (MB) 264, Bankr. L. Rep. (CCH) P 70258 (4th Cir. 1985). This, of course, means the creditor must have an interest in collateral at the relevant time of determination.
10. Radford, 295 U.S. at 555.
11. The statutory language makes the intention of Congress amply clear on the point. See 11 U.S.C.A. § 362(d) ("On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay... for cause, including the lack of adequate protection of an interest in property of such party in interest"); 11 U.S.C.A. § 363(e) ("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, with or without a hearing, *shall prohibit or condition* such use, sale, or lease as is necessary to provide adequate protection of such interest"); 11 U.S.C.A. § 364(d) ("The court, after notice and a hearing, may authorize the obtaining of credit or the incurring of debt secured by a senior or equal lien on property of the estate that is subject to a lien *only if* (A) the trustee is unable to obtain such credit otherwise; and (B) there is adequate protection of the interest of the holder of the lien on the property of the estate on which such senior or equal lien is proposed to be granted."). One effect of this is to render the lack of adequate protection a potent objection to secured postpetition financing. Intercreditor arrangements often require the waiver of adequate protection rights for junior lienholders (who are first affected by diminution in value) to bar them from holding up postpetition financing.
12. In re Beker Industries Corp., 58 B.R. 725, 737 (Bankr. S.D. N.Y. 1986).
13. 11 U.S.C.A. § 361 (emphasis added).
14. For instance, a bankruptcy court could give a secured creditor the right to receive regular reporting on the debtor's operations, or the right to inspect the debtor's operations at reasonable intervals.
15. 11 U.S.C.A. § 507(b); see also In re Scopac, 624 F.3d 274, 282, 53 Bankr. Ct. Dec. (CRR) 221, 64 Collier Bankr. Cas. 2d (MB) 726, Bankr. L. Rep. (CCH) P 81866 (5th Cir. 2010), opinion modified on denial of reh'g, In re Scopac, 649 F.3d 320 (5th Cir. 2011); Grundy Nat. Bank, 876 F.2d at 363; In re James B. Downing & Co., 94 B.R. 515, 520, 20 Collier Bankr. Cas. 2d (MB) 1583 (Bankr. N.D. Ill. 1988); In re Mutschler, 45 B.R. 494, 496 (Bankr. D. N.D. 1984); accord In re McGill, 78 B.R. 777, 780 (Bankr. D. S.C. 1986); In re Callister, 15 B.R. 521, 528, 8 Bankr. Ct. Dec. (CRR) 446, 5 Collier Bankr. Cas. 2d (MB) 1058 (Bankr. D. Utah 1981), subsequently aff'd, 13 Bankr. Ct. Dec. (CRR) 21, 1984 WL 249787 (10th Cir. 1984).
16. Grundy Nat'l Bank, 876 F.2d at 363.
17. In re Carpet Center Leasing Co., Inc., 4 F.3d 940, 941 (11th Cir. 1993).
18. In re American Mariner Industries, Inc., 734 F.2d 426, 433, 12 Bankr. Ct. Dec. (CRR) 227, 10 Collier Bankr. Cas. 2d (MB) 910, Bankr. L. Rep. (CCH) P 69886 (9th Cir. 1984).
19. American Mariner, 734 F.2d at 433.

20. In re Martin, 761 F.2d 472, 474, 12 Collier Bankr. Cas. 2d (MB) 974, Bankr. L. Rep. (CCH) P 70543 (8th Cir. 1985).
21. American Mariner, 734 F.2d. at 431.
22. In re Snowshoe Co., Inc., 789 F.2d 1085, 1088-89, Bankr. L. Rep. (CCH) P 71146 (4th Cir. 1986).
23. See In re Best Products Co., Inc., 138 B.R. 155, 22 Bankr. Ct. Dec. (CRR) 1288, 26 Collier Bankr. Cas. 2d (MB) 1709, Bankr. L. Rep. (CCH) P 74592 (Bankr. S.D. N.Y. 1992), decision aff'd, 149 B.R. 346 (S.D. N.Y. 1992); Matter of Haiflich, 63 B.R. 314, 14 Bankr. Ct. Dec. (CRR) 1195, 15 Collier Bankr. Cas. 2d (MB) 640, Bankr. L. Rep. (CCH) P 71414 (Bankr. N.D. Ind. 1986). See also In re Windsor Hotel, L.L.C., 295 B.R. 307, 314, 50 Collier Bankr. Cas. 2d (MB) 836 (Bankr. C.D. Ill. 2003) (Noting that the purpose of adequate protection is "to preserve the prepetition position of the existing lender.").
24. See Scopac, 624 F.3d at 264 (citing *In re Stembridge*, 394 F.3d 383, 387 (5th Cir. 2004)).
25. See Matter of Continental Airlines, Inc., 146 B.R. 536, 539 (Bankr. D. Del. 1992), subsequently aff'd, 91 F.3d 553, 29 Bankr. Ct. Dec. (CRR) 629, 36 Collier Bankr. Cas. 2d (MB) 785 (3d Cir. 1996).
26. See, e.g., Matter of Johnson, 47 B.R. 204, 40 U.C.C. Rep. Serv. 1114 (Bankr. W.D. Wis. 1985) (with respect to the use of cash collateral).
27. In re Cason, 190 B.R. 917, 927, 34 Collier Bankr. Cas. 2d (MB) 1476 (Bankr. N.D. Ala. 1995).
28. In re Geijssel, 480 B.R. 238, 266 (Bankr. N.D. Tex. 2012) citing In re 499 W. Warren Street Associates, Ltd. Partnership, 142 B.R. 53, 57, 27 Collier Bankr. Cas. 2d (MB) 696 (Bankr. N.D. N.Y. 1992).
29. See Scopac, 624 F.3d at 279; Carpet Center, 991 F.2d at 689.
30. See 11 U.S.C.A. § 506(a) ("Such value shall be determined in light of the purpose of the valuation."); see also In re Heritage Highgate, Inc., 679 F.3d 132, 142, 56 Bankr. Ct. Dec. (CRR) 145, Bankr. L. Rep. (CCH) P 82313 (3d Cir. 2012) ("Congress envisioned a flexible approach to valuation whereby bankruptcy courts would choose the standard that best fits the circumstances of a particular case. 'Courts will have to determine the value on a case-by-case basis, taking into account the facts of each case and the competing interests in the case.'"') (quoting H.R. Rep. No. 95-595, at 356 (1977), reprinted in 1978 U.S.C.C.A.N. 5787, 6311).
31. Heritage Highgate, Inc., 679 F.3d at 141. The bankruptcy court's ultimate determination of value in this context is a factual question that is subject to a clearly erroneous standard of review if challenged. Carpet Center, 991 F.2d at 68 (citing In re Club Associates, 951 F.2d 1223, Bankr. L. Rep. (CCH) P 74438 (11th Cir. 1992) and In re Sublett, 895 F.2d 1381, 22 Collier Bankr. Cas. 2d (MB) 868, Bankr. L. Rep. (CCH) P 73279 (11th Cir. 1990)); *see also* In re Green, 934 F.2d 568, 570, 21 Bankr. Ct. Dec. (CRR) 1287, 24 Collier Bankr. Cas. 2d (MB) 1911, Bankr. L. Rep. (CCH) P 74015 (4th Cir. 1991); Fed. R. Bankr. P. 8013.
32. See, e.g., Scopac, 624 F.3d at 282.
33. In re Aqua Associates, 123 B.R. 192, 196-97 (Bankr. E.D. Pa. 1991) ("[T]he issue of adequate protection... is measured by an analysis of all relevant facts, with a particular focus upon the value of the collateral, the likelihood that it will depreciate or appreciate over time, the prospects for a successful reorganization of the Debtor's affairs by means of the Plan, and the Debtor's performance in accordance with the Plan.") (internal quotations omitted).
34. See American Mariner, 734 F.2d at 435.
35. In re 495 Cent. Park Ave. Corp., 136 B.R. 626 (Bankr. S.D. N.Y. 1992).
36. U.S. v. Geniviva, 16 F.3d 522, 94-1 U.S. Tax Cas. (CCH) P 60156, 73 A.F.T.R.2d 94-2341 (3d Cir. 1994) (Swedeland).
37. In re YL West 87th Holdings I LLC, 423 B.R. 421, 52 Bankr. Ct. Dec. (CRR) 205 (Bankr. S.D. N.Y. 2010).
38. YL West 87th Holdings I LLC, 423 B.R. 421, 441, 52 Bankr. Ct. Dec. (CRR) 205 (Bankr. S.D. N.Y. 2010).

39. The following quote is helpful as well as entertaining in addressing contradictory precedents. To reduce logically, if that is necessary, the two contradictory cases must hang on a common principle. “In actual practice, two cases are rarely, if ever, alike... thus a judge may have a wide discretion in a given case whether to follow either precedent A, or precedent B, both of which seem to have considerable bearing on this case but which, unfortunately, are completely contradictory to one another.” Carr, *The Supreme Court and Judicial Review* 296 (Farrar and Rinehart, Inc. 1942).

40. 11 U.S.C.A. § 552. Note that the court does have the power to make an equitable exception to the postpetition lien on proceeds.

41. Of course, depending on the valuation, it may be that the cost of completing units 11 through 15 is greater than the value of those units and any value they add to units one to 10.

42. Cent. Park, 136 B.R. at 626.

43. Swedeland, 16 F.3d at 556.

44. Swedeland, 16 F.3d at 556.

45. Restructuring Issues Concerning Real Estate Projects, 23 Bankr. L. Rep. (BNA) No. 10 (Mar. 10, 2011).

46. See, e.g., *In re Putnal*, 483 B.R. 799 (Bankr. M.D. Ga. 2012).

47. W. Warren, 142 B.R. at 57.

48. For example, if the value of the collateral on the petition date (Y) is \$100 million and the value of additional development at on the effective date (Z_t) is \$30 million, and the value of the total project at time “t” (assume the effective date of reorganization) (V_t) is \$150 million, then the interest on account of its prepetition security interest is \$150*(\$100/(\$100+\$30) or \$115.4 million . Postpetition new value would be \$150*(\$30/(\$100+\$30) or \$34.6 million. On this basis up to \$34.6 million of new value could serve as a source of value for adequate protection.

49. A helpful discussion of certain aspects of these valuation issues are also discussed in Bingham II and Robertson, Reconciling “Dirt for Debt” Plans with the “Indubitable Equivalent” Standard, 28 Am. Bankr. Inst. J. 8 (Oct. 2009), available at <http://www.stites.com/media/pnc/5/media.1355.pdf>.

50. Restructuring Issues Concerning Real Estate Projects, 23 Bankr. L. Rep. (BNA) No. 10 (Mar. 10, 2011).

51. *In re Mosello*, 195 B.R. 277 (Bankr. S.D. N.Y. 1996) (holding that contingencies such as zoning and the real estate market rendered debtor’s proposed subdivision too risky to provide adequate protection to the prepetition creditor).

52. YL West 87th Holding I LLC, 423 B.R. 421.

53. *In re Strug-Division LLC*, 380 B.R. 505, 514, 49 Bankr. Ct. Dec. (CRR) 109 (Bankr. N.D. Ill. 2008).

54. 11 U.S.C. § 101(51B).

55. 11 U.S.C. § 362(d)(3).

56. See, e.g., *In re Scotia Pacific Co., LLC*, 508 F.3d 214, 49 Bankr. Ct. Dec. (CRR) 12, 58 Collier Bankr. Cas. 2d (MB) 1508, Bankr. L. Rep. (CCH) P 81053 (5th Cir. 2007) (listing multiple examples of non-SARE properties).

57. But see *In re Kara Homes, Inc.*, 363 B.R. 399, 47 Bankr. Ct. Dec. (CRR) 274, Bankr. L. Rep. (CCH) P 80885 (Bankr. D. N.J. 2007). However, Kara Homes has been the subject of criticism for its “very broad determination of SARE.” Hotels, the Real Estate Bust and Bankruptcy, 28-3 Am. Bankr. Inst. J. 20 n.4 (April 1, 2009). See also Tracht, Single Asset Real Estate and Development Projects: The Kara Homes Mistake, 127 Banking L.J. 258, 258 (March, 2010).