UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF NORTH CAROLINA
WILMINGTON DIVISION

In the Matter of:
BATE LAND & TIMBER, LLC
Debtor

Chapter 11
Case No.: 13-04665-8-SWH

SUPPLEMENTAL BRIEF

NOW COMES Bate Land & Timber, LLC (the "Debtor") and submits this Supplemental Brief pursuant to the Court's Order dated August 12, 2014[1]. The Court has heard testimony from multiple witnesses, reviewed and considered briefs and oral arguments by counsel, and been the recipient of extensive post-hearing summaries of evidence. Debtor relies on all pleadings and briefs previously filed in the case, as well as all evidence introduced and arguments of counsel. This Supplemental Brief does not attempt to re-hash the evidence, re-package the evidentiary summaries, or improve the Debtor's position through new arguments, but primarily focuses on two cases that were mentioned by counsel for the parties after the evidentiary record was closed: *In re Brown*, 746 F.3d 1236 (11th Cir. 2014) and *CWCapital Asset Management, LLC v. Burcam Capital II, LLC*, 5:13-CV-278-F (E.D.N.C. June 24, 2014). This Supplemental Brief also outlines case law supporting the use of "fair market value" as the appropriate standard for valuation.

INTRODUCTION

The facts of this case are unique in that the lender/secured creditor Bate Land Company, LP ("BLC"), unlike a traditional bank, was a decades-long owner and manager of the original seventy-nine tracts of collateral property[2] before selling them via Purchase Money Financing to Debtor, who has paid

[1] The Debtor respectfully disagrees that it requested the Court to delay ruling on issues relating to confirmation of its Plan. Settlement was discussed after the record was closed, just as it had been before the Petition was filed, but the Debtor never understood that such discussions would postpone any rulings on pending issues, or require additional briefing.

[2] BLC is a Georgia limited partnership and authorized to do business in North Carolina since 1998. Its business, and that of

over $60 million of the original purchase price. Prior to filing its Petition, Debtor recorded a Deed conveying certain collateral property to BLC intending to satisfy the outstanding debt to BLC of approximately $13 million, which included accrued interest. BLC filed a secured claim, despite the fact that North Carolina law limits the remedies of purchase money lenders to return of collateral property.

The Debtor has since proposed a "dirt for debt" plan, and, as outlined below, this Court has been at the forefront of Chapter 11 cases with similar plans. Valuation of the property to be returned to the creditor is a key finding that the bankruptcy trial judge must make, and this Court heard extensive testimony from appraisers valuing the collateral property. In one of the more recent cases decided by the United States District Court for the Eastern District of North Carolina, *Gateway Bank and Trust Company v. Clarendon Holdings, LLC*, No. 7:11-cv-247-H (E.D.N.C. March 18, 2013), the district court reviewed the trial court's valuation decisions in light of *Associates Commercial Corp. v. Rash*, 520 U.S. 953, 962 (1997). As more fully explained below, the recent Eleventh Circuit case of *In re Brown* calls that *Rash* analysis into question, if it were ever applicable to the facts of this case.

CWCapital Asset Management, LLC v. Burcam Capital II, LLC, 5:13-CV-278-F (E.D.N.C. June 24, 2014) was mentioned by counsel for BLC ostensibly to support its objection that Debtor's Plan was not filed in good faith. As outlined below, the facts of *Burcam* are so dissimilar to the instant case as to have no relevance whatsoever.

I. *In re Brown*, 746 F.3d 1236 (11th Cir. 2014)

A. *Analysis of Rash* and *Brown*

The recent Eleventh Circuit case of *In re Brown* holds that 11 U.S.C. § 506(a)(2)'s replacement value standard applies in a Chapter 7 or 13 bankruptcy when a debtor surrenders collateral in partial or full satisfaction of an allowed secured claim under 11 U.S.C. § 1325(a)(5)(C). In the context of a

its predecessor Harold Bate (the principal and founder of BLC), was to hold real estate and manage timber operations. Tim Tabak, the registered forester called by BLC in this case, testified that he had been doing consulting working for BLC since the year 2000.

Chapter 13 case, an allowed secured claim refers to 11 U.S.C. § 506(a). *See, Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997). Section 506(a)(1) provides that a secured creditor's allowed claim can be divided or bifurcated into a secured and an unsecured claim based on the value of the underlying collateral. Specifically:

> An allowed claim of a creditor secured by a lien on property in which the estate has an interest ... is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property ... and is an unsecured claim to the extent that the value of such creditor's interest ... is less than the amount of such allowed claim. Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property.

See 11 U.S.C. § 506(a)(1) (2006). Section 506(a)(2) provides:

> If the debtor is an individual in a case under chapter 7 or 13, such value with respect to personal property securing an allowed claim shall be determined based on the replacement value of such property as of the date of the filing of the petition without deduction for costs of sale or marketing. With respect to property acquired for personal, family, or household purposes, replacement value shall mean the price a retail merchant would charge for property of that kind considering the age and condition of the property at the time value is determined. See 11 U.S.C. § 506(a)(2) (2006).

The case of *In re Brown* is important because it turns the decision in *Associates Commercial Corp. v. Rash* on its side and establishes in cases filed after the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA") that the replacement value of collateral is the standard to use when valuing a creditor's secured claim.

Before reviewing the *Brown* decision, it is important to look at the *Rash* decision. In *Rash*, the debtor, Mr. Rash, was in the freight-hauling business and purchased a tractor truck that was pledged as collateral for the unpaid balance of the purchase price. Id at 956. Subsequently, Mr. Rash filed a Chapter 13 bankruptcy and listed the truck on his bankruptcy Schedules and Statements. The creditor's claim was listed as secured in an amount equal to the discounted value of the truck -- taking into account depreciation and wear and tear. The remainder of the claim was listed and treated as an unsecured

claim. Id at 957. The focus of *Rash* was on the method used to value the collateral. The *Rash* Court relied heavily on the second sentence of 11 U.S.C. § 506(a), which stated that such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property. Id at 962. As previously noted, 11 U.S.C. § 506(a)(2) was not part of the Bankruptcy Code when *Rash* was decided. The Court ruled that the debtor's continued use of the collateral was important since the truck was in a constant state of depreciation that reduced the creditor's secured claim. The Court held that the replacement value of the collateral rather than foreclosure value was the appropriate method to value the collateral because the debtor chose to retain rather than surrender the collateral. Id at 965.

In *In re Brown*, Santander Consumer USA, Inc., as assignee of Thor Credit Corp. ("Santander"), appealed to the Eleventh Circuit the district court's ruling affirming the bankruptcy court's order overruling Santander's objection to the confirmation of the debtor's plan under Chapter 13 of the United States Bankruptcy Code, which proposed that the debtor surrender his vehicle under 11 U.S.C. § 1325(a)(5)(C) to satisfy Santander's claim. Id at 1238. The bankruptcy court held 11 U.S.C. § 506(a)(1) and (a)(2) determined the vehicle's value and hence the amount of Santander's secured claim that would be satisfied by the debtor's surrender of the vehicle. The issue before the *Brown* court was whether § 506(a)(2)'s valuation standard applies when a Chapter 13 debtor surrenders his vehicle under § 1325(a)(5)(C).

At the confirmation hearing in the bankruptcy court, the parties disagreed on the method for valuing the debtor's vehicle. The debtor argued that § 506(a)(2)'s replacement value standard governed valuation and the amount of Santander's secured claim. Id. The debtor contended that if his vehicle's replacement value exceeded the debt, then surrendering the vehicle would satisfy Santander's entire claim (and the debt) under § 1325(a)(5)(C). Id. Santander argued that in a surrender scenario the

vehicle's value should be based on its foreclosure value and not replacement value. Id.

The bankruptcy court overruled Santander's objection and held that § 506(a)(2) required valuing the debtor's vehicle based on its replacement value. Id at 1239. The bankruptcy court found that while the Supreme Court's 1997 decision in *Associates Commercial Corp. v. Rash* means that a foreclosure valuation would have been applied to the debtor's surrendered vehicle, *Rash* preceded BAPCPA's addition of § 506(a)(2), which required the use of replacement value. Id. The court held that Santander was entitled to a secured claim equal to the replacement value of the collateral and that the debtor's surrender of the vehicle would satisfy that claim under § 1325(a)(5)(C). Id. Following a valuation and confirmation hearing, the bankruptcy court determined that the vehicle's replacement value at least equaled the debt and confirmed the debtor's Chapter 13 plan. Id. Santander appealed the bankruptcy court's decision to apply the replacement value standard to the district court, which rejected Santander's arguments and affirmed the bankruptcy court's decision. Id.

In the Eleventh Circuit, Santander again argued that applying § 506(a)(2)'s replacement value standard when a debtor surrenders property under § 1325(a)(5)(C) would misapply *Rash* and violate § 506(a)(1)'s "disposition and use" language. Id. Specifically, Santander argued that applying a replacement value standard ignores the holding in *Rash* that different valuation standards should apply depending on the collateral's "disposition or use," with foreclosure value governing the surrender of an asset and replacement value governing the retention of an asset. Id. The court noted that this argument ignores the fact that *Rash* preceded BAPCPA's addition of § 506(a)(2), which expressly requires applying the replacement value standard. Id. at 1241.

Alternatively Santander argued that applying § 506(a)(2) in a surrender scenario would be absurd because it allows debtors to surrender collateral in full satisfaction of the debt. The court reasoned that this argument overstated the effect of § 506(a)(2) and that surrender would satisfy the creditor's secured

claim and not necessarily the entire debt. Id. The court added that if a creditor holds an under-secured claim, the creditor would still have an unsecured claim to the extent the debt exceeds the collateral's judicially-determined replacement value. Id.

Santander also argued that applying § 506(a)(2) would be absurd because it eliminates creditors' contract and state law rights to liquidate and pursue an unsecured claim for any deficiency. Id. The court held that state law does not govern if the Bankruptcy Code requires a different result. Id. *See Butner v. United States,* 440 U.S. 48, 55, 99 S.Ct. 914, 918, 59 L.Ed.2d 136 (1979); *Raleigh v. Ill. Dep't of Revenue*, 530 U.S. 15, 20, 120 S.Ct. 1951, 1955, 147 L.Ed.2d 13 (2000) (holding that creditors' rights are "subject to any qualifying or contrary provisions of the Bankruptcy Code"). The court found that, in the *Brown* case, the Bankruptcy Code is contrary to state law, as an unsecured claim under § 506(a)(1) and (a)(2) equals the amount that the debt exceeds the property's replacement value—not the amount of post-sale deficiency and therefore state law cannot apply. Id.

B. Application of *Rash* and *Brown* to Debtor's case

Generally, *Rash* was decided under 11 U.S.C. § 1325 (a)(5)(B), which provides that if a debtor retains collateral over the objection of a creditor, it must provide the creditor over the life of the Chapter 13 plan with the equivalent of the present value of that collateral. The present case involves a different set of facts where the Debtor proposes a surrender of collateral under Section 1129 of the Bankruptcy Code. In *Rash* the collateral was personal property that was used and subject to deterioration from extended use, so the court placed great importance on the proposed disposition or use of the property. Id at 962. Again, the present case involves raw land and a completely different set of facts, and the considerations in *Rash* are not applicable in the context of a dirt for debt case.

Moreover, under the holding of *In re Brown*, the Debtor's proposed disposition or use of the collateral takes on much less importance since the rationale espoused by the Court in *Rash* is no longer

applicable whether or not the property is to be surrendered to a secured creditor. *In re Brown* has effectively overruled *Rash* and established that replacement or fair market value is the standard to apply when valuing the claim of a secured creditor. *Brown* further debunks any arguments that applying fair market value in the surrender context is absurd because it allows debtors to surrender collateral in full satisfaction of the debt or that it eliminates creditors' state law rights to liquidate the collateral and pursue an unsecured claim for a deficiency.

One could argue that the decision in *In re Brown* only applies to cases filed under Chapter 7 or Chapter 13, because 11 U.S.C. § 506(a)(2) only applies to cases filed under those chapters of bankruptcy. Doing so also means that one is forced to recognize that *Rash* was a Chapter 13 case and therefore is not applicable to a Chapter 11 dirt for debt case. Another logical conclusion is that the *Rash* decision does not have to be followed in a dirt for debt case, for the *Brown* ruling established that the disposition or use of collateral is irrelevant to the valuation of that same collateral – retention versus surrender is no longer a distinction that matters. The *In re Brown* decision finally makes clear that a debtor may surrender collateral to a secured creditor in full satisfaction of its debt to such a creditor.

II. *CWCapital Asset Management, LLC v. Burcam Capital II, LLC,* 5:13-CV-278-F (E.D.N.C. June 24, 2014)

Counsel for BLC has raised the issue of whether the recent District Court opinion in *Burcam* is applicable to this case. That case involved an appeal by CWCapital Asset Mangement, LLC ("CWC") of the bankruptcy court's order denying a Motion to Dismiss Burcam Capital II's ("Burcam") Chapter 11 bankruptcy reorganization plan and the order confirming plan.

The facts are as follows: The debtor's original Chapter 11 plan divided the unsecured claims into two separate classes: general unsecured claims and small unsecured claims. The plan provided for payment in full to all creditors. *Burcam* at 2-3. After receiving the plan, CWC filed a Motion to Dismiss the bankruptcy case arguing, among other things, that the debtor could not propose a confirmable plan

under the Bankruptcy Code. *Id.* at 3. In an effort to block confirmation of the plan, CWC purchased sixteen unsecured claims, representing approximately 68% of the unsecured claims (approximately $31,280 of the total $46,000), and filed rejecting ballots on behalf of each of those claims. *Id.* Of the remaining unsecured claims, only two creditors, whose claims total approximately $6,000 in this nearly $14 million bankruptcy case, voted to accept the plan. The majority of the unsecured creditors failed to vote on the plan. *Id.*

The debtor requested a continuance of the confirmation hearing, which the bankruptcy court granted and the debtor then filed a modified Chapter 11 plan. It created a third class of unsecured claims consisting entirely of the unsecured claims purchased by CWC. *Id.* The debtor proposed providing the CWC-purchased unsecured claims a deed of trust on property owned by the debtor and repaying those claims in full with interest at 3.75% over the course of ten years.

At the confirmation hearing, CWC renewed its argument that the plan should be dismissed. *Id.* at 4. CWC argued that Burcam created the separate class of "no votes" solely for purposes of manipulating the vote to confirm the plan, which is prohibited under Fourth Circuit precedent. *See In re Bryson Props. XVIII*, 961 F.2d 496, 502 (4th Cir. 1992). *Id.* Burcam argued that it separately classified the CWC purchased claims because it needed to pay trade creditors (who owned most of the non-CWC purchased claims) on a shorter time frame than claims owned by the secured creditor to maintain business goodwill with the trade creditors. *Id.* The bankruptcy court accepted this argument, finding that Burcam articulated a "legitimate business reason" for the separate classification, denied CWC's Motion to Dismiss and confirmed Burcam's Chapter 11 plan. *Id.*

The district court framed the issue presented on appeal as whether Burcam's separate classification of the CWC-purchased claims is permissible under *In re Bryson Properties XVIII*, 961 F.2d 496, 502 (4th Cir. 1992). *Id.* at 5.

In reviewing the facts of the bankruptcy court case, the district court noted that it was only after Burcam learned that CWC had purchased a majority of the unsecured claims and used these votes to reject the plan that Burcam modified the plan to segregate all the "no votes" into a single class, allowing for ultimate confirmation. *Id.* at 9. This is obvious gerrymandering. *Id.* If paying the trade creditors first was so important to Burcam, it could have classified them differently from the beginning. *Id.* Burcam's segregation of the no votes after it discovered the results of the voting is substantial evidence of voting manipulation and the bankruptcy court inexplicably failed to address this evidence, preferring instead to wholly credit the debtor's self-serving business justification. *Id.* The district court went on to add that "[i]f the bankruptcy court's finding is not overturned, Burcam will be allowed to propose a plan, learn after the votes are cast that the plan is not confirmable, re-classify the unsecured claims such that all the no votes are in one class, and thereby develop a confirmable plan that crams down the interests of the overwhelmingly largest creditor in the case." *Id.* at 12-13. Such obvious gerrymandering cannot "withstand scrutiny" under Bryson nor is it supported by the Bankruptcy Code itself. *Id.*

The district court ultimately held that the bankruptcy court's legitimate business justification finding was clearly erroneous and that separate classification in the case is not otherwise permitted under the Bankruptcy Code. *Id.* at 16. The court reversed the bankruptcy court's orders and remanded for further proceedings.

This *Burcam* opinion has no application to the instant case. The facts are easily distinguishable. This Debtor did not propose a plan, learn after the votes are cast that the plan is not confirmable and then modify the plan to create a small class of unsecured creditors designed to vote "yes" to the plan. In fact, at no time has the Debtor modified or changed the members of the unsecured class or re-balloted creditors. Any argument on gerrymandering raised by counsel for BLC should be immediately

dismissed as such an argument has no relevance to the facts of this case and the proposed Plan of Reorganization.

III. Market value versus distress value of collateral in dirt for debt cases

A key component in dirt for debt cases is the valuation of the collateral. The statutory foundations to which the Court must look in order to make a determination of valuation are found in 11 U.S.C. § 506(a) and 11 U.S.C. § 1129(b). [3] As a threshold requirement for confirmation, 11 U.S.C. § 1129(b)(2) dictates that a plan of reorganization must be fair and equitable to each impaired class of creditors. More specifically, a plan of reorganization must provide the indubitable equivalent for secured creditors whose claims are provided dirt for debt treatment. *See* 11 U.S.C. § 1129(b)(2)(A)(iii). In this case, both the Debtor and BLC presented evidence only of the "fair market value" of the collateral property. Appraisal evidence was exhaustive, but the biggest difference in values was premised upon the highest and best use. Contrast the values from one appraiser with a longstanding relationship with the creditor looking through his wood-colored glasses and seeing almost all timberland, with an appraiser who spent weeks evaluating the properties and making a detailed analysis of comparable transactions to reach values that could justifiably have been higher.

11 U.S.C. § 506(a) gives the Court authority to make a determination as to value. In its entirety, the second sentence of 11 U.S.C. § 506(a) reads:

> Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest.

Two key components of this sentence are the "purpose of the valuation" and the "proposed disposition or use of such property." In the context of a dirt for debt case, the proposed disposition of the property

[3] Debtor does not waive its arguments that the property values were established by the parties in the purchase money financing transaction.

is the surrender of collateral such that the secured creditor receives the indubitable equivalent of its claim. It is also important to note that 11 U.S.C. § 506(a) "does not necessarily contemplate forced sale or liquidation value of the collateral." *United States v. Arnold & Baker Farms*, 177 B.R. 648, 656 (9th Cir. B.A.P. 1994) (quoting H.R. Rep. No. 595, 95th Cong. 1st Sess. 356 (1977)). That concept is particularly relevant in this case, where the undisputed evidence is that BLC had owned and managed the properties for decades, unlike a traditional lender, so BLC could be expected to hold, manage or sell the property in the ordinary course of its business after surrender. Return of the land to the seller BLC would unquestionably be the "indubitable equivalent" of the debt created by the sale of that land.

11 U.S.C. § 506(a) and § 1129(b)(2) collectively require that the collateral is valued in a manner that provides that the creditor receives the indubitable equivalent of its claim. In actuality, it is of little consequence whether the collateral is being retained or surrendered, because a market value standard should reach the same value regardless of whether the collateral is being retained or surrendered. Protecting both the debtor and the creditor is the acknowledgment that "valuation is not an exact science, and … a conservative approach should therefore, be taken." *In re Bannerman* 2010 Bankr. LEXIS 3752, 12 (Bankr. E.D.N.C. October 20, 2010) (quoting *In re Simons*, 113 B.R. 942, 947 (Bankr. W.D. Tex. 1990). The purpose of requiring a conservative approach is to acknowledge the potential uncertainties in valuation, not to bar the determination of market value. The indubitable equivalent will reflect the market value of what a willing buyer would pay a willing seller for the collateral.

A. Market value standard in other courts

The use of market value has been applied in dirt for debt cases. See, e.g., *In re Stockbridge Properties I, LTD.*, 141 B.R. 469 (Bankr. N.D. Ga. 1992); *In re Immanuel LLC*, 2011 Bankr. LEXIS 1015 (Bankr. W.D. Mich. 2011).

The Bankruptcy Court for the Northern District of Georgia in *In re Stockbridge Properties* was faced with determining a valuation standard to apply in a dirt for debt scenario. The debtor owned six undeveloped outparcels that it proposed to surrender to the secured creditor. The court was faced with two competing valuation standards, a market value standard and a fair value standard. The "market value standard" was defined by the court as the most probable price that a property should bring in a competitive and open market under all conditions requisite to a fair sale with the buyer and seller each acting prudently and knowledgeably and assuming the price is not affected by undue stimulus. *In re Stockbridge Properties*, 141 B.R. 469, 471 (Bankr. N.D. Ga. 1992). The court defined a "fair value standard" as the amount that would be realized on a forced sale of the property within six months to one year of its receipt. Id. Finding that a "market value standard" was appropriate, the court determined that, "the … appraisal, which employs the fair market value test, to be more probative of the value of the outparcels … than [the] fair value appraisal. A fair value appraisal is … by definition a duress valuation." Id at 472.

The holding in *Stockbridge* is similar to the present case and is in line with the holding of *In re Brown*. As set forth above 11 U.S.C. § 506(a) and 11 U.S.C. § 1129(b)(2) require a valuation that reflects the market value as the indubitable equivalent. Consequently, the holding in *Stockbridge* is instructive on how a market value standard is appropriately applied to dirt for debt cases.

A recent decision by the Bankruptcy Court for the Western District of Michigan highlighted the application of a fair market value standard in partial dirt for debt cases. *In re Immanuel LLC*, 2011 Bankr. LEXIS 1015 (Bankr. W.D. Mich. 2011). Immanuel LLC was a real estate holding company that owned real property that it proposed to surrender to creditors pursuant to dirt for debt treatment in its reorganization plan. Id at 1, 3. The court determined that the appropriate measure of valuation was a conservative fair market value. Id at 7, 8, 27, 35. In discussing the merits of various appraisals used for

the purpose of determining *ad valorem* tax values in the context of dirt for debt, the court noted that use of such *ad valorem* appraisal values, "does not lend itself to establish valuation in the 'dirt for debt' confirmation context where so much depends upon the court's valuation decision" and where "courts must take a conservative approach to valuation." Id at 26, 27 (referencing In re Bannerman Holdings, LLC, 2010 Bankr. LEXIS 3752 (Bankr. E.D.N.C. October 20, 2010)).

Another court examined the ill effects of a fair value appraisal, analogous to a liquidation value standard, in *In re El Paso Truck Center, Inc*., 129 B.R. 109, 112 (Bankr. W.D. Tex. 1991). The Bankruptcy Court for the Western District of Texas contemplated valuation under 11 U.S.C. § 506(a) and determined it "could find no rational basis for superimposing … fair value on top of the market value." In its discussion of the pitfalls of a fair value appraisal, the court noted:

> "a fair value is also by definition a duress valuation. All that such a directive tells us is what bottom fishers are likely to pay for such a property. Invariably, such an approach to valuation does little more than magnify the current market's anomalies … Given the importance of accurate valuation to the competing interests of both secured and unsecured creditors (and debtors too for that matter), adopting such a valuation technique would be irresponsible."

Id at 112.

B. Market value standard in EDNC dirt for debt cases

The Eastern District of North Carolina has been presented several cases involving plans of reorganization that included dirt for debt treatments. See *In re Bannerman Holdings, LLC*, 2010 Bankr. LEXIS 3752 (Bankr. E.D.N.C. October 20, 2010); *In re Sailboat Properties, LLC* 2011 Bankr. LEXIS 1316 (Bankr. E.D.N.C March 31, 2011); *In re Bath Bridge Water South, LLC* Case No. 11-06817-8-SWH, 2013 (Bankr. E.D.N.C. 2013). In none of these cases was there a determination as to which valuation standard should be used. However, each of these cases set forth the groundwork to demonstrate that a market valuation standard should be used in determining the valuation of collateral.

The *Bannerman Holdings* court decision highlighted the importance of indubitable equivalence and the need to present "evidence focused on the value of the specific property to be surrendered" in dirt

for debt cases. *In re Bannerman Holdings, LLC*, 2010 Bankr. LEXIS 3752, 2, 26 (Bankr. E.D.N.C. October 20, 2010). This basic tenet coupled with the notion that valuations should be conservative in nature set forth the foundation by which valuations should be conducted. The trial court only heard testimony on market value and determined which appraisal evidence was most credible in rendering its opinion.

On appeal, the district court for the Eastern District of North Carolina had the opportunity to examine the issues of indubitable equivalence upon an appeal of the order confirming the debtor's plan of reorganization in *In re Bannerman Holdings, LLC.* See *Sun Trust Bank v. Bannerman Holdings, LLC*, No. 7:11-cv-00009-H (E.D.N.C. September 30, 2011). In remanding the case for further hearing, the district court held that the evidence of valuation presented was a muddled attempt at ascertaining the indubitable equivalent. Id. It was noted that, "the valuation evidence submitted to the bankruptcy court was wide ranging and each adjustment made injected further uncertainty into already tenuous valuation evidence." Id at 16. The application of the district court's holding is the requirement that any evidence of valuation presented need accurately reflect the indubitable equivalent of the collateral. Applying a market value standard is in accordance with the district court's holding because it values the property in a manner which is indicative of the indubitable equivalent. It should be noted that the district court's ruling was based solely on the issue of whether the confirmed plan provided the indubitable equivalent of SunTrust's secured claim and further that the district court did not find that the valuation itself was erroneous.

Only one Eastern District of North Carolina case discusses the appropriate valuation standard. *See Gateway Bank and Trust Company v. Clarendon Holdings, LLC*, No. 7:11-cv-247-H (E.D.N.C. March 18, 2013). At the valuation hearing in the bankruptcy court, the debtor argued that the court should apply a fair-market-value standard regardless of whether the property was to be retained by the

debtor or transferred to Gateway under the plan of reorganization. Id. at 2. Gateway argued that fair market value would apply only if the debtor retained the property and that a liquidation value standard would apply were the property to be transferred to Gateway. Id. The bankruptcy court ruled that the property should be valued according to its fair market value for purposes of the debtor's intended plan to surrender the property to Gateway. Id. The sole issue on appeal was whether the bankruptcy court erred in applying fair-market-value standard in its valuation of collateral that the debtor proposed to surrender to Gateway in exchange for a credit against the indebtedness owed.

As discussed in the first segment of this brief, the district court reviewed the valuation in light of *Associates Commercial Corp. v. Rash*, 520 U.S. 953, 962 (1997). The Court noted that under the ruling in *Rash*, if a debtor chooses to avoid foreclosure and liquidation and retain collateral for its own use, the property must be valued using a replacement-value standard because that standard fairly compensates the secured creditor for deprivation of immediate value, as well as exposure to the attendant risks of the plan. Id at 3, 4. Conversely the court noted that, under *Rash*, a debtor that surrenders collateral for purposes of the creditors' liquidation of the property is not be [sic] entitled to the full fair market value of the property. Id at 4. The district court went on to note that where a plan shifts to the creditor the burden to sell, and hence the risk of loss or potential for gain, the court must take these matters into consideration in valuing the property. Id. As an example the court noted that if a depressed market makes the potential for loss greater than the potential for gain, valuation must be approached conservatively. Id. Additionally, the valuation of property surrendered to a creditor should take into account the loss of income a creditor may encounter prior to the sale or liquidation of the property. Id.

The *Clarendon* appellate court noted that it is unclear from the record on appeal whether the bankruptcy court below considered such factors in determining the value of the collateral to be surrendered by debtor and remanded the case to bankruptcy court. Id. However, the district court did

not specifically rule that the valuation standard should be the surrender value standard set forth in *Rash*. Rather, the court found that the valuation standard is fair market value if the court takes into account the factors listed in its opinion.

In re Sailboat Properties, LLC added an additional step to the dirt for debt valuation methodology used in the Eastern District of North Carolina. A four-part highest and best use test for collateral was adopted, whereby, "the court must first ask: what is the highest and best use of the collateral? Second, what use of the collateral will yield the highest net value? Third, is the highest and best use of the collateral the use that will yield the highest net value? And finally, is that use reasonably available to the secured creditor?" *In re Sailboat Properties, LLC*, 2011 Bankr. LEXIS 1316, 6 (Bankr. E.D.N.C March 31, 2011). The elements of the four part test clearly point to a market value standard whereby the collateral's projected value is sought at its highest point -- not at a point of duress or liquidation value. Additionally, the four part test built upon the conservative approach espoused in *In re Bannerman* protects a secured creditor's interest in the collateral, while ensuring that the value reflects an accurate market value.

In re Bath Bridge Water South, LLC involved a dirt for debt plan where the debtor proposed to surrender to Capital Bank, N.A. ("Capital") a sufficient amount of its properties to provide for Capital's realization of the "indubitable equivalent" of its claims. *In re Bath Bridge Water South, LLC* Case No. 11-06817-8-SWH, 2013 (Bankr. E.D.N.C. 2013).

The court held that the treatment of a secured creditor "may be deemed fair and equitable if it satisfies one of the three criteria set forth under §1129(b)(2)(A)." Id. at 8 citing *In re Bannerman Holdings, LLC*, 2010 Bankr. LEXIS 3752, at 7. In *Bath Bridge Water* the court noted that in analyzing the treatment of Capital's claim, the determination of the value of the properties offered by the debtor for surrender to Capital and the extent to which the debtor will surrender those properties, is most

appropriately and effectively made in the context of whether the debtor's treatment of Capital is fair and equitable and is not limited to the valuation made by the court in determining the existence of a deficiency claim. Id.

The court went on to note that because the court employed a conservative analysis in determining the value of the Bridgewater South property, that value as determined by the court will be used in the indubitable equivalent calculation. Id. See also *In re 3G Properties, LLC*, Case No. 10-04763-8-JRL, 2011 Bankr. LEXIS 4634, at 16, 2011 WL 5902504, at 6 (providing that a conservative approach must be taken for valuations in determining whether the property proposed to be surrendered constitutes the indubitable equivalent of the creditor's claim) (quoting *In re Bannerman Holdings, LLC*, 2010 Bankr. LEXIS 3752, at 12). In reaching the value of the subject property the court analyzed at length various appraisals and the testimony of each appraiser and quoted *In re Sailboat Properties, LLC* - "When two appraisal reports conflict, a court must determine the value based on the credibility of the appraisers, the logic of their analys[es] and the persuasiveness of their subjective reasoning." *In re Sailboat Properties, LLC*, 2011 Bankr. LEXIS 1316, at 17.

Under the court's final valuation it held that there was too much value in the subject property (lots) to require that all 28 lots be surrendered to Capital in order to satisfy the indubitable equivalent test. Id. at 13. "Keeping in mind that any valuation to determine satisfaction of the indubitable equivalent test must be conservative", *In re Bannerman Holdings, LLC*, 2010 Bankr. LEXIS 3752, at 12, "the court holds that the debtor must surrender 18 of the 28 lots to Capital in order to satisfy § 1129(b)(2)(A)(iii)." Id. The court concluded that Capital will receive the indubitable equivalent of its secured claim and the plan's treatment of Capital is thus fair and equitable. The court also held that the court will allow the debtor to choose which of the 18 lots in Catnip Estates it will surrender to Capital. Id.

CONCLUSION

The Debtor has filed its Petition and proposed its Plan in good faith, and the necessary votes have been cast. After exhaustive testimony and hearings, the evidentiary record is complete. The lasting result of *In re Bannerman*, *In re Clarendon*, *In re Sailboat Properties* and *In re Bath Bridge Water South*, as well as the cases from other courts considering dirt for debt plans, is the creation of a standard that is purely driven by what the market dictates for collateral at its highest and best use. And, in doing so, a market value standard reflects both the protection of the secured creditor's interest and accurately reflects the value of the collateral. Furthermore the recent decision in *In re Brown* establishes that this Court is not bound by the rationale of *Rash*, that the disposition and use of the collateral is irrelevant, and that the collateral in a dirt for debt case should be valued based on replacement or market value. Particularly under the facts of this case, where the creditor BLC is not a traditional third party bank who simply loaned money to a debtor to purchase property, but a savvy and long-term holder and manager of real estate who sold the property to the Debtor, the return of collateral property at its market value (if not the original purchase price) is the indubitable equivalent of the claim.

DATED: 09/11/2014

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CERTIFICATE OF SERVICE

I, George M. Oliver, Post Office Box 1548, New Bern, North Carolina 28563, certify:

That I am, and at all times hereinafter mentioned was, more than eighteen (18) years of age;

That on the 11th day of September, 2014, I served copies of the foregoing Supplemental Brief on the parties electronically as indicated.

I certify under penalty of perjury that the foregoing is true and correct.

DATED: 09/11/2014

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