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IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

In re
Dagburg, LLC,

Debtor.

In Chapter 11 Proceedings
Case No. 08-bk-02609-SSC

**MEMORANDUM DECISION RE:
REAL ESTATE EQUITY LENDING,
INC.'S, MOTION FOR RELIEF
FROM STAY.**

I. Preliminary Statement

This matter came before the Court on a "Motion for Relief from Stay, or, Alternatively, for Entry of an Order Dismissing or Converting this Case to a Case Under Chapter 7," filed by Real Estate Equity Lending, Inc. ("REEL"), on June 5, 2008. On June 6, 2008, REEL filed a "Declaration of Michael Coffman" in support of its Motion. On June 26, 2008, the Dagburg, LLC, the Debtor herein, filed its "Response to Motion for Relief from Stay, or, Alternatively, for Entry of an Order Dismissing or Converting this Case to a Case Under Chapter 7." On July 7, 2008, the Debtor filed a "Declaration of Clif Burgener" in support of its Response. On July 15, 2008, the Court conducted a preliminary hearing at which both parties appeared and presented argument, at which time the Court deemed the matter under advisement. This Decision shall constitute the Court's findings of fact and conclusions of law pursuant to Fed.R.Civ.P. 52, Bankruptcy Rule 7052. The Court has jurisdiction over this matter, and this is a core proceeding. 28 U.S.C. §§ 1334 and 157 (West 2007).

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II. Discussion

The Court must consider whether this matter should be set for a final hearing. In determining whether to do so, the Court must conclude that the Debtor has the reasonable probability of succeeding at a final hearing on the Motion. 11 U.S.C. 362(e); United Sv. Ass'n v. Timbers of Inwood Forest, 108 S.Ct. 626 (1988). For the reasons set forth hereinafter, the Court must vacate the stay at this time.

The Declaration of REEL in support of the Motion for Relief from Stay states it provided financing to a third party who is not the debtor in these proceedings in the original principal amount of \$600,000. This indebtedness is secured by certain deeds of trust on the real property in Nevada (the "Property") which belongs to the third party. As of May 22, 2008, the sum of \$1,186,144.42 remained due and owing to REEL, without considering attorneys' fees, costs, and expenses which may have accrued thereon. Because of the third party's failure to pay the indebtedness to REEL, said creditor commenced proceedings under Nevada law to foreclose on its interest in the third party's Property. The trustee's sale of the non-debtor's Property was initially scheduled for March 14, 2008, and has apparently been continued from time to time. REEL notes that it is a private lender, with approximately 75 investors, and REEL has been required to pay said investors pursuant to its agreements with them even though the third party has not made payments on the REEL indebtedness for a prolonged period of time.

At the 341 Meeting of Creditors, the Debtor's principal acknowledged that the Debtor has few creditors, no employees, and its only assets are interests in two separate deeds of trust. Of the creditors listed on Amended Schedule F, the Debtor concedes that Paul Parry, with a claim of \$2,000, and Security Title Agency, with a claim of \$2,500 are the only non-insider creditors. Although the Debtor states that it initially received a 5 percent interest in a deed of trust on the Property in November 2004, it did not record that interest in the public records until shortly before it filed its bankruptcy petition. According to the Debtor's Amended Schedule A, the Debtor's assets are a 5 percent interest in the Deed of Trust on the

1 Property and a third deed of trust on real property located in Prescott, Arizona. The Debtor
2 also listed a litigation claim against Lonestar Mortgage Services on Schedule B, in the amount
3 of \$75,000. The Debtor does not report any income from its assets or from any other source.
4 The Debtor does not appear to have liquid assets of any sort, or the means by which to get
5 such funds from a third party.

6 The Debtor has submitted a current Declaration from its principal and an
7 appraisal of the Property, from 2006, in support of its position that the stay should remain in
8 place and that the Debtor should be entitled to a final hearing on the Motion for Relief from
9 Stay. The Declaration of the Debtor does not controvert the factual predicate that it has few
10 creditors, no employees, the interest of the Debtor in the Property was recently recorded, that
11 it receives no cash distribution from its interests in assets, or that it has little, if any, funding
12 to proceed with any type of reorganization. The Declaration simply states that the appraised
13 value of the Property is \$2,025,000, based upon the 2006 appraisal, and that the beneficiaries
14 under the Deed of Trust, in which the Debtor has a 5 percent interest, are owed at least
15 \$2,400,000. The Debtor simply asserts that the value of the Property exceeds the amount due
16 and owing to REEL, that REEL is adequately protected by an equity cushion in the Property,
17 and that the Property is necessary for an effective reorganization of the Debtor. Counsel for
18 the Debtor also stated, at the preliminary hearing on the REEL Motion, that the Ninth Circuit
19 decision on In re Bialac, 712 F.2d 426 (9th Cir. 1983) supported its request that the automatic
20 stay remain in place.

21 The Debtor assumes that it has the rights of a party that owns the Property.
22 In fact, the Debtor simply owns a 5 percent interest in a Deed of Trust on the Property. The
23 Debtor conceded at the Preliminary Hearing on REEL's Motion that the parties to its Deed of
24 Trust have separately scheduled a trustee's sale of the Property. Assuming that the Debtor's 5
25 percent interest in the Deed of Trust somehow allows it to control the other 95 percent
26 interest, or that the Debtor and the other beneficiary or beneficiaries, are somehow in
27 agreement as to how to proceed, the Debtor is essentially asking that REEL be stayed so that
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1 the Debtor and other parties may proceed with their rights and remedies under Nevada law as
2 to a non-debtor third party. The Debtor has cited no case law to support what the Debtor
3 proposes. The Court sees no basis to allow a debtor to somehow set the playing field to allow
4 it to acquire real property prior to, and in contravention of, the normal procedures that would
5 be permitted to all creditors or third-party bidders at a trustee sale of a third party's real
6 property under applicable state law. In other words, if there is to be a trustee's sale of the
7 Property, the Debtor, REEL, and other interested parties should be able to proceed at that
8 time. Why prefer one creditor over another?

9 More importantly, the Debtor assumes that it need only show that there is
10 equity in the Property to proceed to a final hearing. That is not the case. In the decision of In
11 re A Partners, LLC, 344 B.R. 114 (Bankr. E.D.Cal. 2006), the debtor did not own an interest
12 in one of the real properties at issue.¹ The debtor held a note, secured by a deed of trust, as to
13 real property owned by a related entity. The debtor's lien on this property was fifth in order
14 of priority. The creditor with a senior lien had already commenced the non-judicial
15 foreclosure proceedings under applicable state law. The senior lienholder was not listed as a
16 creditor of the debtor and had not filed a proof of claim in the debtor's bankruptcy
17 proceedings. The debtor had little cash, and could not exercise all of its rights as a junior
18 lienholder under applicable state law. The debtor argued at the hearing on the motion for
19 relief from stay by the senior lienholder that a party was willing to purchase the real property
20 and, thus, pay all secured creditors with a lien thereon in full, including the senior lienholder
21 and the debtor. Alternatively, the debtor argued that it should be able to proceed with its
22 foreclosure, acquire the property, and then provide for the treatment of the secured creditors
23 under its plan of reorganization. The Court disagreed with the debtor's position and vacated
24 the automatic stay.

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28 ¹ The debtor did own another commercial building which was heavily encumbered.

1 In reviewing the debtor’s interest in the deed of trust, the A Partners Court
2 stated that the debtor did not own the real property and that the debtor’s bundle of rights,
3 which became an asset of the bankruptcy estate, was limited to those of a junior lienholder,
4 such as to reinstate the senior liens on the property, redeem the property, or credit bid the
5 amount of its indebtedness at a trustee’s sale. The Court concluded that this bundle of rights
6 was not the same as having an ownership interest in the real property. Moreover, the test
7 under Section 362(d)(1) or (d)(2) was not simply determining the value of the real property of
8 the non-debtor third party, the liens against the real property, and whether there was any
9 equity therein. Indeed such a standard only applied if the debtor owned the real property,
10 which it did not.

11 Although the Court, in A Partners, stated that any assertion of pre-foreclosure
12 rights of reinstatement and redemption, after the bankruptcy case of the debtor had been filed,
13 would be a violation of the automatic stay, relying on Harsh Investment Corp. v. Bialac (In re
14 Bialac), 712 F.2d 426, 432, (9th Cir. 1983), that conclusion did not determine whether the
15 automatic stay should be vacated in its case. The Court stated that the debtor’s interest in the
16 deed of trust did not extend the stay to the underlying real property. Relying on the
17 Bankruptcy Appellate Decision of First Federal Bank of California v. Cogar (In re Cogar),
18 210 B.R. 803, 812 (9th Cir. B.A.P. 1997), the Court also concluded that the senior lienholder
19 on the real property did not have a claim against the estate of the junior lienholder that could
20 be modified in the junior lienholder’s plan of reorganization, even if the debtor’s plan
21 transferred the underlying property to the debtor.

22 In reviewing the debtor’s right to foreclose potentially before the senior
23 lienholder, the Court stated that such a right had no economic value, because the senior
24 lienholder had already started, and substantially completed, its non-judicial foreclosure sale.
25 A Partners, 344 B.R. at 123. As to the debtor’s ability to exercise its other rights to reinstate
26 the obligations or to redeem the property, the debtor had shown no financial ability to do so.
27 Id. The Court then discussed the debtor’s interest as being a contract right, and depending on
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1 the facts and circumstances of each case, that contract right might have little or no value.²

2 The Court concluded that the value of the debtor's interest in the deed of trust, given the
3 debtor's financial circumstance, was near zero.

4 As to the debtor's ability to bid at the foreclosure sale, the Court stated that
5 the debtor's assertion of equity would mean that other parties would be present to bid at the
6 sale and that the debtor would never get control of the real property, only the cash that it
7 might receive on its deed of trust. However, that right never allowed the debtor to stop the
8 foreclosure sale of the senior lieholder. A Partners, 344 B.R. at 125. Based on this analysis,
9 the A Partners Court concluded that cause had been shown to vacate the automatic stay under
10 Section 362 (d)(1).

11 Although REEL in this case argues bad faith, and requests that if the
12 automatic stay is not vacated, that the case be dismissed as a bad faith filing, such a factually
13 intensive finding normally requires a further evidentiary hearing. In re Hall, Bayoutree
14 Associates, Ltd., 939 F.2d 802, 805-06 (9th Cir. 1991); In re Davis-Rice, 2007 WL 2534236
15 (Bankr. N.D.Cal. 2007) ("issues of good and bad faith generally require an evidentiary
16 hearing"). The record in this case already supports vacatur of the automatic stay for cause.
17 As noted in the case law discussed above, the Debtor's interest in a Deed of Trust on the
18 Property is de minimus. Even if the Debtor were somehow able to join with the other
19 interests in the Deed of Trust, and act in concert, the parties do not own the Property. The
20 Debtor does not have the financial ability to reinstate or redeem REEL's senior lien. It is
21 unclear whether the Debtor would be able to acquire the Property at any duly scheduled non-
22 judicial foreclosure sale of the Property. The Debtor's interest in the Deed of Trust is of little

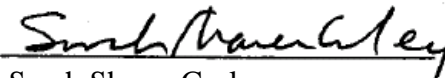
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24 ² The Court focused on number of cases that discussed the debtor's inability to perform
25 because of the factual circumstances. In one case, the debtor was unable to perform on a
26 contract that served as collateral for a loan from a secured creditor to the debtor. The Court,
27 in that case, found that the contract and, hence, the collateral of the secured creditor, had no
28 value. In another case, the debtor had utilized a diamond ring as collateral in a transaction,
but the ring had disappeared without the debtor's knowledge. Although the creditor retained
its security interest in the lost ring, the creditor's interest in the debtor's case was as an
unsecured creditor, with the collateral having zero value. A Partners, 344 B.R. at 123-125.

1 or no value, since the Debtor simply has a 5 percent interest in a \$2,400,000 obligation. That
2 obligation and the REEL obligation total \$3,586,144.42, yet the value of the Property of the
3 third party, even pursuant to the Debtor's appraised value from 2006, is only the amount of
4 \$2,025,000. The economic value of a 5 percent interest in a Deed of Trust which is only
5 partially secured, under the best of circumstances, is zero or close to zero.

6 III. Conclusion

7 Because the Debtor has presented so little information, or so few facts, to
8 support its position, the Court concludes that the Debtor does not have the reasonable
9 probability of succeeding at any final hearing on the REEL Motion for Relief from Stay.
10 REEL presented a prima facie case as to why the automatic stay should be vacated for cause.
11 At that point, the burden shifted to the Debtor to present sufficient evidence that would
12 warrant a final evidentiary hearing. The Debtor did not do that. As a result, the automatic
13 stay must be vacated for cause under Section 362 (d)(1). REEL shall submit a form of order.

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15 Dated this 25th day of July, 2008.

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18 Sarah Sharer Curley

19 United States Bankruptcy Judge
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