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Bankruptcy Code Does Not Require Periodic Postpetition Payments to Undersecured Creditors for Interest on Value of Collateral as Compensation for Delay of Chapter 11 Reorganization Proceedings during Pendency of Automatic Stay.

Robert J. Ogle

CASENOTE

BANKRUPTCY—Adequate Protection—Bankruptcy Code Does Not Require Periodic Postpetition Payments to Undersecured Creditors for Interest on Value of Collateral as Compensation for Delay of Chapter 11 Reorganization Proceedings During Pendency of Automatic Stay

In re Timbers of Inwood Forest Associates
808 F.2d 363 (5th Cir. 1987) (en banc)

In June, 1982, Timbers of Inwood Forest Associates, Ltd. (Timbers) obtained a loan of $4,100,000 from United Savings Association of Texas (United) for the purpose of constructing an apartment complex in northwest Houston.[1] The ten-year loan was secured by a deed of trust on the apartment buildings and an assignment of rental payments.[2] Payments for the first three years were to be $45,842.06 per month, plus a monthly escrow payment of $7,956 for taxes and insurance, resulting in a total payment of $53,798.06.[3] Timbers ceased making payments after August 1984, and United subsequently gave notice of its intent to foreclose.[4] On March 4, 1985, Timbers filed a petition under Chapter 11 of the Bankruptcy Code, resulting in an automatic stay of the foreclosure proceedings.[5] On March 18, 1985, United moved for relief from the stay.[6] United relied upon section 362(d)(1) of the Bankruptcy Code, which provides relief "for cause, includ-

1. *See In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380, 1383 (5th Cir. 1986) (ten-year note, in amount of $4,100,000, was executed by Timbers in June of 1982), *aff'd on rehearing*, 808 F.2d 363 (1987) (en banc).

2. *See id.* (United received deed of trust and assignment of rents as security).

3. *See id.* (terms of note required monthly payments of $45,842.06 for interest and principal, and $7,956 for monthly escrow to cover taxes and insurance).

4. *See id.* (at some point after August 1984, United noticed foreclosure on apartment complex).

5. *See id.* (agreed order entered requiring Timbers to pay United net income produced by apartments).

6. *See id.*

ing lack of adequate protection" of a security interest.[7] The bankruptcy court held an evidentiary hearing and found that United was an undersecured creditor and was thus denied adequate protection.[8] The court ordered Timbers to pay United a "lost opportunity cost" of 12% of the collateral's value.[9] This payment was to be payable out of the rental receipts.[10] The United States District Court for the Southern District of Texas affirmed the Bankruptcy Court's decision.[11] United thereafter appealed to the United States Court of Appeals for the Fifth Circuit.[12] Held—*Reversed and Remanded*.[13] Adequate protection provisions of the Bankruptcy Code do not require periodic postpetition payments to undersecured creditors for interest on the value of their collateral as compensation for the delay of Chapter 11 reorganization proceedings during the pendency of the automatic stay.[14]

Chapter 11 of the United States Bankruptcy Code provides a method by which a debtor may obtain temporary relief from the claims of his creditors.[15] The purpose of the temporary relief is to provide the debtor with an opportunity to evaluate its income and debt, preserve the bankruptcy estate, and formulate a plan for repayment of debt from future earnings.[16] The

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7. *See id.*

8. *See id.* Expert testimony produced by Timbers indicated that the property's fair market value was $4,250,000, while the outstanding debt amounted to $4,366,388.77, leaving the creditor undersecured. The court held that the denial of adequate protection was United's inability to foreclose on its collateral and reinvest the proceeds of resale. *See id.* at 1383-84.

9. *See id.* The court ordered payment of 12% of $4,250,000, which the court found to be the fair market value of the collateral.

10. *See id.* (lost opportunity costs are synonymous with present value in proceeds of resale).

11. *See id.* at 1384.

12. *See id.* at 1382-83. United cross-appealed, complaining that the formula developed by the bankruptcy court to determine the opportunity cost payments was incorrect. *See id.* at 1382-83.

13. *See id.* at 1416.

14. *See id.* at 1416. The holding in the en banc opinion corresponds with the holding in the panel opinion. The en banc opinion reinstated the panel opinion, added to the majority opinion, and included a concurrence and a dissent. *See In re* Timbers of Inwood Forest Assocs., 808 F.2d 363 (5th Cir. 1987) (en banc).

15. *See* 11 U.S.C. §§ 1101-74 (Supp. 1985). Congress introduced Chapter 11 by amending the Bankruptcy Act of 1898 with the Chandler Act in 1938. *See* Chandler Act, ch. 575, Pub. L. No. 696, 52 Stat. 840 (1938). The Bankruptcy Reform Act, generally referred to as the Bankruptcy Code, replaced the Bankruptcy Act of 1898. *See* Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified as amended at 11 U.S.C. §§ 101-1330 (Supp. 1985)).

16. *See* H.R. REP. NO. 595, 95th Cong., 1st Sess. 339, *reprinted in* 1978 U.S. CODE CONG. AND AD. NEWS 5963, 6295.

> The purpose of a business reorganization case, unlike a liquidation case, is to restructure a business' finances so that it may continue to operate, provide its employees with jobs, pay

bankruptcy debtor has the exclusive right to file a plan with the bankruptcy court within 120 days following the filing of the petition, after which time its creditors may file a plan.[17] The plan will place creditors with similar claims into separate classes.[18] The classes of creditors may then vote to accept or reject the debtor's plan for repayment.[19] The bankruptcy court will confirm a plan if the Code requirements are met and the plan is accepted by all impaired creditors.[20] An impaired creditor is one whose claim will not be repaid in full or whose legal rights will be altered.[21] Unimpaired creditors are conclusively presumed to have accepted the plan since they will be fully compensated for their interests.[22] In the event that certain classes of credi-

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its creditors, and produce a return for its stockholders. The premise of a business reorganization is that assets that are used for production in the industry for which they were designated are more valuable that those same assets sold for scrap . . . . It is more economically efficient to reorganize than to liquidate, because it preserves jobs and assets. *Id.*

17. *See* 11 U.S.C. § 1121 (1982 & Supp. 1985). Section 1121 provides that a plan may be filed only by the debtor for 120 days following the date of filing, after which time a party in interest may file a plan. A party in interest may include the debtor, the trustee, a creditor's committee, an equity security holder's committee, a creditor, an equity security holder, or an indenture trustee. *See id. See generally* Rosen and Rodriguez, *Section 1121 and Non-Debtor Plans of Reorganization*, 56 AM. BANKR. L.J. 349 (1982) (general discussion of reorganization plans).

18. *See* 11 U.S.C. § 1122 (1982 & Supp. 1985). Section 1122 provides that claims are to be grouped into classes with those which are substantially similar. Section 1123 requires that a debtor's plan must provide equal treatment to creditors within the same class and must specify whether the class is impaired or unimpaired. *See id.* at § 1123. For a general discussion of classification claims see Anderson, *Classification of Claims and Interest in Reorganization Cases Under the New Bankruptcy Code,* 58 AM. BANKR. L.J. 99 (1984); Watkins, *The Chapter 11 Plan,* PRAC. LAW, Dec. 1982, at 11.

19. *See* 11 U.S.C. 1126 (1982 & Supp. 1985). A creditor who holds a claim allowed under the Code may accept or reject a plan. *See id.*

20. *See* 11 U.S.C. 1129 (1982 & Supp. 1985). Section 1129 provides for confirmation of a plan under two conditions: plans accepted by every class, and plans accepted by less than every class. A plan which is accepted by less than every class may be confirmed if at least one impaired class has voted to accept the plan, the plan does not discriminate unfairly, and the plan is fair and equitable. Whether the plan is accepted by all classes or less than all classes, the section lists eleven requirements which must be met. *See id.* For a discussion regarding confirmation of reorganization plans by the cram-down method, see Broude, *Cramdown and Chapter 11 of the Bankruptcy Code: The Settlement Imperative,* 39 BUS. LAW 441 (1984); Epling, *Cramdown Under the Bankruptcy Code of 1978: Effect Upon the Soft Collateral Lender,* 12 LOY. U. CHI. L.J. 627 (1981); Klee, *All You Ever Wanted to Know About the Bankruptcy Cramdown Under the New Bankruptcy Code,* 53 AM. BANKR. L.J. 133 (1979); Miller, *Bankruptcy Code Cramdown Under Chapter 11: New Threat to Shareholder Interests,* 62 B.U.L. REV. 1059 (1982).

21. *See* 11 U.S.C. § 1124 (1982 & Supp. 1985). A claim is impaired if it will not be repaid in full or its legal rights altered. An interest is also considered impaired if it is adversely affected. *See id.*

22. *See* 11 U.S.C. § 1126(f) (1982 & Supp. 1985). Unimpaired creditors are conclusively

tors do not accept the plan, the bankruptcy court may confirm the plan by a "cram-down" procedure.[23] This procedure applies when a majority of at least one class of impaired creditors votes to accept the plan, and the plan is fair and equitable with regard to all classes of claims.[24] The confirmation of a plan will be based on the debtor's ability to repay the claims filed against the estate by his creditors.[25]

In the course of a Chapter 11 proceeding, a creditor is limited as to the claims it may make against the bankrupt's estate.[26] Generally, the creditor must comply with filing provisions and is precluded from making certain claims, including a claim for unmatured interest.[27] However, an exception

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presumed to have accepted the plan, and the debtor need not solicit acceptance from the unimpaired creditor. *See id. See generally* Fogel, *Confirmation and the Unimpaired Class of Creditors: Is a "Deemed Acceptance" Deemed an Acceptance?,* 58 AM. BANKR. L.J. 151 (1984) (discussing acceptance and acceptance requirements).

23. *See* 11 U.S.C. § 1129 (1982 & Supp. 1985). Subsection (b) provides that the court may confirm a plan even if it is not accepted by all classes of creditors if the plan is fair and equitable as defined in subsection (b)(2). *See id.*

24. *See* 11 U.S.C. § 1129(b) (1982). A requirement of confirmation is that at least one class of claims has accepted the plan. *See id.* The plan is deemed accepted by a class of claims if accepted by the holders of at least two-thirds of the total amount claimed and more than one-half of total number of claims. *See* 11 U.S.C. § 1126(c), (d) (1982 & Supp. 1985). The plan must also be fair and equitable. *See* 11 U.S.C. 1129 (b)(2) (1982 & Supp. 1985). In order for a plan to be fair and equitable with respect to a class of secured claims, section 1129 (b)(2)(A) requires that: (1) the holder of the secured claim retains its lien, (2) the payments made must total the amount of the allowed secured claim, and (3) the payments have a present value equal to the value of the collateral. *See id.*

25. *See, e.g.,* Pizza of Hawaii, Inc. v. Shakey's, Inc., 761 F.2d 1374, 1382 (9th Cir. 1985) (plan which failed to provide for payment of civil judgment was not confirmed); *In re* Neff, 60 Bankr. 448, 452 (Bankr. N.D. Tex. 1985) (plan must provide for payments to creditor of at least the amount he would receive in Chapter 7 liquidation); *In re* Brusseau, 57 Bankr. 457, 459 (Bankr. D.N.D. 1985) (confirmation of plan depends on ability of debtor to pay claims at least in amount that would be provided pursuant to Chapter 7 liquidation).

26. *See* 11 U.S.C. § 502 (1982 & Supp. 1985). This section excludes certain claims and limits allowable claims to those which are properly filed. *See id.* Section 101 defines a claim as either a right to payment or an equitable right to a remedy which would give rise to payment. *See id.* at 101. For a discussion of what claims are allowed under the Bankruptcy Code, see 3 Collier on Bankruptcy, ch. 501 (15th ed. 1985); Blum, *Treatment of Interest on Debtor Obligations in Reorganization Under the Bankruptcy Code,* 50 U. CHI. L. REV. 430 (1983); Weintraub and Resnick, *Allowance of Claims and Priorities Under the New Bankruptcy Code,* 12 U.C.C. L.J. 291 (1980).

27. *See* 11 U.S.C. § 501(a) (1982 & Supp. 1985) (creditor may file proof of claim); 11 U.S.C. § 502(a) (1982 & Supp. 1985) (claim on interest filed pursuant to section 501 is deemed allowed unless objected to by party in interest); *see also* 11 U.S.C. § 502(b)(2) (1982 & Supp. 1985) (claim filed under section 501 is allowed except to extent that it is for unmatured interest). For a discussion of the creditor's approach to making a claim, see generally Hagedorn, *The Survival and Enforcement of the Secured Claim Under the Bankruptcy Reform Act of 1978,* 54 AM. BANKR. L.J. (1980); Rubner, *The Secured Creditor's Initial Response to a Chap-*

to this rule is contained in section 506.[28] This exception provides that an oversecured creditor may be entitled to postpetition interest as an element of its claim.[29] An oversecured creditor is one to whom the amount owed is exceeded by the value of the collateral securing the obligation.[30] The reasoning behind this exception is that the payment of interest to the creditor will not diminish the estate to an amount less than the outstanding debt.[31] This pre-Code principle of bankruptcy law was retained when the bankruptcy laws were codified in the Bankruptcy Reform Act of 1978.[32]

Prior to the Bankruptcy Act of 1898, bankruptcy law had provided that interest does not accrue on debts after a bankruptcy petition is filed.[33] This rule came into effect in order to protect the bankruptcy estate for the benefit of both the debtor and the creditor, as well as to avoid penalizing the debtor who, by operation of law, was prevented from paying his debts.[34] The ex-

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ter 11 Filing, 9 COLO. LAW 2370 (1980); Weintraub and Resnick, *Allowance of Claims and Priorities Under the New Bankruptcy Code*, 12 U.C.C. L.J. 291 (1980).

28. *See* 11 U.S.C. § 506 (1982 & Supp. 1986).

29. *See id.* To the extent that a secured claim is secured by property valued in excess of the value of the claim, the holder of the claim is allowed interest on the claim. *See id. See generally* Blum, *Treatment of Interest on Debtor Obligations in Reorganizations Under the Bankruptcy Code*, 50 U. CHI. L. REV. 430 (1983) (discussing creditor's rights to interest in reorganization provisions of Bankruptcy Code).

30. *See In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380, 1381 (5th Cir. 1986) (an oversecured creditor is "a secured creditor whose collateral is worth more than the amount of its debt"), *aff'd on rehearing*, 808 F.2d 363 (1987) (en banc).

31. *See* Matter of Anderson, 6 Bankr. 601, 610-11 (Bankr. S.D. Ohio 1980) (undersecured creditor is not allowed to collect interest, which would result in prejudice to rights of other creditors).

32. *See In re* United Merchants and Mfr., Inc., 674 F.2d 134, 138 (2nd Cir. 1982) (section 506(b) merely codifies pre-Code law that oversecured creditor may claim interest under credit agreement); *see also* H.R. REP. NO. 595, 95th. Cong., 1st Sess. 356 (1977); S. REP. NO. 989, 95th Cong., 2d Sess. 68 (1978). Section 506(b) codified the current law by allowing an oversecured creditor to collect fees, costs and charges arising from the agreement forming the basis of the claim. Such fees are available only to the extent that the value of the debt is exceeded by the value of the collateral. *See id.*

33. *See* Nicholas v. United States, 384 U.S. 678, 691 (1986) (government denied claim for interest on taxes due); Vanston Bondholders Protective Comm. v. Green, 329 U.S. 156, 163 (1946) (corporate debtor under reorganization not required to pay interest on bonds); Sexton v. Dreyfus, 219 U.S. 339, 344 (1911) (secured creditors not allowed to apply proceeds of sale of security to interest accruing since filing of petition); Thomas v. Western Car Co., 149 U.S. 95, 116-17 (1893) (owner and lessor of railroad car not entitled to interest on mortgage from defaulting lessee during period in which they were in litigation).

34. *See* Vanston Bondholders Protective Comm. v. Green, 329 U.S. 156, 163 (1946). Payment of interest has been suspended by law since it has been considered to be a penalty imposed for the delay in prompt payment, which is a necessary incident to the settlement of the estate. Allowing the payment or accrual of postpetition interest in favor of one creditor would prejudice the rights of other creditors. *See id.*; *see also* Ticonic Nat'l Bank v. Sprague, 303 U.S. 406, 411 (1938) (to ensure equity among creditors, accrual of interest after date of

ception allowing interest payments to oversecured creditors was also recognized in early bankruptcy cases.[35] These cases held that interest could be paid, and the creditors protected, if the value of the collateral exceeded the amount of the debt.[36] This rule survived the enactment of the Bankruptcy Code and still is of significant importance with regard to filing bankruptcy under Chapter 11.[37]

An entity need not "qualify" or be insolvent to file a Chapter 11 bankruptcy petition, but the entity must be a "person" as defined in Chapter 7.[38] Chapter 7 provides that a "person" is an individual, partnership, or corporation.[39] A bankruptcy petition may be filed by the debtor pursuant to section 301 as a voluntary proceeding.[40] A creditor, meeting the requirements of section 303, may also file a petition as an involuntary proceeding.[41] The Code allows the bankruptcy court to maintain control over a Chapter 11 proceeding by empowering the court to either dismiss a Chapter 11 case or convert it to a Chapter 7 liquidation if the likelihood of rehabilitation is absent, or if there is difficulty in formulating or implementing an adequate reorganization plan.[42]

A petition filed under either section 301 or section 303 results in an automatic stay which becomes effective as of the date the petition is filed and continues until it is either lifted by the courts or until the property in question is no longer the property of the estate.[43] The stay prevents creditors

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insolvency is not allowed); Thomas v. Western Car Co., 149 U.S. 95, 116-17 (1893) (interest is not permitted on claims against mortgagor).

35. *See* Sexton v. Dreyfus, 219 U.S. 339, 346 (1911) (the right to apply proceeds to interest is intended where the security is worth more than the debt); Code v. Arts, 152 F. 943, 950 (8th Cir. 1907) (trustee is entitled to payment of interest where proceeds of resale are in excess of debt), *aff'd*, 213 U.S. 223 (1909).

36. *See* Vanston Bondholders Protective Comm. v. Green, 329 U.S. 156, 164-65 (1946) (inequitable to allow interest payments to secured creditor where security was worth less than debt).

37. *See* 11 U.S.C. § 506 (1982 & Supp. 1985).

38. *See id.* § 101(30).

39. *See id.*; *see also* 11 U.S.C. § 109(a) (1982 & Supp. 1985) (Chapter 7 debtor must be "person" under section 101(30)); 11 U.S.C. 109(d) (1982 & Supp. 1985) (any person who may be debtor under Chapter 7, except stockbroker or commodity broker, may be debtor under Chapter 11).

40. *See* 11 U.S.C. § 301 (1982 & Supp. 1985) (voluntary case is commenced by filing of petition with bankruptcy court by debtor).

41. *See id.* § 303 (involuntary case may be commenced against debtor by filing of petition by holder of claim against debtor).

42. *See* 11 U.S.C. § 1112 (1982 & Supp. 1985).

43. *See id.* § 362(a) (1982 & Supp. 1985) (petition filed under §§ 301, 302 and 303 operates as stay of any proceeding to recover claim against creditor); *id.* § 362(c) (1982 & Supp. 1985) (stay of any claim against property of estate is effective until property is not property of estate); *id.* § 362(d) (1982 & Supp. 1985) (court may lift stay upon request of party in interest).

from taking any further action against the debtor or against the property of the estate in order to collect on their claims or enforce their liens.[44] The purpose of the stay is to temporarily protect the debtor and thereby enhance its chances for a successful reorganization or organized liquidation.[45] The stay is intended not only to give the debtor temporary protection from its creditors but also to protect the creditors' rights in the collateral.[46] The creditors may eventually assert their claims, which will be repaid upon confirmation of the plan by the bankruptcy court.[47] The creditors are further protected by provisions which allow the stay to be lifted.[48]

A bankruptcy court may grant relief from the stay upon the request of a party in interest.[49] The court is empowered to modify or terminate the stay either: (1) for cause, including lack of adequate protection of an interest in the property; or (2) if the debtor does not have any equity in the property and the property is not necessary for an effective reorganization.[50] The Code does not define adequate protection but does state that a party who is not

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44. *See* Carlton v. BAWW, Inc., 751 F.2d 781, 785-86 (5th Cir. 1985) (automatic stay prevents creditor from continuing to pursue cause of action to void fraudulent transfer); *In re* Towner Petroleum Co., 48 Bankr. 182, 185 (Bankr. W.D. Okla. 1985) (automatic stay implements goals of preventing dissipation of debtor's assets during pendency of bankruptcy case). For a discussion of the application of the automatic stay, see generally Campbell, *The Automatic Stay in Bankruptcy*, 10 HOUS. LAW. 10 (1983); Kennedy, *Automatic Stays Under the New Bankruptcy Law*, 12 U. MICH. J.L. REF. 1 (1978); *see also In re* Leonard Morgan, 9 BANKR. CT. DEC. (CRR) 926, 928 (Bankr. E.D. Pa. 1982) (stay continues until property is no longer property of estate); *In re* Knight, 3 COLLIER BANKR. CAS. 2D (MB) 742, 746-47 (Bankr. D. Md. 1981) (stay terminated when trustee abandoned estate's interest in property).

45. *See* H.R. REP. NO. 595, 95th Cong., 1st Sess. 340-2 (1977); S. REP. NO. 989, 95th Cong., 2d Sess. 49-51 (1978) (automatic stay is fundamental protection provided by bankruptcy law to protect debtor from claims of his creditors, and permit him to create repayment or reorganization plan).

46. *See id.*; *see also* 11 U.S.C. § 362 (1982 & Supp. 1985). The stay continues until the property is no longer the property of the estate or the case is closed or dismissed. Subsection (e) provides that the stay automatically terminates with respect to a party in interest who has requested relief from the stay, unless the court orders the stay to continue in effect after conducting a hearing. *See id.*

47. *See* 11 U.S.C. § 1129 (1982 & Supp. 1985) (plan will be confirmed if requirements are met, resulting in payment of allowed claim); *id.* § 502 (1982 & Supp. 1985) (defines what claims may be allowed).

48. *See id.* § 362 (1982 & Supp. 1985).

49. *See id.* § 362(d) (1982 & Supp. 1985) (on request from party in interest court may grant relief from stay); *see also* Cathey v. Johns Manville Sales Corp., 711 F.2d 60, 63 (6th Cir. 1983) (bankruptcy court has exclusive authority to grant relief from automatic stay under section 362(d)). *See generally* Martin, *Creditor Alternative to Obtain Relief from Automatic Stays in Bankruptcy*, 87 COM. L.J. 22 (1982) (examination of creditors' options in seeking relief from stay); O'Toole, *Adequate Protection and Post Petition Interest in Chapter 11 Proceedings*, 56 AM. BANKR. L.J. 251 (1982) (general discussion of adequate protection in Chapter 11 context).

50. *See* 11 U.S.C. § 362(d) (1982 & Supp. 1985). Once relief is requested, the burden of

provided adequate protection may be compensated in one of three ways.[51] The first method requires the trustee to make cash payments to a creditor to the extent that the stay results in a decrease in the value of the creditor's interest in the collateral.[52] Secondly, the creditor is provided with a lien to the extent that the stay results in a decrease in the value of the creditor's interest in the collateral.[53] Finally, other relief can be granted which will result in the realization by the creditor of the "indubitable equivalent" of his interest in the collateral.[54] The Code's inclusion of the term "indubitable equivalent" has been the source of considerable debate as to the nature and extent of adequate protection.[55]

The current controversy surrounding Chapter 11 bankruptcy proceedings stems from the dispute of whether adequate protection includes payments of present value or interest on the value of the collateral to an undersecured creditor during the pendency of Chapter 11 proceedings.[56] While the first two subsections of section 361 contemplate a decrease in the value of the creditor's interest in the property as lack of adequate protection, the third

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proof is upon the debtor to prove that the creditor's interest is adequately protected. *See id.* § 362(g)(2) (1982).

51. *See id.* § 361 (1982 & Supp. 1985). *See generally* Jack, *Adequate Protection*, 2 BANK. DEV. J. (1985) (general discussion of adequate protection); Weintraub and Resnick, *From the Bankruptcy Courts: Puncturing the Equity Cushion—Adequate Protection for Secured Creditors in Reorganization Cases*, 14 U.C.C. L.J. 284 (1982) (discussing adequate protection of undersecured creditors).

52. *See* 11 U.S.C. § 361(1) (1982 & Supp. 1985).

53. *See id.* § 361(3) (1982).

54. *See id.*

55. *See, e.g.*, *In re* Island Helicopter Corp., 63 Bankr. 515, 523 (Bankr. E.D.N.Y. 1986) (secured creditor not entitled to restrict debtor's use of insurance proceeds as indubitable equivalent of its interest); *In re* Wolsky, 53 Bankr. 751, 758 (Bankr. D. N.D. 1985) (indubitable equivalents are to be determined on case-by-case basis); *In re* Rhoades, 38 Bankr. 63, 65 (Bankr. D. Vt. 1984) (indubitable equivalent requires debtor to ensure that creditor will be paid); *In re* Aegean Fare, Inc., 33 Bankr. 745, 748 (Bankr. D. Mass. 1983) (indubitable equivalent of adequate protection does not entitle creditor to cash payment equivalent of its interest).

56. *Compare In re* Smithfield Estates, Inc., 48 Bankr. 910, 914 (Bankr. D.R.I. 1985) (adequate protection only requires maintaining status quo during pendency of proceedings) *and In re* Sun Valley Ranches, Inc., 38 Bankr. 595, 598 (Bankr. D. Idaho 1984) (congressional insertion of indubitable equivalent does not require interest payments as adequate protection during interim period between filing petition and confirmation) *and In re* South Village, Inc., 25 Bankr. 987, 996 (Bankr. D. Utah 1982) (Congress did not intend for payments of interest as opportunity costs to be included as adequate protection) *with In re* Western Preferred Corp., 58 Bankr. 201, 211 (Bankr. N.D. Tex. 1985) (secured creditor is entitled to adequate protection through lost opportunity costs) *and In re* Independence Village, Inc., 52 Bankr. 715, 734 (Bankr. E.D. Mich. 1985) (indubitable equivalent of adequate protection must include lost opportunity costs) *and In re* Air Vermont, Inc., 45 Bankr. 931, 935 (Bankr. D. Vt. 1985) (debtor must make cash payments to secured creditor as indubitable equivalent of its interest where debtor is financially able to make payments).

subsection merely authorizes the granting of other relief as is necessary for the creditor to realize his interest in the property.[57] The current inconsistencies in the courts are principally due to the ambiguous "indubitable equivalent" language in the third subsection of section 361.[58]

The term "indubitable equivalent" is a term of art originally coined by Judge Learned Hand in the case of *In re Murel Holding Corp.*[59] Judge Hand was concerned with affording adequate protection to creditors who were subjected to an unfavorable and unfair reorganization plan under the cram-down provisions of the 1898 Bankruptcy Act.[60] The court in *Murel* held that the creditor should receive the present value of its interest in the property because the reorganization plan submitted would likely fail.[61] This indubitable equivalent language is also present in the cram-down provisions of

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57. *See* 11 U.S.C. § 361 (1982 & Supp. 1985). Section 361 addresses adequate protection as follows:

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

Id.

58. *See* 11 U.S.C. § 361(3) (1982). Adequate protection may be provided by granting other relief which will result in the creditor's realization of the indubitable equivalent of its interest in the property. *See id.* The courts have been required to interpret the terms "indubitable equivalent" and "interest in the property" in deciding what relief is permissible under the third subsection of section 361. *See In re* American Mariner Indus., 734 F.2d 426, 432-35 (9th Cir. 1984) (to receive indubitable equivalent of its interest, creditor must receive opportunity costs for its collateral in form of interest). *But see In re* Sun Valley Ranches, Inc., 38 Bankr. 595, 598 (Bankr. D. Idaho 1984) (courts awarding opportunity costs as adequate protection are placing too much unjustified reliance on indubitable equivalent language). *See generally* Gordanier, *The Indubitable Equivalent of Reclamation: Adequate Protection for Secured Creditors Under the Code*, 54 AM. BANKR. L.J. 299 (1980) (evaluating significance of inclusion of term indubitable equivalence in section 361).

59. 75 F.2d 941, 941-42 (2nd Cir. 1935) (adequate protection to dissenting creditors under Bankruptcy Act must compensate creditors fully).

60. *See id.* at 942-43. The debt was $500,000; the property was assessed at $540,000; and the debtor had been unable to make payments for a period of years. *See id.* at 942. *See* 11 U.S.C. § 1129(b) (1982 & Supp. 1985) (court may confirm plan over dissent of creditors, known as cram-down method).

61. *See In re* Murel Holding Corp., 75 F.2d 941, 942-43 (2d Cir. 1935) (plan introduced by debtor was speculative, since debtor had "everything to gain and nothing to lose").

the current Bankruptcy Code.[62] The term is used to ensure that a plan is fair and equitable with regard to the treatment of a secured creditor.[63] The inclusion of this term in section 361, as it applies to adequate protection and relief from the stay, was the result of a legislative compromise between the House and Senate Committees.[64] The committees were otherwise unable to agree upon the scope of the subsection and, therefore, failed to clearly define the scope of the third subsection.[65]

The confusion over the meaning of the terms "indubitable equivalent" and "interest in the property" has created a split of authority among the courts regarding what protection is adequate so as to provide a secured creditor with relief from the stay.[66] Some courts have taken the present value concept provided in the cram-down situation at issue in *Murel* and applied it to

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62. *See* 11 U.S.C. § 1129(b)(2)(A)(iii) (1982 & Supp. 1985) (to be fair and equitable, plan must provide class of creditors with indubitable equivalent of their claims).

63. *See id.*

64. *See* 124 CONG. REC. 32,395 (1978). The compromise proposal replaced the word "value", which appeared in the House version of the bill, with the words "indubitable equivalent." This compromise was the result of the recognition that there may be other methods of protection to be utilized by the courts other than cash payments, liens, and payment of administrative expenses. The compromise deleted the section in the House version which would have allowed the court to award administrative expenses regarding a decrease in the value of the secured creditor's collateral. Adequate protection of a secured creditor's interest in property is intended to protect a creditor's allowed secured claim. *See id.*

65. *See id.* The indubitable equivalent language was the result of a compromise, since the House and Senate were unable to agree upon the inclusion of administrative expenses as an element of adequate protection. The compromise finally led to the so-called catch-all section, which empowers the court to grant other forms of relief, other than administrative expenses. This was a concession to the House version, which had included payment of administrative expense, by the Senate, whose version allowed only the relief granted in the first two subsections of section 361. *See id.*

66. *Compare In re* Aegean Fare, Inc., 34 Bankr. 965, 968 (Bankr. D. Mass. 1983) (right to adequate protection does not entitle creditor to cash payments of interest during stay) *and In re* Shriver, 33 Bankr. 176, 182 (Bankr. N.D. Ohio 1983) (only creditor's allowed secured claim, and not opportunity cost, is entitled to adequate protection) *and In re* Cantrup, 32 Bankr. 1004, 1005 (Bankr. D. Colo. 1983) (creditors are not entitled to compensation for loss of their money) *and In re* Saypol, 31 Bankr. 796, 800 (Bankr. S.D.N.Y. 1983) (adequate protection contemplates only decrease in value of collateral) *and In re* South Village, Inc., 25 Bankr. 987, 989-96 (Bankr. D. Utah 1982) (creditor not entitled to opportunity costs as adequate protection from depreciation of collateral) *and In re* Pine Lake Village Apartment Co., 19 Bankr. 819, 827 (Bankr. S.D.N.Y. 1982) (adequate protection relates to value of collateral, not alternative business opportunities) *with* Matter of Langley, 30 Bankr. 595, 603-06 (Bankr. N.D. Ind. 1983) (adequate protection was intended to be flexible) *and In re* Monroe Park, 17 Bankr. 934, 940 (D. Del. 1982) (indubitable equivalent includes creditor's loss of use of his money) *and In re* Virginia Foundry Co., 9 Bankr. 493, 498-99 (W.D. Va. 1981) (adequate protection of creditor's interest must compensate right to reinvest proceeds from sale of collateral) *and In re* Anchorage Boat Sales, Inc., 4 Bankr. 635, 643 (Bankr. E.D.N.Y. 1980) (creditor must foreclose on its security interest to receive indubitable equivalent of its interest in property).

the creditor's right to adequate protection in seeking relief from the automatic stay.[67] The most notable opinion in this regard is *In re American Mariner Industries*,[68] in which the United States Court of Appeals for the Ninth Circuit held that an undersecured creditor is entitled to lost opportunity costs[69] resulting from the imposition of the stay.[70] Although the payments awarded to the creditor are described as both opportunity costs and present value payments, they actually consist of the payment of interest on the value of the collateral.[71] Relying upon legislative history evidencing a desire to give the secured creditor the benefit of his bargain, the court held that interest payments were allowed as adequate protection for the creditor.[72] This holding was followed by other courts in *Grundy National Bank v. Tandem Mining Corp.*[73] and *In re Briggs Transportation Co.*[74] In *Grundy*, the United States Court of Appeals for the Fourth Circuit held that undersecured creditors are entitled to postpetition interest payments as a matter of law.[75] In *Briggs*, the United States Court of Appeals for the Eighth Circuit

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67. *See, e.g., In re* Bear Creek Ministorage, Inc., 49 Bankr. 454, 456-57 (Bankr. S.D. Tex. 1985) (undersecured creditor entitled to reasonable rate of return from alternative investment of collateral); *In re* Monroe Park, 6 COLLIER BANKR. CAS. 2D (MB) 139, 144-45 (Bankr. D. Del. 1982) (appreciation of property alone not sufficient to offset mortgagee's loss of interest); *In re* Sundale Assocs., 11 Bankr. 978, 981 (Bankr. S.D. Fla. 1981) (court recognized right of undersecured creditor to interest).

68. 734 F.2d 426 (9th Cir. 1984).

69. *See id.* at 435.

70. *See id.* The court held that the creditor's right to take possession of the collateral and sell or invest it had a substantial, measurable value. The court relied upon the Act's legislative history to determine that the purpose of the section was to permit the secured creditor to get the benefit of his bargain. *See id.* at 429-34.

71. *See id.* at 430-35. The Mariner opinion demonstrates the different types of terminology used to describe the disputed measure of adequate protection. The payments awarded to creditors have been referred to as opportunity costs, present value, and interest. All of these terms, however, actually refer to the payment of interest on the value of the collateral. These payments are opportunity costs in that they represent the creditor's right to foreclose on the collateral and reinvest the proceeds of resale at a specified rate of return. They are present value inasmuch as they require the payment of interest on the value of the collateral which, in its simplest terms, is merely interest. *See id.*

72. *See id.* at 435. The court stated that the creditor's interest in the property includes the right to foreclose on the property securing his loan and, as a result, the right to invest the proceeds and make beneficial use of that collateral. *See id.*

73. 754 F.2d 1436 (4th Cir. 1985).

74. 780 F.2d 1339 (8th Cir. 1985).

75. *See* Grundy Nat'l Bank v. Tandem Mining Corp., 754 F.2d 1436, 1441 (4th Cir. 1985). The court held that a secured creditor is entitled to periodic payments of interest until either: (a) a plan of reorganization is confirmed, (b) the case is closed or dismissed, (c) the collateral is relinquished, or (d) the automatic stay is lifted. *See id.* at 1440. The court ordered the interest rate to be paid at the market rate for the same type of loan. *See id.* at 1441. The court based its decision primarily on the ruling in the *American Mariner* case. *See id.* at 1440-41.

held that it is within the discretion of the court to award such interest.[76] In spite of these three appellate court decisions, the majority of bankruptcy courts do not award payments of interest or opportunity costs, and continue to recognize a distinction between undersecured and oversecured creditors.[77] As provided in section 506, these courts do not allow for interest payments to be made to a creditor unless the creditor is oversecured, since the estate will not otherwise be properly protected.[78]

In *In re Timbers of Inwood Forest Associates*,[79] the United States Court of Appeals for the Fifth Circuit held that undersecured creditors are not entitled to opportunity costs or postpetition interest while the automatic stay is in place.[80] The court premised its opinion on the fact that the issue involved was merely one of statutory interpretation, requiring simply that the court consider the plain meaning of the statute's provision.[81] The court examined

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76. *See In re* Briggs Transp. Co., 780 F.2d 1339, 1350-51 (8th Cir. 1985). The court held that since numerous factors must be considered in providing protection to the creditor, the bankruptcy judge should be permitted to use his discretion. The court stated that the decision of the bankruptcy court must weigh the interests of the secured creditor against the rights of the debtor. *See id.* at 1349-50.

77. *See, e.g.*, *In re* Smithfield Estates, Inc., 48 Bankr. 910, 914 (Bankr. D.R.I. 1985) (adequate protection only entails protection of creditor's interest against decrease in value of collateral); *In re* Sun Valley Ranches, Inc. 38 Bankr. 595, 598 (Bankr. D. Idaho 1984) (indubitable equivalent does not require interest payments as adequate protection during stay); *In re* Keller, 45 Bankr. 469, 473 (Bankr. N.D. Iowa 1984) (creditor not entitled to benefit of his bargain; court declined to follow *American Mariner*); *In re* S.W. Sheppley & Co., 45 Bankr. 473, 481 (Bankr. N.D. Iowa 1984) (adequate protection does not require complete protection of value of security); *In re* Cantrup, 32 Bankr. 1004, 1005 (Bankr. D. Colo. 1983) (creditors not entitled to compensation for loss of use of their collateral); *In re* Shriver, 33 Bankr. 176, 182 (Bankr. N.D. Ohio 1983) (creditor not entitled to opportunity cost); *In re* Pine Lake Village Apartment Co., 19 Bankr. 819, 827 (Bankr. S.D.N.Y. 1982) (adequate protection must only protect value of collateral, not opportunity cost); *In re* Ramco Well Serv., Inc., 32 Bankr. 525, 531-32 (W.D. Okla. 1983) (adequate protection does not give right to foreclosure on collateral, but only right to protection of value); *In re* Wheeler, 12 Bankr. 908, 909-10 (Bankr. D. Mass. 1981) (bankruptcy provides that creditor will not suffer depreciation of his collateral during pendency of automatic stay).

78. *See* 11 U.S.C. § 506 (1982 & Supp. 1985).

79. 808 F.2d 363 (5th Cir. 1987) (en banc).

80. *See In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380, 1416 (5th Cir. 1986), *aff'd on rehearing*, 808 F.2d 363 (5th Cir. 1987) (en banc). The panel opinion was vacated when the court agreed to hear the case en banc; the en banc opinion subsequently reinstated the panel opinion in its entirety. *See In re* Timbers of Inwood Forest Assocs., 808 F.2d 363, 364 (5th Cir. 1987) (en banc). The holding of the en banc opinion is essentially identical to that of the panel opinion, although the en banc court included a concurrence and a dissent, as well as adding to the majority panel opinion. *See id.* at 364-87.

81. *See In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380, 1384 (5th Cir. 1986), *aff'd on rehearing*, 808 F.2d 363 (1987) (en banc). The court stated its intention to adhere to the plain meaning rule, which involves first looking to the plain language of the provision, then reading the entire statute as a whole if ambiguities exist. *See id.* at 1384.

the two pertinent areas of the Code: those sections pertaining to the payment of interest, and those pertaining to adequate protection and relief from the stay.[82] The court determined that the pertinent sections concerning claims for interest specifically disallowed such claims, with the exception of oversecured creditors.[83] The automatic stay and adequate protection provision, however, required a more extensive examination.[84] The Fifth Circuit concluded that, based on an absence of any legislative history to support such payments, the term indubitable equivalent in subsection (3) of section 361 did not contemplate the payment of interest or present value.[85] The court in *Timbers* declined to follow the ruling of *American Mariner*, reversing the judgment of the lower court which had followed *Mariner* by ordering Timbers to pay lost opportunity costs to United in the form of interest on the value of the collateral.[86] The court in *Timbers* further justified its conclusion by considering the underlying principles of bankruptcy and Chapter 11 reorganization, neither of which support the payment of interest during the pendency of bankruptcy proceedings.[87]

Upon rehearing en banc,[88] the Fifth Circuit reinstated the panel opinion, adding a legislative postscript concerning the enactment of the Family Farmer Bankruptcy Act of 1986 (Farmer Act).[89] The opinion, written by Judge Randall, emphasized that those who testified at the hearings preceding

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82. *See id.* at 1385-1401.

83. *See id.* at 1385-87. The court's examination of the interest provisions revealed that a claim for interest is prohibited by the Code. *See id.* The court noted that an exception to this rule allows interest payments to oversecured creditors, but dismissed this avenue of relief since United was held to be undersecured. *See id.* at 1387.

84. *See id.* at 1387-1401. The court conducted extensive research into the common law development of adequate protection, as well as the legislative history behind the enactment of the adequate protection provisions of the Code. The conclusion reached by this research was the foundation of the court's holding that undersecured creditors are not entitled to interest payments during the automatic stay as an element of adequate protection. *See id.*

85. *See id.* at 1401. The court concluded that section 361(3) was designed to provide relief to creditors, other than cash payments replacement liens which would compensate the creditor for a decrease in the value of collateral. *See id.* at 1416.

86. *See id.* at 1383. The bankruptcy court ordered Timbers to pay 12% of the fair market value of the collateral, together with the $7,956 escrow payment, totalling $50,456. The bankruptcy court labeled this payment a "lost opportunity cost" payment. *See id.*

87. *See id.* at 1408-16 (payments of interest or opportunity cost endorsed by *American Mariner* are not consistent with fundamental principles of the Bankruptcy Code).

88. *See In re* Timbers of Inwood Forest Assocs., 802 F.2d 777, 778 (5th Cir. 1986) (ordering case to be heard en banc).

89. *See In re* Timbers of Inwood Forest Assocs., 808 F.2d 363, 364-70 (5th Cir. 1987) (en banc); *see also* Family Farmer Bankruptcy Act of 1986, Pub. L. No. 99-554, 100 Stat. (1986) (to be codified at 11 U.S.C. §§ 1200-1231). The new adequate protection section, which is to be codified at 11 U.S.C. 1205, applies only to Chapter 12 proceedings, and states that Section 361 does not apply. Adequate protection is defined as follows:

In a case under this chapter, when adequate protection is required under section 362, 363,

the enactment of the Farmer Act were critical of the dangerous results of the *Mariner* decision.[90] The opinion noted that the Farmer Act, to be codified as Chapter 12 of the Bankruptcy Code, amended the adequate protection provisions in section 361 to delete the indubitable equivalent language.[91] Judge Randall cited to provisions of the Code which would protect a creditor without resort to section 361(3), and added that the bankruptcy judge must use sound judgment, granting relief to the creditor in accordance with the underlying principles of the Bankruptcy Code.[92]

Judge Jones, dissenting in the en banc opinion, asserted that the conclusion reached in the *Mariner* case was the proper interpretation of section 361.[93] Judge Jones reasoned that the creditor's lost opportunity costs are

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or 364 of this title of any interest of an equity in property, such adequate protection may be provided in—

(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 property securing a claim or of an entity's ownership interest in 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 property securing a claim or of an entity's ownership interest in property;

(3) paying to such entity for the use of farmland the reasonable rent customary in the community where the property is located, based upon the rental value, net income, and earning capacity of the property; or

(4) 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 adequately protect the value of property securing a claim or of such entity's ownership interest in property.

Id.

90. *See In re* Timbers of Inwood Forest Assocs., 803 F.2d 363, 364 (5th Cir. 1987). Virtually all witnesses who testified criticized the *Mariner* decision. The witnesses expressed the sentiment that the payments required by *Mariner* would be fatal to the farmers' chances of proceeding with a successful reorganization. *See id.*

91. *See id.* at 368. Section 1205 disposes of the indubitable equivalent language of section 361 and eliminates any prospect of opportunity cost payments. *See id.*

92. *See id.* at 370-74 (each bankruptcy judge must fairly manage cases before him in manner which will promote the principles and objectives of the Bankruptcy Code).

93. *See id.* at 374-84 (Jones, J., dissenting). The dissent stated that its position is best demonstrated by a quote from *Mariner*:

> The secured creditor's right to take possession of and sell collateral on the debtor's default has substantial, measurable value. The secured creditor bargains for this right when it agrees to extend credit to the debtor and both parties consider the right part of the creditor's bargain. The right constitutes an "interest in property" that is "created and defined by state law," and we are aware of no federal interest that requires this right of the secured creditor to go unprotected "simply because an interested party is involved in a bankruptcy proceeding."

Id. at 384 (Jones, J., dissenting) (quoting *In re* American Mariner Indus., 734 F.2d 426 (9th Cir. 1984)). The Supreme Court in *Butner v. United States* observed that "[u]niform treatment

substantial and found support for their inclusion as adequate protection under the *Murel* rationale.[94] The dissent emphasized that interest payments are not to be confused with opportunity cost payments, and that the majority's emphasis on the Code provision denying interest was not proper support for the denial of opportunity costs.[95] Finally, the dissent stressed the reality that Chapter 11 proceedings may be pending for a period of years, thereby denying adequate protection to the secured creditor.[96] Accordingly, Judge Jones urged the adoption of measures which would shorten the proceedings.[97]

The source of the controversy concerning interest payments stems from competing legal theories and the opposing views of those who represent the interests of the creditor and the debtor.[98] Representatives of the debtor are concerned with legislative intent and a proper interpretation of the applicable statutes.[99] Advocates of the creditor stress an economic present value theory, asserting that bankruptcy precludes a creditor from foreclosing on the property and reinvesting the proceeds at a more favorable rate of return.[100] *Timbers* represents the view of the debtors, who seek to strictly

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of property interests by both state and federal courts within a State serves . . . to prevent a party from receiving a windfall merely by reason of the happenstance of bankruptcy." Butner v. United States, 440 U.S. 48, 54-55 (1979) (quoting Lewis v. Manufacturers Nat'l Bank, 364 U.S. 603, 609 (1961)). To the extent that the debtor in bankruptcy can prevent the secured creditor from enforcing its rights against collateral while the debtor benefits from the creditor's money, the debtor and his unsecured creditors receive a windfall at the expense of the secured creditor. *See In re* Timbers of Inwood Forest Assocs., 808 F.2d 363, 384 (5th Cir. 1987) (Jones, J., dissenting).

94. *See In re* Timbers Forest Assocs., 808 F.2d 363, 377-78 (5th Cir. 1987) (lost opportunity costs is term of art which has been understood since *Murel* to mean that creditors are entitled to be compensated for time value of their collateral).

95. *See id.* at 380-82 (opportunity costs can be compensated without the use of interest payments).

96. *See id.* at 378-79.

97. *See id.*.

98. *Compare In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380, 1382 (5th Cir. 1986) (Congress did not intend for undersecured creditors to be entitled to periodic postpetition interest payments on value of their collateral), *aff'd on rehearing*, 808 F.2d 363 (1987) (en banc) *with In re* American Mariner Indus., 734 F.2d 426, 435 (undersecured creditor is entitled to compensation for period of time in which it is prevented from enforcing its rights against debtor).

99. *See, e.g., In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380, 1382 (5th Cir. 1986) (interest payments to undersecured creditors would have an adverse impact on debtor's ability to reorganize), *aff'd on rehearing*, 808 F.2d 363 (1987) (en banc); *In re* Mathies, 64 Bankr. 279, 285 (Bankr. N.D. Tex. 1986) (undersecured creditor not entitled to periodic postpetition interest payments as adequate protection); *In re* Smithfield Estates, Inc., 48 Bankr. 910, 915 (Bankr. D.R.I. 1985) (purpose of adequate protection is not to place an undersecured creditor in better position than existed when stay became effective).

100. *See, e.g., In re* American Mariner Indus., 734 F.2d 426, 432 (9th Cir. 1984) (equitable principles require that value of creditor's interest in collateral be protected); *In re* Briggs

interpret the principles of bankruptcy and enforce specific statutes in accordance with those principles.[101]

The court in *Timbers* prefaced its analysis of whether a creditor is entitled to interest payments as relief from the stay, by stating its intent to adhere to the plain meaning rule in interpreting statutory intent.[102] The inescapable conclusion, when attempting to ascertain the legislative purpose for providing an automatic stay in Chapter 11 reorganization proceedings, is that the stay is necessary to provide relief to the debtor when he is attempting to formulate a reorganization plan.[103] Congress stated that an effective plan must be the product of detached thought and calculation, which is possible only if the debtor is free of his creditors' claims long enough to take inventory of his assets, forecast his cash flow, and restructure his debt accordingly.[104] The respite provided by the stay also protects the interests of the creditor by preserving the value of the estate through careful planning.[105] The legislative purpose of providing relief from the stay, as evidenced in section 361, is to protect a creditor who is being injured by the stay because his collateral is depreciating, thereby depriving him of adequate protection.[106] In contrast, the broad language of subsection (3) of section 361, is

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Trans. Co., 780 F.2d 1339, 1349 (8th Cir. 1985) (while courts should encourage reorganization efforts, reorganization should not operate to detriment of secured creditor); Grundy Nat'l Bank v. Tandem Mining Corp., 754 F.2d 1436, 1441 (4th Cir. 1985) (secured creditor must be compensated for use of its funds resulting from its inability to liquidate and reinvest). *See generally* Jackson, *Bankruptcy, Non-Bankruptcy Entitlements and the Creditor's Bargain,* 91 YALE L.J. 857, 879 (1982) (Bankruptcy Code is at odds with creditor's property rights under state law).

101. *See In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380, 1384 (5th Cir. 1986) (while economic debate is of significance to Congress, judges must be concerned with determining legislative intent of Bankruptcy Code), *aff'd on rehearing*, 808 F.2d 363 (1987) (en banc).

102. *See id.* at 1384. The court stated that the plain meaning rule should be followed in any endeavor into statutory interpretation. The court also expressed concern with avoiding the dangers of judicial legislation. *See id.*; *see also* Kirschbaum v. Walling, 316 U.S. 517, 520-23 (1942) (court must avoid any expansion of statute, which is judicial legislation).

103. *See* H.R. REP. NO. 595, 95th Cong., 1st Sess. 174-75 (1977). The overriding purpose for the automatic stay is to provide the debtor with a breathing spell, free from the claims of his creditors, in order to allow him to attempt to create a reorganization plan absent the pressures which forced him into bankruptcy. *See id.*

104. *See id.* at 220. The purpose of a Chapter 11 reorganization is to permit the debtor to make use of his cash flow to meet expenses and to restructure his finances so that he may continue to operate. *See id.*

105. *See id.* at 340. The automatic stay protects the creditor by providing for an orderly liquidation or reorganization, and preventing a race among the creditors to have first access to the debtor's assets. *See id.*

106. *See* 124 CONG. REC. 32,418 (1978). Rep. Butler states that Section 361 is intended to provide relief to a creditor who fears that his collateral is being misused or is depreciating. *See id.*

very general, consistent with Congressional intent to provide a catch-all provision.[107]

When collateral is diminishing in value, the creditor can utilize section 361 to protect its interest through cash payments from the debtor or a replacement lien.[108] The third subsection of section 361 provides the bankruptcy court with flexibility to fashion other relief as necessary if these specific remedies fail to properly protect against the collateral's depreciation.[109] The confusion is created by the use of the term indubitable equivalent of the creditor's interest in the property.[110] The indubitable equivalent language merely broadens the scope of available relief, allowing the bankruptcy judge flexibility in correcting depreciation problems which cannot be solved by cash payments or a replacement lien.[111] The lower court in *Timbers* reached its conclusion by following the *American Mariner* hypothesis that the inclusion of "indubitable equivalent" was intended to provide present value or interest payments during the pendency of the proceedings.[112] Any intent to include the term indubitable equivalent for this reason is conspicuously absent from the legislative history and the plain language of the Bankruptcy Code.[113] It is improper to presume that Congress would change the long-standing practice of denying interest and present value payments without clearly expressing an intention to do so.[114]

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107. *See* H.R. REP. NO. 595, 95th Cong., 1st Sess. 174-75 (1977). Disagreement between the Senate version of section 361 which had no catch-all subsection, and the House version, which included a catch-all, led to the inclusion of a catch-all subsection which allowed other relief, with the exception of administrative expenses. *See id.*

108. *See* 11 U.S.C. § 361(1), (2) (1982 & Supp. 1985) (adequate protection may consist of cash payments or lien to compensate for decrease in value of creditor's interest in collateral).

109. *See id.* § 361(3) (1982) (court may grant other relief which "will result in the realization by such entity in the indubitable equivalent of such entity's interest in such property").

110. *See id.* The term indubitable equivalent, which is not defined in the statute, leaves the courts with the task of interpreting its meaning. *See id.*

111. *See, e.g., In re* Island Helicopter Corp., 63 Bankr. 515, 523 (Bankr. E.D.N.Y. 1986) (court denied creditor access to insurance proceeds from destruction of collateral); *In re* Wolsky, 53 Bankr. 751, 758 (Bankr. D. N.D. 1985) (indubitable equivalent as adequate protection must be determined by the court on a case-by-case basis); *In re* Colrud, 45 Bankr. 169, 177 (Bankr. D. Alaska 1984) (indubitable equivalent standard must be reviewed based on specific facts of each case to determine whether creditor's interest is adequately protected).

112. *See In re* Bear Creek Ministorage, Inc., 49 Bankr. 454, 459-61 (Bankr. S.D. Tex. 1985), *rev'd sub. nom. In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380 (5th Cir. 1986), *aff'd on rehearing*, 808 F.2d 363 (1987) (en banc). The courts ordered the debtor to make payments based on the *Mariner* formula of interest on the value of the collateral. *See id.*

113. *See* 124 CONG. REC. 32,395 (1978) (Rep. Edwards states adequate protection of an interest in property is intended to protect creditor's allowed secured claim). The Code contains no provision expressly allowing a claim for present value prior to confirmation or dismissal. *See* 11 U.S.C. § 101-1331 (1982 & Supp. 1985).

114. *See, e.g.,* Watt v. Alaska, 451 U.S. 259, 271 (1981) (it is not conceivable that legislature would change a long standing rule of law without stating its express intent to do so);

In addition to the lack of legislative history showing Congressional intent to provide the undersecured creditor with present value or interest through the adequate protection provisions, the Code itself lacks any specific provision which would provide such payments.[115] The Code does, however, contain specific provisions which address the payment of interest and present value, but only after confirmation of a plan by the court.[116] The Code provides that a claim for unmatured interest is not allowed, unless the claim is made by an oversecured creditor.[117] This exception is justified by the fact that the oversecured creditor can be compensated with interest payments without the danger of depleting the estate to an amount less than the debt itself.[118] The Code also requires that a reorganization plan must include the payment of present value to a secured creditor to be fair and equitable.[119] Congress provided the creditor with a right to interest and present value, but only after confirmation of a plan by the court, and subject to the automatic stay.[120] While the legislature could have made such claims available during

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Scipps-Howard Radio, Inc. v. F.C.C., 316 U.S. 4, 11 (1942) (silence of Congress is an improper guide to its intent); Drummond Coal Co. v. Watt, 735 F.2d 469, 474 (11th Cir. 1984) (unexplained changes within committee are not proper indicators of Congressional intent); *see also* Addison v. Holly Hill Fruit Prods., Co., 322 U.S. 607, 618 (1944) (judicial function is merely to interpret and properly apply statute as intended by legislature).

115. *See* 11 U.S.C. §§ 101-1330 (1982 & Supp. 1985). The Code contains no specific provisions allowing a claim for present value or interest during the pendency of bankruptcy proceedings. *See id.*

116. *See id.* § 502(b)(2) (1982 & Supp. 1985) (claim may be allowed except to extent that it is for unmatured interest); *id.* § 1129(b)(2)(A)(II) (for plan to be fair and equitable, it must provide for payment of value of holder's interest as of effective date of plan).

117. *See id.* § 506(b) (1982 & Supp. 1985) (the holder of claim is allowed interest on claim if value of collateral exceeds amount of debt).

118. *See* H.R. REP. NO. 595, 95th Cong., 1st Sess. 174-75 (1977) (automatic stay provisions of Code are intended to protect creditor from rush of claims against property in which he has secured interest). By analogy, the "equity cushion" analysis will not permit the oversecured creditor to obtain relief from the stay, since the creditor can be certain that the estate is sufficient to repay the debt, and the creditor is adequately protected. *Compare In re* McMartin Indus., 62 Bankr. 718, 772-23 (Bankr. D. Neb. 1986) (creditor adequately protected by equity cushion where collateral was not depreciating) *and In re* Brokmeyer, 51 Bankr. 704, 706-07 (Bankr. S.D. Tex. 1985) (equity cushion sufficient adequate protection of creditor even though cushion would rapidly erode) *with In re* Gellert, 55 Bankr. 970, 972 (Bankr. D. N.H. 1985) (where no equity cushion exists as adequate protection, secured creditor is entitled to relief from automatic stay) *and In re* Aled Corp., 47 Bankr. 257 (Bankr. E.D. Pa. 1985) (where mortgage was in excess of value of property, mortgagee is entitled the relief from automatic stay). An equity cushion alone may constitute adequate protection. *See In re* Jamaica House, Inc., 31 Bankr. 192, 194-95 (Bankr. D. Vt. 1983).

119. *See* 11 U.S.C. § 1129(b)(2)(A)(II) (1982 & Supp. 1985).

120. *See id.* (present value must be provided in plan as prerequisite to confirmation); *see also id.* § 506(b) (provision allowing interest refers to interest as allowed secured claim, to be paid upon confirmation of plan). Neither section 1129 nor section 506(b) serve to supersede the automatic stay. *See id.* §§ 506(b), 1129(b)(2)(A) (II) (1982 & Supp. 1985).

the pendency of the stay, it chose not to do so in accordance with the principles of bankruptcy.[121]

While the proponents of the economic analysis are correct in their concern that creditors are denied their right to foreclose on their collateral and reinvest the proceeds, they fail to consider that such a scheme of logic runs contrary to established principles of bankruptcy law.[122] Economists insist that a creditor be protected by periodic postpetition payments equalling the amount which would be realized by foreclosing on its collateral and reinvesting the proceeds.[123] This proposed right is referred to as present value or opportunity cost, but it actually represents the payment of interest on the value of the collateral.[124] Since the payment of interest to an undersecured creditor is explicitly denied by the provisions of the Code, it is significant that the courts which subscribe to the *Mariner* theory seldom refer to such payments as interest.[125] The *Mariner* court used such nebulous phrases as

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121. *See In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380, 1395-96 (5th Cir. 1986), *aff'd on rehearing*, 808 F.2d 363 (1987) (en banc). The court noted that its research, encompassing 35 days of hearings, and 2700 pages of testimony from over 100 witnesses, failed to reveal any discussion of the subject of periodic postpetition interest payments for undersecured creditors. *See id.* at 1395-96; H.R. REP. NO. 595, 95th Cong., 1st Sess. 174-75 (1977). The automatic stay was enacted to provide relief to the debtor from the claims of the creditors until such time as he can effectively create a plan for repayment or reorganization. *See id.*; *see also* Caminetti v. United States, 242 U.S. 470, 485 (1917) (sole function of court is to enforce statute in accordance with its terms).

122. *See, e.g.,* Vanston Bondholders Protective Comm. v. Green, 329 U.S. 156, 163 (1946) (general rule in bankruptcy is that interest ceases to accrue on initiation of proceedings); Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934) (primary purpose of bankruptcy is to give an honest debtor relief from pressure of his indebtedness and allow him to make fresh start); Sexton v. Dreyfus, 219 U.S. 339, 344 (1911) (theory of bankruptcy law, since mid-1800s, is that interest on debt ceases to accrue upon filing of bankruptcy petition). *See* H.R. REP. NO. 595, 95th Cong., 1st Sess. 174-75 (1977). The automatic stay is a fundamental debtor protection under bankruptcy law. It provides the debtor with a breathing spell from the claims of his creditors. The stay prevents any attempt at collection, foreclosure or harassment by the creditor. Its purpose is to allow the debtor to attempt a plan of reorganization and repayment and to relieve him from the claims which caused him to resort to bankruptcy. *See id.* at 340-42.

123. *See In re* American Mariner Indus., 734 F.2d 426, 433 (9th Cir. 1984) (substitute for most indubitable equivalent must compensate for present value and protect creditor's interest in collateral).

124. *See, e.g., In re* Deeter, 53 Bankr. 623, 629 (Bankr. N.D. Ind. 1985) (payments for lost opportunity costs are interest payments); *In re* B&W Tractor Co., 38 Bankr. 613, 617 (Bankr. E.D.N.C. 1984) (opportunity cost payments are postpetition interest payments); *In re* Shriver, 33 Bankr. 176, 185 (Bankr. N.D. Ohio 1983) (opportunity cost payments constitute payment to creditor of interest at market rate, and not contract rate).

125. *See, e.g., In re* Western Preferred Corp., 58 Bankr. 201, 211 (Bankr. N.D. Tex 1985) (undersecured creditor entitled to adequate protection by cash payments of lost opportunity costs); *In re* Deeter, 53 Bankr. 623, 627 (Bankr. N.D. Ind. 1985) (creditor is entitled to value of its right to foreclose and reinvest proceeds). *In re* Independence Village, Inc., 52 Bankr. 715, 735 (Bankr. E.D. Mich. 1985) (creditor is entitled to opportunity costs as adequate pro-

"indubitable equivalent" and "benefit of the bargain" to conclude that the legislature intended present value payments to be made to the creditor during the pendency of the automatic stay.[126] The courts granting present value payments have ignored the express provisions of the Bankruptcy Code.[127]

The failed logic of the *Mariner* economic analysis argument is evident in its practical application by the bankruptcy court in *Timbers*.[128] The bankruptcy court ordered payment of an amount of $50,456 as monthly interest on the value of the collateral after Timbers had filed for Chapter 11 bankruptcy due to its inability to make monthly payments of $53,798.06 on its ten-year note.[129] This order illustrates the defective reasoning of the economic analysis.[130] In order to calculate the adequate protection payment proposed by *Mariner* and the lower court in *Timbers*, the court must estimate: (1) a reasonable rate of return available to the creditor on a similar investment; (2) the time required to foreclose and effect resale; and (3) the compensation to be realized upon resale.[131] This process may result in a

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tection). *See generally*, Murphy, *Use of Collateral In Business Rehabilitations: A Suggested Redrafting of Section 7-203 of the Bankruptcy Reform Act*, 63 CALIF. L. REV. 1483, 1506 (1975) (if court is to award cash payments, it should perhaps provide creditor with interest payments for loss of use of its funds).

126. *See In re* American Mariner Indus., 734 F.2d 426, 433 (9th Cir. 1984). The court traced the term indubitable equivalent back to an opinion written by Judge Learned Hand, who used the term to denote the possibility of present value payments to creditors who were subject to the cram-down provisions of the Code. *See id.*

127. *Compare* 11 U.S.C. §§ 101-1330 (1982 & Supp. 1985) (Code contains no provision as to present value, interest or opportunity costs as adequate protection to provide relief from stay) *with In re* Briggs Transport. Co., 780 F.2d 1339, 1340 (8th Cir. 1985) (adequate protection may include opportunity costs depending on discretion of court) *and* Grundy Nat'l Bank v. Tandum Mining Corp., 754 F.2d 1436, 1441 (4th Cir. 1985) (secured creditor entitled to periodic payments of interest on value of collateral during pendency of stay) *and In re* American Mariner Indus., 734 F.2d 426, 433 (9th Cir. 1984) (indubitable equivalent may include payments to secured creditor of present value as adequate protection).

128. *See In re* Bear Creek Ministorage, Inc., 49 Bankr.454, 459-61 (Bankr. S.D. Tex. 1985) (debtor ordered to make monthly opportunity cost payments to creditor), *rev'd sub. nom. In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380 (5th Cir. 1986), *aff'd on rehearing*, 808 F.2d 363 (1987) (en banc).

129. *See id.* (debtor's monthly loan payment was $53,798.06; court ordered debtor to make payment of 12% of value of collateral, equalling $50,456 per month).

130. *See id.* The opinion of the court is devoid of any discussion or explanation of the similarity in amount of the payment ordered and the contract payment. The court made no attempt to justify its actions, the result of which would undoubtedly force the debtor into Chapter 7 liquidation. *See id.* This is especially significant since Timbers had already agreed to pay United rental receipts from the property. *See In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380, 1383 (5th Cir. 1986), *aff'd on rehearing*, 808 F.2d 363 (1987) (en banc).

131. *See In re* Bear Creek Ministorage, Inc., 49 Bankr. 454, 459-61 (Bankr. S.D. Tex. 1985), *rev'd sub. nom. In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380 (5th Cir. 1986), *aff'd on rehearing*, 808 F.2d 363 (1987) (en banc). The bankruptcy court accepted Timbers' evidence of the value of the collateral, which varied substantially from the evidence presented

payment which is inexact as well as inequitable.[132] The risk of inequities is magnified by the fact that some courts, in applying the economic analysis, have determined present value payments based on a market rate which is higher than the contract rate.[133] The result is that the creditor is placed in a better position than if bankruptcy had not been filed, and the debtor is denied the benefit of his bargain.[134]

The Bankruptcy Code provides for alternative measures of relief which make the payment of present value under section 361 an unnecessary burden on the debtor.[135] Section 362(d)(2) is commonly used by creditors to obtain relief from the stay if the debtor does not have an equity in the property and the property is not necessary for an effective reorganization.[136] United may well have been successful in obtaining relief under this provision by asserting that Timbers had no equity in the collateral, and that an effective reorganiza-

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by United. *See id.* at 460. The court then estimated, without explanation, that a 12% rate of return should be allowed and provided for a six month period in which to foreclose and commence making a return on resale of the proceeds. The court did not make mention of a reasonable time in which to resell the property. *See id.*; *cf. In re* Roberts, 63 Bankr. 372, 376-78 (Bankr. E.D. Mich. 1986) (market value was not proper test to determine value of land since depressed market would result in period of one to three years to effect resale).

132. *See In re* Bear Creek Ministorage, Inc., 49 Bankr. 454, 459-61 (Bankr. S.D. Tex. 1985), *rev'd sub. nom. In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380 (5th Cir. 1986), *aff'd on rehearing*, 808 F.2d 363 (1987) (en banc). Before the debtor is allowed to propose a plan for reorganization, the creditor and the debtor must produce conflicting testimony and must take adversarial positions in stating their claims with the court. *See id.*

133. *See In re* Victory Constr. Co., 9 Bankr. 570, 574 (Bankr. C.D. Cal. 1981) (court found an 18% interest rate to be appropriate even though contract rate was 8%). *See generally* Fortang and Mayer, *Valuation in Bankruptcy*, 32 U.C.L.A. L. Rev. 1061, 1088-90 (1985) (general discussion of evaluation of amount of claims).

134. *See, e.g., In re* Martin, 761 F.2d 472, 477 (8th Cir. 1985) (adequate protection requires determination of value of creditors' interest in collateral in proportion to risk posed to such interest); *In re* Rankin, 49 Bankr. 565, 569 (Bankr. W.D. Mo. 1984) (assessment of risk to creditors' interest in property is element of any determination of adequate protection); *In re* Hagel Partnership, 40 Bankr. 821, 824-25 (Bankr. D. D.C. 1984) (mortgagees who had accepted risk of depreciation by financing at top price were not permitted to shift risk to debtors through use of adequate protection).

135. *See In re* Timbers of Inwood Forest Assocs., 808 F.2d 363, 370-74 (5th Cir. 1987) (en banc) (secured creditor is able to enforce its right without aid of adequate protection provisions by wide range of remedies provided by Congress in Bankruptcy Code).

136. *See* 11 U.S.C. § 362(d)(2) (1982 & Supp. 1985). This provision states that a party may be entitled to relief from the automatic stay if the debtor does not have an equity in such property, and such property is not necessary for an effective reorganization. *See id.*; *see also* Stewart v. Gurley, 745 F.2d 1194, 1196 (9th Cir. 1984) (creditor granted relief from stay where debtor had no equity in property); *In re* Jug End in the Berkshires, Inc., 46 Bankr. 892, 903 (Bankr. D. Mass. 1985) (creditor allowed to foreclose and stay terminated where debtor had no equity in property and no reasonable likelihood of reorganization existed); *In re* Merrick, 44 Bankr. 967, 970-71 (Bankr. S.D. Ohio 1984) (mortgagee entitled to relief from stay where debtor had no equity in property and mortgagee was without adequate protection).

tion was not possible.[137] A valid argument may have been made that Timbers did not have any equity in the apartment complex since bankruptcy courts have generally held that an undersecured creditor cannot have an equity in the collateral because the debt cannot be satisfied by the full value of the collateral.[138] Creditors already are protected from delays in the proceedings insofar as they may file a plan after 120 days from the date of filing; likewise, the court may convert the proceeding to a Chapter 7 liquidation in response to undue delay or inability to reorganize.[139] Provisions of the Code allow the court to effect confirmation of a plan in a timely manner, at which time a proper claim for interest or present value will be allowed.[140] There is no question that a secured creditor may be entitled to relief from the stay if the value of his interest in the collateral is diminishing.[141] These alternatives are further evidence that Congress did not intend for an undersecured creditor to be entitled to periodic payments of interest or present value during the pendency of the proceedings as an element of adequate protection under section 361.[142]

The court's decision in *Timbers* was the product of an extensive analysis of the Bankruptcy Code, guided by the intention to forego judicial legislation in favor of statutory interpretation. Acting on this commitment, the court determined that the legislative purpose of the automatic stay provision is to protect the debtor's prospects for reorganization and repayment. The court further found that the adequate protection provisions relied upon by United

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137. *See* Stewart v. Gurley, 745 F.2d 1194, 1196 (9th Cir. 1984). The creditor merely had to prove that a reorganization plan was unlikely, and that the debt was undersecured, to obtain relief from the automatic stay. *See id.*

138. *See In re* Colrud, 45 Bankr. 169, 178 (Bankr. Alaska 1984) (equity, for purpose of granting relief from automatic stay, is determined by value of property and amount of liens against it); Hagendorfer v. Marlette, 42 Bankr. 17, 19 (D.C. Ala. 1984) (where value of liens was to be greater than value of property, creditor entitled to adequate protection); *In re* Mellor, 734 F.2d 1396, 1401 (9th Cir. 1984) (creditor adequately protected where value of property exceeded value of debt.)

139. *See* 11 U.S.C. § 1121 (1982 & Supp. 1985).

140. *See id.* § 1129.

141. *See id.* § 361 (where creditor's interest in collateral is decreasing, he is entitled to cash payments or replacement lien).

142. *See* Axe, *Penetrating the Iron Curtain: Representing Secured Creditors in Chapter 11 Reorganization Proceedings,* 67 MARQ. L. REV. 421, 430-31 (1984) (concept of adequate protection requires that secured creditor's position as of date of filing does not deteriorate because of imposition of automatic stay); Bisbee, *Business Reorganization Practice Under the Bankruptcy Reform Act of 1978,* 28 EMORY L.J. 709, 726-27 (1979) (purpose of adequate protection to preserve position of creditor as of date of filing from erosion of collateral); Masari, *Adequate Protection Under the Bankruptcy Reform Act,* in W. NORTON, 1978 ANNUAL SURVEY OF BANKRUPTCY LAW 171, 173 (the purpose of section 361 is to prevent loss or diminution of collateral), *cited in In re* Timbers of Inwood Forest Assocs., 793 F.2d 1380 (5th Cir. 1986), *aff'd on rehearing,* 808 F.2d 363 (1987) (en banc).

contemplate relief from depreciation of the creditor's property interest, not maintenance of his financial position. While economic theorists are understandably concerned with the creditor's inability to make use of his collateral while bankruptcy proceedings are pending, this theory cannot overcome the weight of established bankruptcy law. The economic proposal of *American Mariner* has an impractical and inequitable result, and its necessity is diminished by alternative provisions of the Code which yield a similar result. The Fifth Circuit in *Timbers* correctly decided that opportunity costs, or interest payments, are not provided to undersecured creditors by the Code's adequate protection provisions. The result of this decision will be to clarify the misconceptions surrounding the *American Mariner* analysis and provide a valuable authority for the proper application of the Bankruptcy Code. Inasmuch as *Timbers* solidifies an extant split of authority among the Federal Courts of Appeals, the United States Supreme Court should rule on this issue by affirming the holding of the Fifth Circuit.

Robert J. Ogle