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## ACCELERATION OF PLAN CONFIRMATION ANALYSIS TO THE PRE-CONFIRMATION STAGE UNDER THE FEDERAL BANKRUPTCY CODE

[In re *Martin*, 761 F.2d 472 (8th Cir. 1985)]

### INTRODUCTION

Over the past three years, sixty-six farms have been lost per day as a result of bankruptcy.<sup>1</sup> Furthermore, during the past six years, the financial condition of many farmers has deteriorated significantly. Three principle factors account for this deterioration:<sup>2</sup> high interest rates;<sup>3</sup> depressed commodity prices;<sup>4</sup> and stagnating or even declining land prices.<sup>5</sup> Farming has been a cyclical activity, and farm businesses have suffered through a number of periods of economic strife.<sup>6</sup> The importance of the use of unencumbered cash collateral<sup>7</sup> as a reorganization vehicle for the farmer is magnified as a result of the depressed agricultural economy. Conversely, the depressed farm economy also heightens the awareness of adequately protecting the competing interest of the secured creditor.

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1. See Meyers, *Is There Life After Farming? Yes, And For Some It Is A Better Life*, Minneapolis Star & Trib., Aug. 11, 1985, at 28A, col. 1.

2. Grossman & Fischer, *The Farm Lease in Bankruptcy: A Comprehensive Analysis*, 59 NOTRE DAME LAW. 598, 598 (1984). "Stagnating or declining land prices have reduced the value of the farmer's equity and pose special problems for landowners who borrowed extensively to purchase land at inflated values." *Id.* An increasingly large portion of farm income is being consumed by interest costs. "In 1978, interest had absorbed approximately one-fifth of the total farm income remaining after all other operating expenses had been subtracted; by 1981 it had absorbed approximately two-fifths." *Id.* Decreasing commodity prices have decreased net cash farm income from \$37 billion in 1979 to \$31 billion in 1982. This decline in farm income has created cash-flow problems for many farmers and has prevented some from meeting their financial obligations resulting in foreclosure. *Id.*

3. *Id.*

4. *Id.*

5. *Id.*

6. Landers, *Reorganizing Farm Business Under Chapter 11*, 5 J. AGRIC. TAX'N & L. 11, 11 (1983). "The present farm economy whether called a recession, depression, or something else, has been no different. Farm income is down, farm prices are down, and farm failures are up." *Id.*

7. See 11 U.S.C. § 363(a) (Supp. II 1984). Section 363(a) sets forth a definition important to the working of section 363 and defines "cash collateral" as 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 and includes the proceeds, products, offspring, rents, or profits of property subject to a security interest as provided in section 552(b) of this title, whether existing before or after the commencement of a case under this title. *Id.*

In re *Martin*,<sup>8</sup> a recent Eighth Circuit Court of Appeals decision, involved this type of farm crisis. In *Martin*, the debtors sought to sell grain and use the cash proceeds to finance continued farming operations.<sup>9</sup> The Eighth Circuit remanded the case for further analysis in view of the bankruptcy court's failure to establish the value of the creditor's security interest in the stored grain and to identify the associated risks.<sup>10</sup> The *Martin* decision indicates that the debtor must demonstrate specific valuations illustrating that the creditor's security interest is not at risk.—This is an arduous task.

The consequence in many reorganization cases is that constitutionally-mandated adequate protection for a secured creditor's rights cannot be provided under the Bankruptcy Code<sup>11</sup> without placing the possibility of successful reorganization in jeopardy.<sup>12</sup> Narrow interpretations of adequate protection<sup>13</sup> will crowd out potential reorganizations in an already desperate agricultural economy.

This Comment discusses *Martin* and the reasoning the Eighth Circuit used in establishing a flexible adequate protection standard in the context of the amorphous indubitable equivalent requirement of the Bankruptcy Code.<sup>14</sup> First, the Comment will focus on the potential negative results of a narrow construction of adequate protection for cash collateral purposes. Second, it analyzes the similarities between the feasibility requirement applicable to confirmation<sup>15</sup> and ad-

8. 761 F.2d 472 (8th Cir. 1985).

9. *See id.*

10. *Id.* at 478.

11. Section 361 of the Bankruptcy Code provides:

When adequate protection is required under section 362, 363, or 364 of this title of an interest of 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.

11 U.S.C. § 361 (Supp. II 1984).

12. Gordanier, *The Indubitable Equivalent of Reclamation: Adequate Protection for Secured Creditors under the Bankruptcy Code*, 54 AM. BANKR. L.J. 299, 300 (1980). If Chapter 11 reorganizations are to produce economically viable businesses, secured creditors must be assured that collateral will not be impaired in any way. Otherwise, liquidation and/or disastrously higher commercial credit costs will result. *Id.*

13. *See supra* note 11.

14. *See* 11 U.S.C. § 361(3).

15. *Id.* § 1129(a)(11) (1982). Section 1129 states in pertinent part:

equate protection<sup>16</sup> through the use of cash collateral.<sup>17</sup> The implication is that the correlation will impede attempts at farm reorganization under Chapter 11.<sup>18</sup>

## I. BACKGROUND

Traditionally, there has been a strong policy of debtor rehabilitation in bankruptcy law.<sup>19</sup> Through the enactment of section 361 of the Bankruptcy Code,<sup>20</sup> the policy has taken a pro-secured creditor shift.<sup>21</sup> The goal is to balance a policy of debtor rehabilitation with

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(a) The court shall confirm a plan only if all of the following requirements are met:

(11) Confirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan, unless such liquidation or reorganization is proposed in the plan.

*Id.*

16. *Id.* § 361(3).

17. *Id.* § 363. Section 363(a) provides:

(a) 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 and includes the proceeds, products, offspring, rents, or profits of property subject to a security interest as provided in section 552(b) of this title, whether existing before or after the commencement of a case under this title.

*Id.*

18. See *infra* notes 156-66 and accompanying text.

19. Massari, *Adequate Protection Under the Bankruptcy Reform Act*, 1979 ANN. SURV. BANKR. L. 171, 171; see also *Charlestown Sav. Bank v. Martin (In re Colonial Realty)*, 516 F.2d 154, 158 (1st Cir. 1975) (the purpose of Chapters X and XII, under the Act, is to restore, not dismantle, the economically distressed debtor).

An intrinsic purpose of bankruptcy law is to give the debtor a chance at a fresh start in life without creditor harassment. See *Perez v. Campbell*, 402 U.S. 637, 648 (1971) (basic purposes of bankruptcy laws is to give certain debtors a fresh start). Bankruptcy laws are no longer used primarily to punish insolvents who may have made some mistakes. See *Beall v. Pinckney*, 150 F.2d 467, 470 (5th Cir. 1945). Instead, the laws are intended to release and rehabilitate the debtor and allow him to start anew. *Id.* Public policy looks beyond the debtor to his family, and regards reasonable protection of that family as a greater concern than the full payment of debts. *Id.* In keeping with these policy considerations, certain property of the debtor can be treated as exempt. See 11 U.S.C. § 522 (1984). The goals of the exemption provisions are: (1) to protect the debtor from abject poverty; (2) to assist and encourage the debtor on the road to recovery through a fresh start; and (3) to shift the burden of the welfare of the debtor and his family from society as a whole to the creditors who dealt with the debtor and contributed to his economic demise. *In re Merwin*, 4 BANKR. CT. DEC. (CRR) 17, 18 (Bankr. M.D. Fla. 1978).

20. 11 U.S.C. § 361.

21. See Massari, *supra* note 19, at 171.

Section 361 provides protection for secured creditors early in bankruptcy proceedings. Section 361 also allows the court, if necessary, to become rapidly familiar with the status of the debtor's business, the value of the debtor's encumbered assets,

the rights of the secured creditor.<sup>22</sup> The Code attempts to achieve this result by requiring "adequate protection" of a secured creditor's interest.<sup>23</sup>

Congress passed the Bankruptcy Reform Act in 1978,<sup>24</sup> the first comprehensive reform of bankruptcy law in forty years.<sup>25</sup> The widespread changes in debtor-creditor relationships, caused in part by the adoption of the Uniform Commercial Code (U.C.C.), mirrors the drafters' intention behind the new Bankruptcy Code.<sup>26</sup> The primary goal of the Bankruptcy Code is to give the debtor a "fresh start."<sup>27</sup> The new Chapter 11 attempts to protect the creditor through reha-

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the "bargained-for" collateralization ratio and current collateral-debt ratio, and whether or not there is a controversy concerning the amount or validity of a secured creditor's claim." *Id.* at 189. Section 361 provides secured creditors a powerful forum early in the proceedings to make the court aware of any possible threats to their collateral. In facilitating reorganization, however, the Code may prove to be no more successful than its predecessor, the Bankruptcy Act, and for the same reason: secured creditors have, invariably, a veto over many if not most of the plans proposed under Chapter 11. This power permits the creditors to foreclose on their collateral and, in many cases, undermine the proposed plan, thus sending the debtor into liquidation. This is what the Code was intended to prevent. See Gordanier, *supra* note 12, at 299.

22. Massari, *supra* note 19, at 171.

23. *Id.*

24. Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5787 (codified at 11 U.S.C. §§ 101-151326 (1982)). The law took effect October 1, 1979. In 1984, Congress amended the Bankruptcy Code. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 333 (1984).

25. The last significant revision of the bankruptcy laws before the Bankruptcy Reform Act was the Chandler Act, ch. 575, 52 Stat. 840 (1938). The Bankruptcy Reform Act is the fifth bankruptcy law enacted by Congress. The prior acts were the Bankruptcy Act of 1800, ch. 19, 2 Stat. 19 (repealed 1803); Bankruptcy Act of 1841, ch. 9, 5 Stat. 440 (repealed 1843); Bankruptcy Act of 1867, ch. 176, 14 Stat. 517 (repealed 1878); Bankruptcy Act of 1898, ch. 541, 30 Stat. 544, amended by Chandler Act, ch. 575, 52 Stat. 840 (1938) (codified at 11 U.S.C. §§ 1-1103 (1976)) (repealed 1978).

For a brief history of the development of bankruptcy laws in the United States, see I W. NORTON, NORTON BANKRUPTCY LAW AND PRACTICE §§ 1.01-.03 (1981). For detailed information tracing the development of the Bankruptcy Reform Act, see Forman, *The Bankruptcy Reform Act*, PA. B. ASS'N Q., July, 1979, at 168. For an overview of the changes which the new statute created in bankruptcy law, see Patrick & Meyer, *An Overview of the Bankruptcy Reform Act of 1978*, 1 Bankr. 1 (1980).

26. See H.R. REP. NO. 95-595, 95th Cong., 2d Sess. 3-4, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5963, 5965. It has only been since the widespread adoption of the Uniform Commercial Code in the early 1960's that commercial credit has grown to its present magnitude. The report concluded that "[t]he Bankruptcy Act has not kept pace with the modern consumer credit society." *Id.* at 116-17, reprinted in 1978 U.S. CODE CONG. & AD. NEWS at 6077.

27. See, e.g., S. REP. NO. 95-989, 95th Cong., 2d Sess. 6, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5787, 5792; H.R. REP. NO. 595, 95th Cong., 1st Sess. at 220.

bilitation of the debtor as a going concern.<sup>28</sup> Alternatively, debtors may chose liquidation and discharge of debts under Chapter 7.<sup>29</sup>

### A. Adequate Protection

The concept of adequate protection stems from the fifth amendment, which provides that no private property shall be taken for public use<sup>30</sup> without just compensation.<sup>31</sup> A security interest has been determined to be a property interest within the meaning of the fifth amendment.<sup>32</sup> Therefore, any diminution in value of a security interest will constitute a "taking" if no compensation is offered to the creditor.<sup>33</sup> The Bankruptcy Code protects against an infringement on the creditor's property interests by implementing the concept of adequate protection.<sup>34</sup>

The phrase "adequate protection" originated in the Bankruptcy Act under section 77B(5).<sup>35</sup> Section 77B(5) provided for a "cram-down"<sup>36</sup> of creditors not accepting the debtor's plan of reorganiza-

28. See Note, *Standards and Sanctions for the Use of Cash Collateral Under the Bankruptcy Code*, 63 TEX. L. REV. 341, 341 (1984).

29. See 11 U.S.C. §§ 701-77 (Supp. II 1984).

30. A corporation is considered as a private entity. Thus, under Chapter 11, any taking of the creditor's property is arguably for a private, rather than a public use. See Comment, *Obtaining Operation Capital in a Chapter 11 Reorganization Proceeding Under § 363(c) and § 364(d) of The Bankruptcy Code*, 1983 ANN. SURV. BANKR. L. 217, 228 n.7.

31. U.S. CONST. amend. V. The fifth amendment states, in pertinent part, "[n]o person shall . . . be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation." *Id.*

32. See *Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555, 602 (1935).

33. *Ginsberg v. Lindel (In re Globe Dep't Store)*, 107 F.2d 721, 726 (8th Cir. 1939). The Eighth Circuit stated:

Of course under the bankruptcy power Congress may provide for the fair and equitable distribution of a debtor's property among his creditors; may discharge the debtor from liability for preexisting debts; may impair or destroy the obligation of the private contracts; and may effect changes in the lienholder's remedy or delay its enforcement . . . . Due process of law inhibits the taking of one man's property and giving it to another . . . without notice or an opportunity for a hearing . . . . Congress, in the exercise of the bankruptcy power . . . may not take a property right from one creditor and transfer it without compensation to another without violating the Fifth Amendment.

*Id.* (citations omitted); see also *In re Penn Cent. Transp. Co.*, 494 F.2d 270, 278 (3d Cir. 1974).

34. Adequate protection is defined in 11 U.S.C. § 361. For the text of section of section 361, see *supra* note 11.

35. Act of June 7, 1934, Pub. L. No. 73-296, § 77B(5), 48 Stat. 911, 914. Section 77B(5) was included as part of the 1934 amendments to the Bankruptcy Act of 1898. See *id.*

36. "Cram-down" refers to the process of confirming a plan of reorganization or arrangement over the dissent of a class of creditors. See Massari, *supra* note 19, at 189 n.2.

tion.”<sup>37</sup> Subsequently, the cram-down provision was adopted as revised in the 1938 Chandler Act amendments to the Bankruptcy Act.<sup>38</sup> The revised cram-down provisions of Chapters X and XII, in contrast to section 77B(5), provided the dissenting creditors adequate protection of their interest in the debtor’s property.<sup>39</sup> Accordingly, adequate protection issues under the language of section 77B arose only in the context of plan confirmation over the dissent of disgruntled creditors.<sup>40</sup> The change in language from the 1934 amendments to those of 1938 reflected that adequate protection was an equitable remedy for the dissenting creditor’s right to payment or possession of the collateral or the right to vote and participate in the reorganization plan.<sup>41</sup>

Adequate protection issues under section 361 of the Code, in contrast to Chapters X and XII of the Act, are confronted at the origin of the the reorganization process and thus do not directly impact plan confirmation.<sup>42</sup> Section 361, however, merges the adequate protection language of the Bankruptcy Act, section 77B(5), 216(7), and 461(11).<sup>43</sup> Therefore, case law interpretations of the former sections remain significant in analyzing section 361 of the Code.<sup>44</sup>

The purpose of adequate protection is “to insure that the secured creditor receives in value essentially what he bargained for.”<sup>45</sup> Thus,

37. See 11 U.S.C. § 77B(5) (1976). The substantive language of section 77B(5) required that there be a two-thirds majority of nonaccepting creditors in which case the cram-down provision provided “adequate protection for the realization by them of the value of their interest, claims, or liens . . . .” *Id.* Section 77B(5) provided four methods in which adequate protection could be provided. *Id.*

38. The revised edition of section 77B(5) was codified at section 216(7) of Chapter X and section 461(11) of Chapter XII. These are the “cram-down” provisions that are no longer used. *Cf.* 11 U.S.C. § 1129(b).

39. See Massari, *supra* note 19, at 173. Section 77B(5), on the other hand, provided for the realization by the creditor of its interest, claim, or lien. See 11 U.S.C. § 77B(5) (1976).

40. Massari, *supra* note 19, at 173.

41. *Id.*

42. See *id.*

43. Compare 11 U.S.C. § 361 (Supp. II 1984) with 11 U.S.C. §§ 77B(5), 216(7), 461(11) (1976).

44. See Massari, *supra* note 19, at 173.

45. H.R. REP. NO. 95-595, 95th Cong., 2d Sess., at 339, reprinted in 1978 U.S. CODE CONG. & AD. NEWS at 6295; see *United Virginia Bank v. Virginia Foundry Co.* (*In re Virginia Foundry Co.*), 9 Bankr. 493, 498 (W.D. Va. 1981). For an excellent discussion of adequate protection, see *Banker’s Life Ins. Co. v. Alyucan Interstate Corp.* (*In re Alyucan Interstate Corp.*), 12 Bankr. 803, 805-06 (Bankr. D. Utah 1981).

Some cases have interpreted adequate protection more in terms of contractual benefits than economic values. They have focused on language in the legislative history suggesting that secured creditors must receive the “benefit of their bargain.” H.R. REP. NO. 95-595, 95th Cong., 2d Sess., at 339, reprinted in 1978 U.S. CODE CONG. & AD. NEWS at 6295. Congress, however, was not referring to a contractual bargain between creditors and debtors because the next portion of the House Report

bankruptcy courts have required that creditors receive relief which results in the "realization of value."<sup>46</sup> Therefore, a primary design of section 361 is to alleviate the concerns of the creditor when the court approves the use of its collateral security in the debtor's plan of reorganization.<sup>47</sup> Adequate protection was not defined by Congress when it reformed the bankruptcy laws in 1978 and 1984.<sup>48</sup> Consequently, inferences drawn from the legislative history become impor-

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acknowledges, "[t]here may be situations in bankruptcy where giving a secured creditor an absolute right to his bargain may be impossible or seriously detrimental to the bankruptcy laws. Thus, [section 361] recognizes the availability of alternate means of protecting a secured creditor's interest." *Id.*

Whether and to what extent non-contractual or business elements of a bargain may be factored into the adequate protection equation is problematical. Some courts, employing an equity cushion analysis, insist that a ratio of debt to collateral is "bargained for" between debtor and creditor and must be considered in determining adequate protection. *See, e.g.,* Vlahos v. Pitts (*In re* Pitts), 2 Bankr. 476, 478 (Bankr. C.D. Cal. 1979). No secured creditor structures a transaction in such a fashion that the value of the property equals the amount of his claim. The existence of an equity, in terms of collateral value in excess of the secured creditor's claim, is an elementary and fundamental part of the transaction. *Id.*

Recent Eighth Circuit authority indicates that the "benefit of the bargain" may be only one element of adequate protection. *See* Lend Lease v. Briggs Transp. Co. (*In re* Briggs Transp. Co.), 780 F.2d 1339, 1346-47 (8th Cir. 1985). Indubitable equivalence was designed to broaden, not circumscribe the available solutions. *Id.* at 1346 (citing *In re* Shriver, 33 Bankr. 176, 184 (Bankr. N.D. Ohio 1983)). The requirement of indubitable equivalence must be construed as an alternative means of calculating value. *Briggs*, 780 F.2d at 1346 (citing *In re* Colrud, 45 Bankr. 169, 175 (Bankr. D. Ala. 1984)). Thus, the case law indicates that the creditors' rights to be afforded adequate protection depend on a variety of factors. *Id.*

46. *E.g.,* *Virginia Foundry*, 9 Bankr. at 498.

47. *See* Massari, *supra* note 19, at 172. Thus, the crux of adequate protection centers around the value of the creditor's interest at stake. The legislative history reflects this point: "[t]hrough the creditor might not receive his bargain in kind, the purpose of the section is to insure that the secured creditor receives in value essentially what he bargained for." H.R. REP. NO. 95-959, 95th Cong., 2d Sess., at 339, *reprinted in* 1978 U.S. Code Cong. & Ad. News at 6295. This point is reemphasized by noting that adequate protection is derived from the fifth amendment protection of property interests. *See* U.S. Const. amend. V. In *Wright*, Justice Douglas wrote the opinion which held that the bank received "the value of the [interest in] property" and that "there is no constitutional claim of a creditor to more than that." *Wright*, 311 U.S. at 278.

The *Alyucan* court stated:

[T]he 'interest in property' entitled to protection is not measured by the amount of the debt but by the value of the lien. A mushrooming debt, through accrual of interest or otherwise, may be immaterial if the amount of the lien is not thereby increased, while vicissitudes in the market, loss of insurance or other factors affecting the value of the lien are relevant to adequate protection. The purpose of adequate protection is to assure the recoverability of this value during the hiatus between petition and plan, or in the event the reorganization is stillborn, between petition and dismissal.

*Alyucan*, 12 Bankr. at 808.

48. Comment, *Adequate Protection*, 2 BANKR. DEV. J. 21, 22 (1985); *see* *Briggs*, 780 F.2d at 1344.



tant to determine exactly what Congress intended would constitute adequate protection.<sup>49</sup> At the very minimum, the debtor must assure the secured creditor that the value of its interest will be reasonably protected.<sup>50</sup> "When the status quo of the creditor's interest can be sustained, that interest is said to be adequately protected."<sup>51</sup>

Section 361 refers directly to the secured creditor's interest in the debtor's property.<sup>52</sup> The courts, however, have not agreed as to the extent to which the creditor's security position is to be protected.<sup>53</sup> The majority of courts hold that adequate protection of the secured creditor's interest includes the creditor's lost opportunity cost, or that amount the creditor might have earned on the reinvestment of its liquidated interest in the collateral had the stay<sup>54</sup> not been imposed.<sup>55</sup> Other courts use a more narrow interpretation, holding that this protection extends only to the value of the collateral at the time of filing debtor's petition for relief.<sup>56</sup> A split of authority in the federal courts indicates that this issue is still unresolved.<sup>57</sup>

According to the legislative history of section 361, there may be situations where giving a secured creditor an absolute right to its bargain is impossible or seriously detrimental to the policy behind the bankruptcy laws.<sup>58</sup> Thus, section 361 recognizes the availability of alternative means of protecting a secured creditor's interest.<sup>59</sup>

49. *Briggs*, 780 F.2d at 1344.

50. *See Smith v. Cooley (In re Cooley)*, 37 Bankr. 590, 592 (Bankr. E.D. Pa. 1984).

51. Comment, *supra* note 48, at 22; *see Fairchild v. Lebanon Prod. Credit Ass'n*, 31 Bankr. 789, 795 (Bankr. S.D. Ohio 1983).

The real question in any Chapter 11 proceeding is not whether a debtor is capable of maintaining the *status quo* (which typically is insolvency), but what are the prospects for retirement of debt. In the overall scheme of Chapter 11, adequate protection is not sufficient, and primary concern should instead be directed toward the content and viability of the plan of reorganization.

*Id.* at 795.

52. *See supra* note 34 and accompanying text.

53. Comment, *supra* note 48, at 22.

54. *See* 11 U.S.C. § 362 (1984).

55. *See In re American Mariner Indus., Inc.*, 734 F.2d 426, 435 (9th Cir. 1984); *Central Bank of Kansas City v. Orlando (In re Orlando)*, 53 Bankr. 245, 249-50 (Bankr. D. Minn. 1985); *In re Lilyerd*, 49 Bankr. 109, 117 (Bankr. D. Minn. 1985); *In re Trombley*, 34 Bankr. 141, 144 (Bankr. D. Vt. 1983); *In re Langley*, 30 Bankr. 595, 601-02 (Bankr. N.D. Ind. 1983).

56. *See, e.g., In re Sun Valley Ranches, Inc.*, 38 Bankr. 595, 597 (Bankr. D. Idaho 1984); *Shriver*, 33 Bankr. at 181-82; *In re South Village*, 25 Bankr. 987, 996-97 (Bankr. D. Utah 1982); *Alyucan*, 12 Bankr. at 808 (Bankr. D. Utah 1981).

57. *See supra* notes 55, 56 and cases cited therein; *see also Briggs*, 780 F.2d at 1350-51. The Eighth Circuit concluded that it could not hold, as a matter of law, that a creditor is always entitled to its lost opportunity costs. The court deferred final resolution to the bankruptcy courts for determinations based on individual fact situations.

58. *See H.R. REP. NO. 595, 95th Cong., 1st Sess. at 339 (1977).*

59. *Id.*

However, case law has interpreted adequate protection to be compensatory in nature, with the indubitable equivalent<sup>60</sup> standard under section 361(3)<sup>61</sup> contemplating total, not partial compensation.<sup>62</sup> This divergence in authority indicates a need for more certainty in this area of bankruptcy law. Ultimately, however, it is within the discretion of the bankruptcy court as to whether the creditor has been adequately protected.<sup>63</sup>

The landmark bankruptcy decision that dealt with the issue of adequate protection is *In re Murel Holding Corp.*<sup>64</sup> The importance of the *Murel* decision is that it set the foundation for a standard of review under adequate protection.<sup>65</sup> In the words of Judge Learned Hand,

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60. See *infra* note 65 and accompanying text.

61. 11 U.S.C. § 361.

62. In *Murel*, where Judge Learned Hand held that denial to the creditor of all amortization payments for a period of ten years was insufficient to justify a stay of the creditor's foreclosure proceeding because it constituted failure to provide the creditor with total compensation. See also *Virginia Foundry*, 9 Bankr. at 497 (court held that failure to provide secured creditor with interest payments at the current market rate denied creditor the benefit of his bargain since the creditor would have been entitled to the higher market rate had debtor not filed for bankruptcy). *Murel*, 75 F.2d at 942. But see *In re Besler*, 19 Bankr. 879, 884 (Bankr. D.S.D. 1982), in which the court decided that since adequate protection was merely interim protection for the duration of the automatic stay, a dilution in the value of the creditor's security interest was not sufficient to justify lifting the stay under section 362.

63. See *Briggs*, 780 F.2d at 1351. "Although the concept of adequate protection requires the court to protect the creditor's allowed [security interest], what constitutes adequate protection in a particular case is best left to the bankruptcy court." *Id.*

Under Bankruptcy Rule 810, a bankruptcy court's findings will be upheld on appeal unless clearly erroneous. "A finding is 'clearly erroneous' when although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed." *In re Stanely Hotel, Inc.*, 15 Bankr. 660, 662 (D.C. Colo. 1981) (quoting *United States v. United States Gypsum Co.*, 333 U.S. 364, 395 (1966)); see also *Martin*, 761 F.2d at 474 (bankruptcy court's factual findings should not be overturned unless clearly erroneous; its conclusions of law, however, are subject to *de novo* review).

This flexibility complies with the intent of the legislature that these matters are best left to a case-by-case interpretation and development. In light of the restrictive approach of the section to the availability of provisions for providing adequate protection, this flexibility allows the courts to adapt to varying circumstances and changing methods of financing. Pub. L. No. 95-598, 92 Stat. 2549, 5840; *Martin*, 761 F.2d at 474.

64. 75 F.2d 941 (2d Cir. 1935).

65. See *id.* at 942. "It is plain that 'adequate protection' must be completely compensatory. . . . [A creditor] wishes to get his money or at least the property. We see no reason to suppose that the statute was intended to deprive him of that in the interest of junior holders, unless by a substitute of the most indubitable equivalence." *Id.* One author has stated:

Judge Hand used the word "substitute" whereas section 361(3) speaks of "such other relief." Both reflect congressional policy and, in a sense, define the concept without limiting its application in any way. Thus, the debtor

now embodied in section 361(3) of the Code,<sup>66</sup> section 77B(5) required either payment in full or "a substitute of the most indubitable equivalence."<sup>67</sup> The legislative history implies that the indubitable equivalent language is intended to follow the strict approach taken by Judge Hand in *Murel*. *Murel* arose in the context of debtors' attempting to have their reorganization plans confirmed.<sup>68</sup> The Code, however, uses Judge Hand's phrase twice: first in section 361(3) (adequate protection prior to confirmation), and again in section 1129(b)(2)(A)(iii) (confirmation of the reorganization plan).<sup>69</sup> The difference in language between the "most indubitable equivalence" of Judge Hand and the "indubitable equivalent" of the Code could support a construction of section 361(3) that would afford somewhat greater flexibility for debtors than Judge Hand seems to suggest.<sup>70</sup> However, this is not a firmly held interpretation in light of the history

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must devise ways under any or all of the three subsections of section 361 to protect interests of secured creditors as well as its own interests.

Price, *Adequate Protection Under the Bankruptcy Act of 1978*, 71 Ky. L.J. 727, 741 (1983).

66. See 11 U.S.C. § 361(3). The Bankruptcy Code described indubitable equivalence as "granting such other relief, other than entitling such entity to compensation allowable under section 503(b)(1) of [Title 11] as an administrative expense, as will result in the realization by such entity of the indubitable equivalence of such entity's interest in such property." *Id.*

67. *Murel*, 75 F.2d at 942. Section 361(3) uses the words "indubitable equivalent" as opposed to "indubitable equivalence" as stated in *Murel*.

The legislative history indicates that indubitable equivalent was substituted for value in the final draft of section 361. See H.R. REP. NO. 95-595, 95th Cong., 2d Sess. 340, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 6296. Section 361(3) is derived from section 216(7)(d) of Chapter X of the superseded Bankruptcy Act. Section 216 of the Act required, inter alia, that a plan provide for adequate protection of secured creditors. If not otherwise supplied by the plan, "adequate protection for the realization by [secured creditors] of the value of their claims against the property" could be provided for "by such method as [would], under and consistent with the circumstances of the particular case, equitably and fairly provide such protection . . ." 11 U.S.C. § 216(7) (1976).

68. See *Murel*, 75 F.2d at 942. In *Murel*, the debtor proposed borrowing an additional \$11,000 to refurbish the mortgaged property for rent purposes. The lender was to have priority over existing mortgages. The secured creditor was to receive interest at 5 1/2%, but was to forego amortization payment for ten years. As Judge Hand stated, "[p]ayment ten years hence is not generally the equivalent of payment now. Interest is indeed the common measure of the difference, but a creditor who fears the safety of his principal will scarcely be content with that; he wishes to get his money or at least the property." *Id.* The order confirming the plan was reversed, and the creditor was allowed to foreclose. *Id.* at 943.

69. See 11 U.S.C. §§ 361(3), 1129(b)(2)(A)(iii).

70. See 2 L. KING., COLLIER ON BANKRUPTCY § 362.07[d][1], 362-52 to -53 (15th ed. 1985) [hereinafter cited as COLLIER]. The last alternative of § 361 should be applied narrowly, consistent with the standards of *Murel*. Bear in mind, however, that only the indubitable equivalent rather than the *most* indubitable equivalent is demanded. Ample room is given in § 361 for appropriate standards. *Id.* at 362-53.

of "indubitable equivalence" as it developed under the Act.<sup>71</sup>

### B. Cash Collateral

Prior to the Bankruptcy Code of 1978, the concept of cash collateral<sup>72</sup> was almost entirely judicially constructed. At that time, the Bankruptcy Act did not recognize cash collateral *per se*,<sup>73</sup> but the trend in case law was to consider cash collateral as distinct from other forms of property and, therefore, subject it to independent restrictions.<sup>74</sup>

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71. See Gordanier, *supra* note 12, at 317.

72. See 11 U.S.C. § 363(a). The Bankruptcy Code defines cash collateral as: 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 and includes the proceeds, products, offspring, rents, or profits of property subject to a security interest as provided in section 552(b) of this title, whether existing before or after the commencement of a case under this title.

*Id.*

This definition also includes proceeds that enter the estate after the petition is filed. See H.R. REP. No. 95-595, 95th Cong., 2d Sess. 344-45, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 6300-02 (stating that money from mortgage property coming into the estate after the petition is filed is cash collateral).

73. Cf. Webster, *Collateral Control Decisions in Chapter Cases: Clear Rules v. Judicial Discretion*, 51 AM. BANKR. L.J. 197, 214-21, 243-45 (1977) (examining the conflict between the Third Circuit's "clear rules test" and the discretionary "balancing test" applied to the control of cash collateral before passage of section 363(a)).

Two cases decided in the 1950's were particularly important to the later treatment of cash collateral. The first case, *Reconstruction Fin. Corp. v. Kaplan*, 185 F.2d 791 (1st Cir. 1950), departed from the traditional reluctance of the courts to apply turnover orders to cash collateral without the creditor's consent. The court treated cash collateral just as it would have treated other forms of collateral. *Id.* at 798. The Bankruptcy Code now distinguishes between cash collateral and other forms of property. See 11 U.S.C. § 363(c)(2).

The court in the second case, *Third Ave. Transit Corp. v. Lehman*, 198 F.2d 703 (2d Cir. 1952), reached a different conclusion about the nature of cash collateral. The *Third Ave.* court held that the debtor could use cash collateral only when "it is imperative to obtain the funds and . . . they cannot be obtained [elsewhere]." *Id.* at 706. This case differed from most disputes over cash collateral in that the issue was whether the creditor had to surrender funds he already had received. The usual case involves the creditor demanding that the debtor turn over funds. The parties in *Kaplan* also were in this reversed position. Regardless of who sues whom, the real dispute concerns who should have control of the collateral. If the debtor cannot obtain funds, the *Third Ave.* court stated, he must show a great likelihood that his business can be reorganized in a reasonable time and that the creditor will not be injured. *Third Ave.*, 198 F.2d at 706-07. Apparently, the court found cash collateral different from other forms of property and determined that the use of these funds should be subject to independent restrictions. See *id.*

74. See *supra* note 73 and accompanying text. The reaction to *Third Ave.* was diverse. Later cases eroded the standard of *Third Ave.* due to the implications by the courts that it was improbable that the debtor could make a showing that "reorganization was likely" at the beginning of bankruptcy. See *Charlestown Sav. Bank v. Martin (In re Colonial Realty Inv. Co.)*, 516 F.2d 154, 160-61 (1st Cir. 1975) (whether

The adoption of Article 9 of the U.C.C. radically altered commercial transactions.<sup>75</sup> Article 9 expanded the commercial importance of cash collateral by permitting a secured party to claim an interest in the cash or liquid proceeds from the sale of the original collateral.<sup>76</sup> Although Article 9 does not hinder the treatment of cash collateral in bankruptcy, the Bankruptcy Code recognizes the U.C.C.'s effect on cash collateral.<sup>77</sup> Article 9 also expanded the commercial importance of cash collateral by allowing a secured party to claim an interest in the cash or liquid proceeds from the sale of his original collateral.<sup>78</sup>

The Bankruptcy Code altered the treatment of cash collateral in many respects to conform to the increasing commercial reliance on cash collateral.<sup>79</sup> The Bankruptcy Code now recognizes the exten-

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there is sufficient possibility of a successful arrangement to justify whatever risk to the collateral of secured parties may be entailed); *In re Bermec Corp.*, 445 F.2d 367, 369 (2d Cir. 1971) (reasonable possibility of successful reorganization); *Freuhauf Corp. v. Yale Express Sys., Inc.* (*In re Yale Express Sys., Inc.*), 384 F.2d 990, 991 (2d Cir. 1967) (successful reorganization was a reasonable possibility). The Bankruptcy Code, however, effectively adopts the injury to the creditor criterion of *Third Ave.* See 11 U.S.C. § 362(d)(1) (requiring the trustee to provide adequate protection for the secured party's interest in the collateral to prevent lifting of the stay); *Id.* § 363(c)(2)(B) (requiring consent or notice and a hearing before the trustee uses cash collateral). Fifth amendment concerns were at the forefront of the decision, and indeed, the strict test in *Third Ave.* was partly prompted by constitutional considerations.

75. See Note, *supra* note 28, at 347.

76. The Uniform Commercial Code § 9-306(3)(6) provides that a security interest in proceeds is continuously perfected if "a filed financing statement covers the original collateral and the proceeds are identifiable cash proceeds." U.C.C. § 9-306(3)(b) (1985). Consequently, the major limitation with respect to a security interest in proceeds is the ability of the secured party to trace the proceeds.

77. Under the supremacy clause of the United States Constitution, U.S. CONST. art. VI, cl. 2, the Bankruptcy Code supersedes any state laws in the area of bankruptcy. The Uniform Commercial Code §§ 9-306(4)(b) to -306(4)(d) creates an interest that becomes valid only in the event of insolvency. The validity of these provisions is hotly debated because § 545 of the Bankruptcy Code invalidates every statutory lien that comes into effect upon the insolvency of the debtor. See Henson, "Proceeds" Under the Uniform Commercial Code, 65 COLUM. L. REV. 232, 242-47 (1965); see also *Commercial Credit Corp. v. Allen* (*In re Crosstown Motors, Inc.*), 272 F.2d 224, 227 (7th Cir. 1959) (voiding a similar provision in the Illinois Trust Receipts Act in the context of bankruptcy proceedings). If U.C.C. § 9-306(4)(d) is upheld, it will be because the courts view the section as a way to trace cash proceeds rather than as a separate lien coming into existence on the date of Bankruptcy Code.

78. See *supra* note 76.

79. See 11 U.S.C. § 363. The definition is not restricted to property of the estate that is cash collateral on the date of the filing of the petition. Thus, if non-cash collateral is disposed of and the proceeds come within the definition of cash collateral as set forth in this subsection, the proceeds would be cash collateral as long as they remain subject to the original lien on the non-cash collateral under § 552(b). To illustrate, rents received from real property before or after the commencement of the

sion of a security interest into cash proceeds,<sup>80</sup> but treats cash collateral proceeds as distinct from other forms of secured property.<sup>81</sup> The risk that cash collateral may be quickly consumed in a reorganization necessitates this difference in treatment.<sup>82</sup> The Bankruptcy Code responded to this risk by creating specific procedures the debtor must follow before cash collateral can be used.<sup>83</sup> In addition, the Code affords the creditor the right to adequate protection of its security interest in order to protect its value.<sup>84</sup>

The debtor's ability to use its assets immediately after filing for Chapter 11 relief is a requisite to the success of reorganization.<sup>85</sup> One of the most critical limitations on the debtor's use of property in

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case would be cash collateral to the extent that they are subject to a lien. 2 COLLIER, *supra* note 70, § 363.02, at 363-15.

80. See 11 U.S.C. § 363(a). Before the 1984 amendments to the Bankruptcy Code, a dispute existed about whether proceeds from a sale after the petition was filed were cash collateral and thus subject to the procedural and substantive protections of § 363. One commentator concluded that subjecting these funds to the strictures of § 363 would thwart the policy of rehabilitation because the debtor would be at the mercy of the secured creditor. See Levit, *Use and Disposition of Property Under Chapter 11 of the Bankruptcy Code: Some Practical Concerns*, 53 AM. BANKR. L.J. 275, 280-82 (1979). The majority view, however, was just the opposite. As stated in COLLIER, "if collateral which is not cash collateral becomes cash collateral during the case, these cash proceeds are, subject to the limitations of section 552, 'cash collateral' and the creditor is entitled to the protections of section 363(c)." 2 COLLIER, *supra* note 70, § 363.02, at 363-15. The legislative history also supports this argument. See S. REP. NO. 95-595, 95th Cong., 2d Sess. 55, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5841 (stating that rents received from mortgaged property after the commencement of the case are cash collateral to the extent that they are subject to a lien).

In the 1984 amendments to the Bankruptcy Code, Congress codified the majority view, set forth in COLLIER by inserting the words "whenever acquired" into the definition of cash collateral. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 333, 371 (1984) (codified at 11 U.S.C. § 363(a) (Supp. II 1984)). This reinforces the importance of cash collateral for a debtor throughout reorganization. The previous dispute and the resolution demonstrates that cash collateral was specifically designed to deal with concerns over a particular form of liquid collateral and was intended to be more than a limited restriction to the use of cash proceeds at the beginning of bankruptcy proceedings.

81. See 11 U.S.C. § 363.

82. See, e.g., 2 COLLIER, *supra* note 70, §§ 363.01[2], 363.02.

83. See 11 U.S.C. § 363(c).

84. *Id.*

85. Weintraub & Resnick, *From the Bankruptcy Court: The Use of Cash Collateral in Reorganization Cases*, 15 U.C.C. L.J. 168, 168 (1982). Ordinarily, a debtor in possession may sell, use, or lease its assets in the regular course of its business without court permission. *Id.*; see 11 U.S.C. § 363(c)(1). The reorganization plan is the cornerstone of Chapter 11. The plan structures the debtor's payments to creditors and attempts to present a workable alternative to foreclosure by the creditor. See 11 U.S.C. § 1123 (Supp. II 1984). Once the court confirms the plan, the debtor is free from court supervision and creditor attack as long as the scheduled payments of the plan are maintained. See 11 U.S.C. §§ 1141, 1142 (Supp. II 1984).

reorganization is the use of cash collateral.<sup>86</sup> In most situations, discontinuance of the debtor's business during the case would lead to the loss of customer goodwill, leaving rehabilitation impossible.<sup>87</sup> When the debtor must use cash collateral in the normal operation of the business and cannot obtain the secured party's consent, the exigent economic circumstances require prompt court approval.<sup>88</sup>

Whether the debtor will be able to reorganize frequently depends on the ability to use cash collateral because the inability to use collateral leads to the ultimate demise of the debtor.<sup>89</sup> Despite the critical importance of the use of cash collateral by the debtor, the Bankruptcy Code does not prescribe standards for its use.<sup>90</sup> The courts have failed to provide a consistent test for when the debtor may use cash collateral.<sup>91</sup>

## II. THE *MARTIN* DECISION

In *Martin*,<sup>92</sup> the Eighth Circuit Court of Appeals held that the issue of whether the debtor has provided adequate protection for a secured creditor is a question of fact.<sup>93</sup> The case was remanded to the

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86. See Weintraub & Resnick *supra* note 85, at 168.

87. See Note, *supra* note 28, at 342. Due to a need for working capital to keep the business open, the debtor may try to sell assets such as inventory or accounts receivable to obtain needed funds. In most cases, these assets will be covered by security interests that extend to the "proceeds" received from the sale of the assets. *Id.*

88. *Id.* Cash collateral is imperative to the debtor's reorganization, this is especially true where the business often uses accounts receivable as security for loans, and therefore, the major source of cash flow falls under the category of cash collateral. See Weintraub & Resnick, *supra* note 82, at 168. Under § 9-306 of the U.C.C., the accounts receivable financier will also have a security interest in the cash proceeds when the accounts are collected. *Id.* at 168 n.5.

89. Commentators describe cash collateral as the "lifeline" of a successful reorganization. Weintraub & Resnick, *supra* note 82, at 168. If the debtor can not use these funds, he may have to shut down. See *In re Sel-O-Rak Corp.*, 24 Bankr. 5, 7 (Bankr. S.D. Fla. 1982).

90. See 11 U.S.C. §§ 363(c), (e).

91. See, e.g., *In re Stein*, 19 Bankr. 458, 459-60 (Bankr. E.D. Pa. 1982) (the conflicting and irreconcilable interests of the parties must be balanced according to the circumstances and the equities of the case); *In re International Horizons*, 11 Bankr. 366, 368 (Bankr. N.D. Ga. 1981) (the court hinted that in some circumstances a debtor might have the free and unfettered use of cash collateral); *In re Prime, Inc.*, 15 Bankr. 216, 219 (Bankr. W.D. Mo. 1981) (the court determined a funding arrangement using cash collateral in the form of accounts receivable adequately protected creditor who had a second mortgage on real estate and a security interest in inventory and could maintain adequate protection into the future by limiting advances to new billings); *In re Gaslight Village, Inc.*, 6 Bankr. 871, 875 (Bankr. D. Conn. 1980) (if the court finds that the debtor should not have an unfettered right to use cash collateral, the court could either prohibit such use or allow the debtor to use the cash collateral).

92. 761 F.2d 472 (8th Cir. 1985).

93. *Id.* at 474. *Martin* is a consolidation of three debtors cases, including *In re*

bankruptcy court with specific instructions to accord sufficient weight to the statutory language and to the congressional goal of affording the secured creditor the benefit of its bargain.<sup>94</sup>

The debtors in *Martin* were farmers who filed petitions for reorganization under Chapter 11 of the Bankruptcy Code.<sup>95</sup> The debtors unsuccessfully attempted to secure loans from various lending institutions after filing their petitions.<sup>96</sup> In order to obtain the needed cash, the debtors proposed to sell grain stored in bins mortgaged to the creditor, the Commodity Credit Corporation (CCC).<sup>97</sup> The debtors filed motions in bankruptcy court requesting the use of cash collateral to finance the planting and harvesting of the 1984 crop.<sup>98</sup>

The bankruptcy court held that the debtors' offer of protection was adequate under the circumstances.<sup>99</sup> The CCC appealed from

Berg, 42 Bankr. 335 (D.N.D. 1984), and *In re Nikolaisen*, 38 Bankr. 267 (Bankr. D.N.D. 1984).

As a result of this holding, the issue of adequate protection is subject to the clearly erroneous standard of review. See *Martin*, 761 F.2d at 474.

94. See *Martin*, 761 F.2d at 478 (quoting *In re American Mariner Indus.*, 734 F.2d 426, 434-35 (9th Cir. 1984)). The *Martin* court indicated:

On remand, the bankruptcy court should initially decide: whether an adequate protection determination will have any practical effect at this time. This will depend upon an evaluation of the individual debtor's situation: are they still in possession of the land; have they made other financial arrangements for the current crop year; have arrangements been made for someone else to farm their land in the current year. If the bankruptcy court concludes that an adequate protection determination will have present significance, it should then proceed to apply the correct legal standard and consider additional evidence in light of the opinion.

*Id.* at 478-79.

95. *Id.* at 473.

96. *Id.*

97. *Id.* The CCC is an agency of the United States government whose primary purpose is to stabilize, support, and protect the agricultural commodities market. See 15 U.S.C. § 714 (1982).

The CCC argued that the use of cash collateral would, in effect, place them in a position of a lending institution, a purpose for which the agency was not designed. The bankruptcy court dealt this argument a swift blow by holding that if the CCC grain were deemed not available to § 363 use by a farmer, a dichotomy would exist which might well emasculate a farmer's ability to successfully reorganize. *Nikolaisen*, 38 Bankr. at 269. It would be a dichotomy because the CCC program is a set aside program intended principally to assist farmers, who by reason of financial distress, have the CCC grain as their only source of cash for ongoing operations. *Id.* at 270.

98. *Martin*, 761 F.2d at 473.

99. *Nikolaisen*, 38 Bankr. at 270. The CCC argued that the debtors' offer of adequate protection of future interest was too speculative and not the equivalent of the interest in the stored grain. The bankruptcy court held, however, that "it is virtually certain between a first lien on 1984 crops and an assignment of crop insurance proceeds, that Commodity Credit will be insured a return of its interest." *Id.* The debtors clearly showed that the use of cash collateral is necessary to continue efforts at reorganizing their farming operation. Also, it was extremely unlikely, as a result of



the bankruptcy court order to the district court, which reversed and held that the offer of adequate protection was not the "indubitable equivalent" of a lien on already existing commodities in storage.<sup>100</sup>

On appeal, the debtors argued that the value of the first lien on the 1984 crop exceeded the value of the collateral being requested from the CCC.<sup>101</sup> The Eighth Circuit, however, agreed with the district court that the bankruptcy court was incorrect in determining that the CCC's security interest was adequately protected.<sup>102</sup> Specifically, the bankruptcy court failed to apply the standard of adequate protection mandated by section 361(3).<sup>103</sup>

The Eighth Circuit was confronted with two issues in *Martin*. First, did the bankruptcy court apply the correct legal standard in finding that the debtors' offer of a substitute lien in the 1984 crop, along

the strained relationship with the financial institutions, that the debtors would be able to obtain financing other than through cash collateral. *Id.*

100. *Berg*, 42 Bankr. at 338. The district court concluded that an offer of a lien on a crop contemplated to be grown in 1984, plus an assignment of federal crop insurance proceeds, is not adequate protection. The court distinguished the bankruptcy court's holding by showing that the cases relied upon by the debtors all dealt with existing collateral, where, as a practical matter, the debtors have provided a promise of collateral which may not exist in the future. "This is, in effect, an offer of no collateral at all." *Id.* The court was quick to point out the speculative nature of a crop not yet in existence, by noting that weather, fire, explosions or other disasters could partially or totally destroy the 1984 crop. *Id.*

101. *Martin*, 761 F.2d at 475. The debtors also argued that a lack of adequate protection would be realized only if there was a failure of the crop. The relevant testimony produced at the hearing on the motion before the bankruptcy court regarding the Martin 1984 farming operation included the following:

- (1) Martins are requesting the use of \$162,642.00 in cash collateral;
- (2) Martins have been farming in the Hunter-Arthus, N.D. area since 1946;
- (3) Martin's 1984 crop will consist of: 478 acres of corn (at 100% share), 68 acres of corn (at 75% share), 365 acres of soybeans (at 100% share), 75 acres of navy beans (at 76% share);
- (4) Anticipated revenues from the 1984 crop are \$279,676.00;
- (5) Projected yields and unit prices are based on 1984 proven yields and government loan prices;
- (6) Anticipated expenses to plant, bring to maturity and harvest the 1984 crop total is \$162,642.00 ;
- (7) Martins will obtain \$174,242.00 in federal crop insurance coverage, based upon their increased proven yield;
- (8) Martins have sought financing for 1984 operating costs from private lending institutions and were unable to obtain such financing; and
- (9) It is customary for lenders in this area to loan money to farmers to put in crops and to secure repayment with a crop mortgage;

Brief for Appellant at viii-ix, *In re Martin*, 761 F.2d 472 (8th Cir. 1985).

102. *Martin*, 761 F.2d at 475.

103. *Id.* In reaching this conclusion, the court relied primarily on the wording of the applicable statutory provisions and their legislative histories. Under the circumstances, the court felt it appropriate to remand the case back to the district court with instructions to remand to the bankruptcy court to apply the correct standard. Accordingly, the court did not reach the issue of whether the bankruptcy court's finding that the CCC's interest was adequately protected is clearly erroneous. *See id.* at 478.

with an assignment of federal crop insurance proceeds, adequately protected the CCC's security interest?<sup>104</sup> Second, assuming the adequate protection standards were met, did the bankruptcy court's determination of adequate protection fulfill the clearly erroneous standard of review?<sup>105</sup> Ultimately, however, the court only dealt with the first issue.<sup>106</sup>

### A. Adequate Protection Analysis

The court's analysis of adequate protection was directed at the proposed use of cash collateral by the debtor.<sup>107</sup> The crux of the analysis focused, in particular, on the indubitable equivalent requirement of section 361(3).<sup>108</sup> The court looked to the legislative history and case law to interpret the meaning of section 361(3).<sup>109</sup>

Significant reliance was placed in Judge Learned Hand's explanation of adequate protection in *Murel*.<sup>110</sup> Specifically, the court focused its analysis on the indubitable equivalent language coined by Judge Hand.<sup>111</sup> The court recognized the inherent uncertainty of the indubitable equivalent requirement exemplified by the inconsistent original House and Senate versions of section 361.<sup>112</sup> Although

104. *Martin*, 761 F.2d at 475.

105. *Id.*

106. *See id.*

107. *Martin*, 761 F.2d at 473-74. Section 363(e) of Chapter 11 provides that whenever the bankruptcy trustee proposes to use, sell, or lease property of the bankruptcy estate in which the creditor has an interest, the court shall, at the request of the creditor, "prohibit or condition such use, sale, or lease as is necessary to provide adequate protection of [the creditor's] interest." 11 U.S.C. § 363(e).

108. *See* 11 U.S.C. § 361. For the text section 361, *see supra* note 11.

109. *See Martin*, 761 F.2d at 475-76.

110. *See Murel*, 75 F.2d at 942.

111. *See Martin*, 761 F.2d at 476.

It is plain that "adequate protection" must be completely compensatory; and that payment ten years hence is not generally the equivalent of payment now. Interest is indeed the common measure of the difference, but a creditor who fears the safety of his principal will scarcely be content with that; he wishes to get his money or at least the property. We see no reason to suppose that the statute was intended to deprive him of that in the interest of junior holders, unless by a substitute of the most indubitable equivalence.

*Murel*, 75 F.2d at 942.

112. *See Martin*, 761 F.2d at 476. Inclusion of the indubitable equivalent concept occurred as the result of a legislative compromise. The original House and Senate versions of section 361 differed in certain important respects. Both bills offered in identical form the two subsections that presently are codified as §§ 361(1)-(2). The House version, however, contained two additional methods of providing adequate protection. *Id.*

The first method granted the secured creditor an administrative expense priority to the extent of the loss. H.R. REP. NO. 95-595, 95th Cong., 2d Sess. 340, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 6296. The Senate, however, deleted this provision, recognizing that "such protection is too uncertain to be meaningful." *Martin*, 761 F.2d at 476; S. REP. NO. 95-989, 95th Cong., 2d Sess. 54, *reprinted in* 1978 U.S.

the final draft of section 361(3) is similar to the original House version, the court noted the conspicuous additional requirement, that other forms of adequate protection provide the secured creditor with the indubitable equivalent of its present interest.<sup>113</sup> The Eighth Circuit concluded from the legislative history that a debtor, in structuring a proposal of adequate protection, "should as nearly as possible . . . provide the creditor with the value of its bargained for rights."<sup>114</sup>

The determination of adequate protection for a secured creditor is a question of fact.<sup>115</sup> Therefore, whether adequate protection exists in a given case depends on the nature of the collateral and the debtor's proposed use of that collateral.<sup>116</sup> To encourage reorganization and provide greater predictability, the court formulated a three-part adequate protection test.<sup>117</sup> In any given case, the bankruptcy court must necessarily (1) establish the value of the secured creditor's interest; (2) identify the risks to the secured creditor's value resulting from the debtor's request for use of cash collateral; and (3) determine whether the debtor's proposal protects the value of the collateral against risks consistent with the concept of indubitable equivalence.<sup>118</sup> In addition, the Eighth Circuit emphasized that in order to encourage reorganization, the adequate protection standard must be applied in a flexible manner.<sup>119</sup>

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CODE CONG. & AD. NEWS 5840. The House bill also permitted the courts to provide other forms of protection "that will result in the realization by the [secured party] of the value of its interest in the property involved." *Martin*, 761 F.2d at 476; H.R. REP. NO. 95-595, 95th Cong., 2d Sess. 340, reprinted in 1978 U.S. CODE CONG. & AD NEWS at 6296. The Senate bill contained no such provision. *Martin*, 761 F.2d at 476; S. REP. NO. 95-989, 95th Cong., 2d Sess. 54, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5840.

Subsection 3, in its final form, allows the courts discretion to grant other forms of adequate protection to a secured creditor. *Martin*, 761 F.2d at 476; see 11 U.S.C. § 361(3).

113. *Martin*, 761 F.2d at 476. The court noted that it had recently recognized that a reorganization plan "may be confirmed over the objections of a secured creditor if the plan affords the creditor the indubitable equivalent of his claim." *Id.*; see *In re Monnier Bros.*, 755 F.2d 1336, 1338 (8th Cir. 1985). Effectively, the court is providing a link between confirmation of the reorganization plan and adequate protection analysis of cash collateral at the beginning of the proceedings.

114. *Martin*, 761 F.2d at 476 (citing *American Mariner*, 734 F.2d at 435).

115. *Id.* at 474.

116. *Id.* at 476.

117. *Id.* at 476-77.

118. *Id.*; see *In re George Ruggiere Chrysler-Plymouth*, 727 F.2d 1017, 1019 (11th Cir. 1984) (whether a creditor's secured interest is are protected, there must be an determination of the value of that interest and whether a proposed use of cash collateral is a threat to that value).

119. *Martin*, 761 F.2d at 476. The flexibility, however, must not operate to the detriment of the secured creditor's interest. *Id.*

The court then highlighted the reasons for the bankruptcy court's failure to adequately establish the value of the CCC's security interest.<sup>120</sup> The *Martin* court cited two reasons. First, the court noted that the debtors provided no documentary evidence of estimated 1984 crop yields.<sup>121</sup> Calculation of the 1984 crop value was a condition precedent to determine the indubitable equivalence of a creditor's security interest in stored grain.<sup>122</sup> Second, the Eighth Circuit ruled that the bankruptcy court failed to identify the risk to the secured creditor's interest in a nonexistent crop.<sup>123</sup> A crop failure, unless due to "unavoidable consequences" within the meaning of the debtor's federal crop insurance policy, would leave the creditor's security interest completely unprotected and valueless.<sup>124</sup> In order to redress the failure of the bankruptcy court, the Eighth Circuit identified the associated risks and consequences of a crop failure and listed the factors the bankruptcy court should consider.<sup>125</sup> The court, however, did not intend to create an exclusive list but merely an illustrative one.<sup>126</sup> The *Martin* court stressed that the concerns it expressed are not insurmountable, but merely in accord with congressional

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120. *Id.* at 477. In addressing the bankruptcy court's flawed analysis, the *Martin* court found itself wedged between the competing interest of the debtor and the creditor. *See id.*

121. *Id.*

122. *Id.* The bankruptcy court noted the constant fluctuation of market prices in farm products. This market price analysis addressed the same concern as that in *Monnier*, 755 F.2d at 1338-40 (an interest award held as necessary to protect a mortgagee from loss of the use of money resulting from reorganization).

The *Martin* court also mentioned that the bankruptcy court may want to consider whether the CCC is entitled to interest for any delay in repayment occasioned by the debtor's proposed use of cash collateral. *Martin*, 761 F.2d at 477. This issue is analogous to the one decided in *American Mariner*, where the undersecured creditor, which was stayed by the bankruptcy petition from repossessing its collateral, was entitled, under the concept of adequate protection, to compensation for delay in enforcing its rights against the collateral. *American Mariner*, 734 F.2d at 431-35.

123. *Martin*, 761 F.2d at 477.

124. *Id.* The debtor's policy specifically disclaimed any liability for crop failure resulting from the farmer's neglect or failure to follow good husbandry practices. *See id.*

125. *Id.* at 477. The *Martin* court stated:

On remand, the bankruptcy court should consider: the anticipated yield in light of the productivity of the land; the husbandry practices of the farmer, including his proven crop yields from previous years; the health and reliability of the farmer; the condition of the farmer's machinery; whether there are encumbrances on the machinery which may subject it to being repossessed before the crop is harvested; the potential encumbrances on the present or future crop by other secured creditors; the availability of crop insurance and the risk of crop failure not covered by the crop insurance; and the anticipated fluctuation in market price of the farmer's crop.

*Id.*

126. *See id.* The court stated, "[t]hese factors are by no means exclusive but merely illustrative of ones affecting CCC's security interest." *Id.*

policy.<sup>127</sup> The bankruptcy court must ultimately decide whether the debtor's adequate protection proposal provides protection to the creditor consistent with the concept of indubitable equivalence.<sup>128</sup> The concept of indubitable equivalence mandates "such relief as will result in the realization of value."<sup>129</sup> If adequate protection cannot be afforded as set forth above, the debtor's motion to use cash collateral should be denied.<sup>130</sup>

### III. ANALYSIS AND CONSEQUENCES OF THE *MARTIN* DECISION

In *Martin*, the Eighth Circuit balanced the competing interest of debtor rehabilitation and the secured creditor's right to the benefit of its bargain.<sup>131</sup> The court's three-part test implies that the debtor must convey more than a personal guarantee as adequate protection of the secured creditor's interest.<sup>132</sup> The result of the Eighth Circuit's modified adequate protection test is twofold. First, the Eighth Circuit's test provides the debtor, the creditor, and the courts greater predictability.<sup>133</sup> Second, a heavier burden is placed on the debtor by accelerating confirmation issues to the pre-confirmation stage.<sup>134</sup>

127. *Id.*

128. *Id.*

129. *Id.*; see *In re Sheehan*, 38 Bankr. 859, 864 (D.S.D. 1984). The *Sheehan* court stated:

[t]he use of alternative means of protecting the value of a secured creditor's interest is recognized, so long as the creditor receives in value essentially what it bargained for . . . . Congress intended adequate protection to be flexible to permit courts to adapt to varying circumstances and changing modes of financing. Finally, Congress expected that adequate protection would be further developed on a case-by-case basis.

*Id.*

130. *Martin*, 761 F.2d at 478. The CCC also argued that the debtor's sale of grain and use of cash collateral would be inconsistent with the statute and regulations concerning price support programs. Specifically, the CCC's position was that it is not set up to provide loans to farmers. The court rejected this argument for two reasons. First, the regulation cited by CCC, 7 C.F.R. § 1421.19(a), was not applicable to the debtor's situation. Second, no provisions in the Bankruptcy Code indicate that Congress intended the CCC to be treated differently from other secured creditors seeking adequate protection under § 363. *Id.*

131. See *Martin*, 761 F.2d at 475-79.

132. See *id.* at 477.

133. See *id.* at 475-79; see also *Clarkson v. Cooke Sales & Service Co. (In re Clarkson)*, 767 F.2d 417, 419-20 (8th Cir. 1985) (failure of feasibility of plan was the lack of detailed reports of the plan). Prior to this test, the debtor could not place much stock in the indubitable equivalent requirement because it was dependent upon the facts of each individual case. See *infra* notes 143-45 and accompanying text.

134. See *infra* notes 156-66 and accompanying text.

### A. Adequate Protection Analysis

It is generally assumed that a debtor require cash collateral in order to rehabilitate its business.<sup>135</sup> Thus, the dispositive issue in a section 361(3) hearing is whether the secured creditor can be adequately protected by being granted an interest in something other than the collateral at issue.<sup>136</sup> The inherent problem in farm reorganization cases arises when the offer of adequate protection for the use of cash collateral is insufficient or simply speculative.<sup>137</sup> This predicament is magnified, as in *Martin*, when the farmer attempts to liquidate stored grain which is subject to a lien.<sup>138</sup> The *Martin* court found that the amorphous indubitable equivalence test<sup>139</sup> produced inconsistent results in reorganization cases.<sup>140</sup> In order to alleviate this problem, the court established a more reliable test. Although the *Martin* test employed the indubitable equivalence language, the test will produce more consistent results.<sup>141</sup> It accomplishes this by delineating specific factors the court considers in determining whether the creditor's right to indubitable equivalence has been satisfied in the context of cash collateral.<sup>142</sup>

*Martin* represents the current trend of the law.<sup>143</sup> Circuit courts

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135. Note, *supra* note 30, at 221.

136. *See id.* It has been stated:

[i]f there is no way to offer adequate protection to the creditor, the use of cash collateral must be prohibited. In such a situation the debtor's business will probably fail, and courts are reluctant to acquiesce in the premature demise of the debtor's business. Thus, courts will often search for sources of protection until they reach the level of security called "adequate protection."

*Id.*

137. *See infra* notes 143-45.

138. *See Martin*, 761 F.2d at 473.

139. *See id.* at 477-78. The bankruptcy and district courts also applied the indubitable equivalent test. *See, e.g., Berg*, 42 Bankr. at 338; *Nikolaisen*, 38 Bankr. at 269-70.

140. This is evidenced by the fact that the *Martin* court established criteria for bankruptcy courts to use in the future. *Martin*, 761 F.2d at 476-77.

141. *Id.* The bankruptcy court must necessarily determine the following: (1) establish the value of the secured creditor's interest; (2) identify the risks to the secured creditor's value resulting from the debtor's request for use of cash collateral; and (3) determine whether the debtor's adequate protection proposal protects value as nearly as possible against risks to that value consistent with the concept of indubitable equivalence. *Id.*

142. *See id.* Previously, the debtor had only the indubitable equivalence language of § 361(3) to rely upon. *See* 11 U.S.C. § 361(3).

143. Other federal courts have denied cash collateral proposals similar to *Martin*'s. *See, e.g., Bankwest, N.A. v. Todd*, 49 Bankr. 633, 638 (D.S.D. 1985) (while question of whether adequate protection exists in particular case depends upon nature of collateral and nature of debtor's proposed use of collateral; it is plainly not enough in any case for a debtor to merely make predictions for adequate protection); *First Bank of Miller v. Wieseler*, 45 Bankr. 871, 878 (D.S.D. 1985) (a bare replacement lien in nonexistent crops did not meet burden of proof of adequate protection because the

have generally found adequate protection lacking when the creditor is not reasonably assured of receiving its bargain in kind.<sup>144</sup> Only a minority of courts, however, have allowed the use of cash collateral where the adequate protection proposal included a detailed analysis of the reorganization plan, which dispelled mere speculation.<sup>145</sup>

Whether the debtor will be able to reorganize is frequently contingent upon the ability to utilize cash collateral.<sup>146</sup> Consequently, the

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debtor didn't make apparent profitability potential); *Berg*, 42 Bankr. at 338 (offer of lien on nonexistant crop, plus crop insurance held not adequate because value to creditor was less than promise); Philadelphia Consumer Discount Co. v. Commercial Credit Bus. Loans, Inc. (*In re Philadelphia Consumer Discount Co.*), 37 Bankr. 946, 948-49 (E.D. Pa. 1984) (cash collateral offered represented loan receivables; debtors may not merely theorize that such protection might materialize); International Harvester Credit Corp. v. Trombley (*In re Trombley*), 34 Bankr. 141, 144 (Bankr. D. Vt. 1983) (debtor's payment under plan not adequate where a mere bare promise of periodic payments was given); *In re Schaller*, 27 Bankr. 959, 961-62 (W.D. Wis. 1983) (equity cushion did not itself offer adequate protection where it was being rapidly eroded by interest); *In re C.F. Simonin's Sons, Inc.*, 28 Bankr. 707, 713 (Bankr. E.D.N.C. 1983) (lender's adequate protection had to include payment of lost opportunity costs, in view of fact that debtor's chance of successful reorganization was highly speculative). *Cf.* Dahlquist v. First Nat'l Bank, 40 Bankr. 969, 971 (D.S.D. 1983) (where cattle being fed and crops irrigated and cared for, use of cash collateral is necessary and value of security is enhanced); Federal Land Bank v. Carson (*In re Carson*), 34 Bankr. 502, 507 (D. Kan. 1983) (otherwise sufficient equity cushion may not adequately protect creditor if cushion is being eroded by accruing interest and/or depreciation); *Ahucyan*, 12 Bankr. at 809 (creditor holding debtor's realty not entitled to stay relief on grounds of adequate protection where creditor had first lien with ample collateral to protect itself).

144. Compare *American Mariner*, 734 F.2d at 432 (sections 361 and 362(d) were drafted to insure that the creditor receives the value of its interest) and *Murel*, 75 F.2d at 942 (the plan must provide adequate protection for the dissenting class of the full value of their interest, claims, or liens; it must be completely compensatory) with *Monnier*, 755 F.2d at 1340 (secured creditor was not inadequately protected where with equity cushion, value of property as of confirmation date would have been more than enough to satisfy debtor's obligation to creditor) and *George Ruggiere*, 727 F.2d at 1020 (since value of creditor's secured interest was the wholesale value, the bankruptcy court's allowing debtor to use only gross profits and requiring that it remit the wholesale value to the creditor did not impair creditor's secured interest).

145. See *In re Berens*, 41 Bankr. 524, 527-28 (Bankr. D. Minn. 1984) (adequate protection was offered to the extent that debtors would plant the crop on their own land, but adequate protection was not offered with respect to crop which was to be planted on rented land); *Sheehan*, 38 Bankr. at 868 (chapter 11 debtor's offer of adequate protection, anchored by replacement lien in 1984 crops and supported by substantial testimony regarding prospective farm operations and management by tested, experienced professionals, was sufficient to warrant grant of motion by debtors to use cash collateral for post petition financing for spring planting); *In re Heatron, Inc.*, 6 Bankr. 493, 496-97 (Bankr. W.D. Mo. 1980) (debtor's motion to use cash collateral granted because even conservative appraisals revealed value of security exceeded the amount of debt).

146. See Note, *supra* note 28, at 342. A debtor's ability to use its assets immediately after the filing of a Chapter 11 petition is often crucial to the success of the reorganization process. Pursuant to the Bankruptcy Code, a debtor in possession

inability to use this powerful tool for reorganization is a contributing factor which may result in the debtor's liquidation.<sup>147</sup> The *Martin* court's analysis of adequate protection, in relation to cash collateral, addressed the need for certainty and predictability in this volatile area of bankruptcy law.<sup>148</sup> Prior case law failed to provide a consistent test for determining when a debtor may use cash collateral,<sup>149</sup> and consequently, what constitutes adequate protection.<sup>150</sup>

Subsequent cases have interpreted *Martin* as requiring the debtor to produce a detailed analysis of the cash collateral proposal.<sup>151</sup> In

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ordinarily may sell, use, or lease its assets in the regular course of its business without court permission. See 11 U.S.C. § 363(c)(1). One of the most important limitations on a debtor's use of property in reorganization cases relates to the use, sale, or lease of cash collateral. When the debtor must use cash collateral in the normal operation of the business, and is unable to obtain the secured party's consent, it is imperative to obtain court approval promptly. The debtor's lifeline may be cut off, after the petition for reorganization is filed, if it is unable to use cash collateral on very short notice. This is especially true of a business in financial trouble because they often use accounts receivable as security for loans, and therefore, the only major source of cash flow falls within the category of cash collateral. Congress also realized the potentially crippling side effects of the limitation on the use of cash collateral and provided an ameliorative procedure granting the debtor an early day in court. Weintraub & Resnick, *supra* note 85, at 168-69.

147. As previously stated, cash collateral is described as the lifeline of a successful reorganization. See Weintraub & Resnick, *supra* note 85, at 168; see also *Sel-O-Rak*, 24 Bankr. at 7 (if the debtor cannot use these funds, he may have to shut down).

148. See *Martin*, 761 F.2d at 476-77. Standards developed to govern cash collateral would be relevant only for the period between the filing of the petition and the plan's confirmation by the court. The provisions on preferential transfers govern payments to creditors before the petition is filed. See 11 U.S.C. § 547 (1984). The plan governs payments to creditors after the court confirms the plan. See 11 U.S.C. §§ 1126-1146 (1984). Moreover, such standards apply only in those cases in which a secured party does not consent to the use of cash collateral. See 11 U.S.C. § 363(c)(2)(A). If the creditor consents, presumably the debtor can use cash collateral in any way that does not contravene the consent agreement. Thus, the bankruptcy court is not involved.

149. Although bankruptcy courts have tried to devise workable standards, they have failed to develop consistent rules. Some courts have adopted a balancing test that tries to reconcile the demands of debtors and creditors. See *Stein*, 19 Bankr. at 459-60; *Mickler*, 9 Bankr. at 123. Another court opted for a chronological test based upon immediate need. See, e.g., *International Horizons*, 11 Bankr. at 368. One court thought that in some circumstances a debtor might have the unfettered use of cash collateral. *Gaslight Village*, 6 Bankr. at 875. In another case the court appeared to look only to the adequate protection of the creditors. *Prime*, 15 Bankr. at 219.

150. See *supra* notes 143-45 and accompanying text.

151. See *Todd*, 49 Bankr. at 638 (plainly not enough for a debtor to merely make predictions, write them down and offer them as exhibits showing adequate protection). Prior case law supports this conclusion. Compare *Wieseler*, 45 Bankr. at 876 (debtors in the instant case must go beyond simply estimating what they hope they can harvest and what they hope the market will bring for it) with *Berens*, 41 Bankr. at 527-28 (adequate protection sufficient where debtors plant crop on own land as opposed to rented land and have all-risk insurance), and *Sheehan*, 38 Bankr. at 868



order for the debtor to obtain the use of cash collateral, the debtor's plan of reorganization must at least demonstrate: (1) the value of the creditor's collateral; (2) a replacement lien of equal or greater value; (3) all risk insurance; and (4) a detailed analysis illustrating adequate protection of the creditor's interest.<sup>152</sup>

In adopting these factors, the *Martin* court has arguably narrowed the traditional indubitable equivalence standard. Bankruptcy courts might disregard the broad indubitable equivalence language of section 361(3) by adhering to the narrower adequate protection considerations established in *Martin*. In applying the Eighth Circuit's adequate protection factors, however, bankruptcy courts would be mindful of the Code's traditional goal of debtor rehabilitation.<sup>153</sup> Considering this goal, section 361 should not be interpreted too narrowly. If so construed, it would undoubtedly thwart many reorganization proceedings and defeat the underlying policy of debtor rehabilitation.<sup>154</sup> This is particularly true of adequate protection proceedings in the very early stages of a bankruptcy case.<sup>155</sup>

### B. Analogy with Confirmation of the Plan

Section 1129(a)(11) of the Bankruptcy Code, requires, as a condition of confirmation, that the debtor is unlikely to need further financial reorganization.<sup>156</sup> Section 1129(a)(11) requires the court to scrutinize the reorganization plan to determine whether it offers a

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(debtor's 11-point offer of adequate protection was sufficient to warrant grant of motion to use cash collateral).

152. Cf. *Martin*, 761 F.2d at 477 (requiring debtor to establish and protect the associated risk affecting the creditor's security interest); *Todd*, 49 Bankr. at 638 (debtor must offer exhibits evidencing adequate protection); *Wieseler*, 45 Bankr. at 876 (citing lack of all risk insurance as a factor along with mere estimations by debtor); *Berens*, 41 Bankr. at 527 (lack of all risk insurance); *Sheehan*, 38 Bankr. at 868 (detailed analysis offering adequate protection sufficient).

153. Massari, *supra* note 19, at 171. "Under Chapter 11 the purposes of business reorganization 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 business's finances so that it may continue to operate, provide its employees with jobs, pay its creditors, and produce a return for its stockholders.'" See *Martin*, 761 F.2d at 475 (quoting *American Mariner*, 734 F.2d at 431 (quoting H.R. REP. NO. 95-595, 95th Cong., 2d Sess. at 220, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS at 6179)).

154. See H.R. REP. NO. 95-595, 95th Cong., 2d Sess. 220, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 6179.

155. There is a strong presumption in favor of rehabilitation early in the proceeding. *In re Colonial Realty*, 519 F.2d 154, 160 (1st Cir. 1975). This presumption wanes if the proceedings continue without a successful plan or other arrangement being made by the debtor. Massari, *supra* note 19, at 173 n.111.

156. 11 U.S.C. § 1129(a)(11) (1982) provides that, "[c]onfirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorgani-

reasonable prospect of success.<sup>157</sup> The purpose of the feasibility requirement is to prevent confirmation of visionary or impracticable schemes.<sup>158</sup> As a result, Congress included the indubitable equivalent language not only in section 361(3), but also in section 1129 of the Code.<sup>159</sup> The reason for including it in both code sec-

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zation, of the debtor or any successor to the debtor under the plan, unless such liquidation or reorganization is proposed in the plan." *Id.*

Section 1129(a)(11) was written pursuant to feasibility tests contained in §§ 221(2), 366(2), and 472(2) of the Bankruptcy Act, which were applicable, respectively, in Chapter X, Chapter XI and Chapter XII cases. 5 COLLIER, *supra* note 70, ¶ 1129.02[11], at 1129-36.

157. See *United Properties Inc. v. Emporium Dep't Stores, Inc.*, 379 F.2d 55, 65-66 (8th Cir. 1967) (quoting *In re Transvision, Inc.*, 217 F.2d 243, 246 (2d Cir. 1955)). In *United Properties*, the Eighth Circuit reversed a lower court order finding a plan of arrangement to be feasible on the grounds that the evidence failed to establish that the debtor could operate at a profit, that the absence of evidence justified inventory valuation which called into question the debtor's solvency, and that the debtor's projected cash flow could not reasonably be expected to sustain the debtor's business and permit the debtor to make payments required under its plan of arrangement. *Id.*

Basically, feasibility involves the question of the emergence of the reorganized debtor in a solvent condition and with reasonable prospects of financial stability and success. It is not necessary that success be guaranteed, but only that the plan present a workable scheme of organization and operation from which there may be a reasonable expectation of success. 5 COLLIER, *supra* note 70, ¶ 1129.02, at 1129-33.

158. However honest in its efforts the debtor may be, and however sincere its motives, the district court is not bound to clog its docket with visionary or impracticable schemes for resuscitation. See *Tennessee Publishing Co. v. American Nat'l Bank*, 299 U.S. 18, 22 (1936).

159. See 11 U.S.C. §§ 361(3), 1129(b). Section 1129(b) provides in pertinent part:

(b)(1) Notwithstanding section 510(a) of this title, if all of the applicable requirements of subsection (a) of this section other than paragraph (8) are met with respect to a plan, the court, on request of the proponent of the plan, shall confirm the plan notwithstanding the requirements of such paragraph if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims of interest that is impaired under, and has not accepted, the plan.

(2) For the purpose of this subsection, the condition that a plan be fair and equitable with respect to a class includes the following requirements:

(A) with respect to a class of secured claims, the plan provides—

(i)(I) that the holders of such claims retain the liens securing such claims, whether the property subject to such liens is retained by the debtor or transferred to another entity, to the extent of the allowed amount of such claims; and

(II) that each holder of a claim of such class receive on account of such claim deferred cash payments totaling at least the allowed amount of such claim, of a value, as of the effective date of the plan, of at least the value of such holder's interest in the estate's interest in such property;

(ii) for the sale, subject to section 363(k) of this title, of any property that is subject to the liens securing such claims, free and clear of such liens, with such liens to attach to the proceeds of such sale, and the treatment of such liens on proceeds under clause (i) or (iii) of this subparagraph; or

(iii) for the realization by such holder of the indubitable equivalent of such claims.

tions is that the creditor's security interest is at risk at both the confirmation<sup>160</sup> and pre-confirmation<sup>161</sup> stages.

In *Martin*, the court established several factors the bankruptcy court will consider at the pre-confirmation stage.<sup>162</sup> Comparing the *Martin* factors with those established under the feasibility test of section 1129, the similarities are obvious.<sup>163</sup> Both Code provisions utilize similar prospective analytical factors. The difference is that adequate protection is a pre-confirmation issue, while feasibility is a confirmation issue.<sup>164</sup>

The upshot of utilizing factors in an adequate protection analysis, which are similar to those used in a confirmation analysis, is that it accelerates confirmation issues to the pre-confirmation stage. In effect, this denies the debtor the breathing period provided by the automatic stay of section 362 of the Code. It also contravenes the legislative policy of providing the debtor with a fresh start.<sup>165</sup> The general trend in bankruptcy law has gone against the farmer-debtor.<sup>166</sup> *Martin* imposes the burden the debtor of gathering complex information and making accurate predictions with very little time to do so. Requiring the debtor to provide feasibility-type predictions to fulfill adequate protection requirements at the pre-confirmation stage imposes an almost impossible burden.

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*Id.* § 1129(b) (emphasis added).

160. See 11 U.S.C. § 1129(b)(2).

161. *Id.* §§ 361, 363.

162. See *Martin*, 761 F.2d at 477.

163. See *Clarkson*, 767 F.2d at 420. The Second Circuit has declared that feasibility contemplates "the probability of actual performance of the provisions of the plan. Sincerity, honesty, and willingness are not sufficient to make the plan feasible, and neither are any visionary promises. The test is whether things which are to be done after confirmation can be done, as a practical matter, under the facts." *In re Bergman*, 585 F.2d 1171, 1179 (2d Cir. 1978). Again, the pertinent factors to consider include the business's earning power, the sufficiency of its capital structure, general economic conditions, managerial efficiency, and whether the same management will continue to operate the company. *In re Great N. Protective Serv., Inc.*, 19 Bankr. 802, 803 (Bankr. W.D. Wash. 1982).

Where the debtor is engaged in business, the court should consider the adequacy of the capital structure. See *In re Pressed Steel Car Co.*, 16 F. Supp. 329, 339 (W.D. Pa. 1936) (decided under the former § 77B). The court should also consider the economic conditions, the ability of management, the probability of a continuation of the same management, and any other related matters which determine the prospects of a sufficiently successful operation to enable performance of the provisions of the plan. See generally 5 COLLIER *supra* note 70, at § 1129.02 (discussing the provisions of the feasibility requirement).

164. See 11 U.S.C. §§ 361(3), 1129(a)(11). Adequate protection is not a standard which the Bankruptcy Code uses in connection with confirmation decisions. Instead, the adequate protection requirements apply primarily in the context of preconfirmation proceedings. See *Monnier*, 755 F.2d at 1340.

165. See *supra* note 19.

166. See *supra* note 143.

## CONCLUSION

In *Martin*, the Eighth Circuit concerned itself with balancing the competing interests of debtor and creditor in the cash collateral context. In order to provide greater predictability in farm bankruptcy cases, the court outlined specific factors bankruptcy courts must consider in evaluating the indubitable equivalence requirement. These factors, aside from promoting greater predictability, also have a negative effect on a farmer's ability to use cash collateral. Congressional policy promotes the rehabilitation of the depressed farm economy by providing the debtor with a fresh start.<sup>167</sup> Under *Martin*, however, the debtor is faced with the possible consequence of confirmation denial at the pre-confirmation stage.<sup>168</sup>

The result after *Martin* is that the farmer-debtor will have to prove a potential for successful reorganization before the court will grant a large scale cash collateral proposal.<sup>169</sup> The practical significance of *Martin* is that bankruptcy courts may disregard the broad indubitable equivalent language of section 361(3) by adhering to the more narrow adequate protection considerations established by the Eighth Circuit.<sup>170</sup> While *Martin* provides a more tangible standard, the policy behind the indubitable equivalent language of broadening the range of solutions available to the debtor<sup>171</sup> may be overlooked. Accelerating confirmation issues to the pre-confirmation stage does an injustice to the debtor and defeats the overall policies of the bankruptcy laws.

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167. See *supra* note 27 and accompanying text.

168. Cf. *Martin*, 761 F.2d at 477-79.

169. *Id.* Subsequent caselaw interpreting *Martin* has indicated this trend. See *Todd*, 49 Bankr. at 637-38.

170. See *Martin*, 761 F.2d at 477 (describing the adequate protection factors the bankruptcy court should consider).

171. See *Briggs*, 780 F.2d at 1346.

