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**FILED**  
**JAN 08 2018**  
 UNITED STATES BANKRUPTCY COURT  
 EASTERN DISTRICT OF CALIFORNIA

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 EASTERN DISTRICT OF CALIFORNIA

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In re ) Case No. 17-23627-B-11  
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 CAPITOL STATION 65, LLC, a ) DC No. NH-3  
 ) California Limited Liability )  
 ) Company, )  
 )  
 Debtor(s). )

\_\_\_\_\_ )  
 In re ) Case No. 17-23629-B-11  
 )  
 CAPITOL STATION MEMBER, LLC, )  
 )  
 Debtor(s). )

\_\_\_\_\_ )  
 In re ) Case No. 17-23628-B-11  
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 CAPITOL STATION HOLDINGS, LLC, )  
 )  
 Debtor(s). )

\_\_\_\_\_ )  
 In re ) Case No. 17-23630-B-11  
 )  
 TOWNSHIP NINE OWNERS, LLC, )  
 )  
 Debtor(s). )

NOT FOR PUBLICATION

**MEMORANDUM AND ORDER GRANTING MOTION TO APPROVE POSTPETITION  
 FINANCING, GRANTING PRIMING LIEN, AND RELATED RELIEF**

Presently before the court is a motion by Capitol Station 65, LLC, Capital Station Member, LLC, Capitol Station Holdings, LLC, and Township Nine Owners, LLC, each a debtor and debtor in possession - collectively, "Debtors" - to approve postpetition

1 financing, grant a priming lien, and for related relief. An  
2 initial hearing on the motion was held on August 29, 2017. A  
3 final evidentiary hearing on the motion was held on December 11,  
4 2017. Appearances at both hearings were noted on the record.  
5 This memorandum and order constitutes the court's final decision  
6 on the motion and its findings of fact and conclusions of law  
7 pursuant to Federal Rule of Civil Procedure 52(a) applicable by  
8 Federal Rules of Bankruptcy Procedure 7052 and 9014(c).

9  
10 **INTRODUCTION**

11 The Debtors request authorization to borrow up to an  
12 aggregate amount of \$10,000,000.00 from Serene Investment  
13 Management, LLC, or its assigns ("Serene"), as postpetition  
14 debtor in possession financing (the "DIP Loan"). The Debtors  
15 also request authorization to grant Serene a super-priority  
16 administrative claim and a senior priming lien on substantially  
17 all real and personal property assets, including the real  
18 property comprising the development known as the Township Nine  
19 project which encompasses approximately 65 acres bound by North  
20 5th Street on the west, North 7th Street on the east, Richards  
21 Boulevard on the south, and the American River on the north (the  
22 "Township Nine Property"). The Township Nine Property, and the  
23 Debtors' other personal property assets, are encumbered by a deed  
24 of trust held by Township Nine Avenue, LLC, which is the assignee  
25 of Copia Lending, LLC.<sup>1</sup> There are also additional encumbrances

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<sup>1</sup>To avoid confusion, Township Nine Avenue, LLC, will be referred to by its former name, i.e., Copia.

1 on the Township Nine Property.

2 Copia opposes the motion and the DIP Loan. Copia filed an  
3 initial opposition on August 15, 2017, and a supplemental  
4 opposition on November 27, 2017. The Debtors filed an initial  
5 reply on August 22, 2017, and a supplemental reply on December 4,  
6 2017. The Unsecured Creditors' Committee also filed a position  
7 statement on August 15, 2017, and it has expressed support for  
8 both the motion and the DIP Loan.

9 At the conclusion of the August 29, 2017, hearing the court  
10 granted the Debtors' motion on an interim basis and authorized  
11 the Debtors to borrow up to \$1,900,000.00 through December 8,  
12 2017. The borrowing date was subsequently extended to January 9,  
13 2018, and the amount increased to \$2,000,000.00 on a further  
14 interim basis following the final evidentiary hearing held on  
15 December 11, 2017.

16 As an initial matter, the court adopts and by this reference  
17 incorporates herein its evidentiary rulings stated on the record  
18 in open court on December 11, 2017, regarding objections to, and  
19 the admissibility and admission of, the parties' direct testimony  
20 declarations and exhibits.

21 The court also adopts and incorporates herein as its final  
22 findings of fact and conclusions of law the tentative findings of  
23 fact and conclusions of law stated on the record in open court on  
24 August 29, 2017, as they pertain to the following sections of  
25 Copia's initial opposition: (i) § III.A. (objection re: "end run"  
26 around § 362(d)(3)); and (ii) § III.C. (objection re: use of the  
27 proposed DIP Loan as a sub-rosa plan). See Transcript, dkt. 128,  
28 at 6:3-7:17 (re: § III.A.) and 10:12-11:13 (re: § III.C.).

1 Section III.F. of Copia's initial opposition, which pertains to  
2 repayment of the DIP Loan, was addressed and sufficiently  
3 resolved by the § 1125 "adequate information" disclosures made in  
4 the context of the now-approved disclosure statement. See dkts.  
5 175, 177, and 179.

6 In addition to valuation and adequate protection  
7 determinations, that leaves §§ III.B., III.D., and III.E. of  
8 Copia's initial opposition and the additional objections and  
9 arguments in Copia's supplemental opposition. Those matters are  
10 addressed below.

11  
12 **BACKGROUND**

13 As noted above, the Township Nine Property is a master  
14 planned development that consists of approximately 65 gross acres  
15 north of Downtown Sacramento. The development includes  
16 approximately 31.62 net developable acres. Anthem United Homes,  
17 Inc. ("Anthem") is under contract to buy 11.27 of the net  
18 developable acres (land) for \$17,677,000.00. Anthem will also  
19 assume \$4,398,420.00 in infrastructure completion costs  
20 associated with the land it is buying. It is also buying fee  
21 credits.

22 The Township Nine Property is a mixed-use, transit-oriented  
23 development that does and will include high-density rental units  
24 and for-sale housing, retail and office space, open space,  
25 trails, and parks. It includes 2,201 residential units  
26 consisting of apartments, condominiums, hotel, hospitality, and  
27 attached and detached townhouse projects. It also includes up to  
28 840,000 square feet of office space and 150,000 square feet of

1 retail space as well as 27 acres of parks and open space. The  
2 development is light rail accessible on the Green Line and  
3 includes extensive footage along the American River and Twin  
4 Rivers Bike Trail. The project was entitled in August 2007, with  
5 the tentative map amended in 2010 and again in 2017.

6 Copia holds a first deed of trust on the Township Nine  
7 Property. That deed of trust secures Copia's 2008 loan to the  
8 Debtors in the original principal amount of \$20,000,000.00.  
9 Copia contends that as of December 11, 2017, the loan balance is  
10 \$46,787,543.00, exclusive of attorney's fees after May 24, 2017.  
11 The Debtors dispute that amount. Other encumbrances on the  
12 Township Nine Property total approximately \$597,154.00.

13 On December 11, 2017, the court heard several hours of  
14 testimony by two appraisers: Arthur E. Gimmy, President of AGI  
15 Valuations ("AGI"), and Adam Bursch, Director of Appraisal with  
16 Bender Rosenthal, Inc. ("BRI"). Both appraisers have extensive  
17 education, training, and professional qualifications. Both are  
18 qualified as experts.

19 Mr. Gimmy testified for the Debtors. Mr. Gimmy prepared an  
20 appraisal which the Debtors submitted with their motion. That  
21 initial appraisal, dated March 29, 2016, concluded that as of  
22 March 15, 2016, (i) the total appraised market value of the  
23 Township Nine Property, with fee credits, was \$78,160,000.00, and  
24 (ii) the market value of the "as is" fee simple interest in the  
25 Township Nine Property, without fee credits, was \$64,950,000.00.

26 Mr. Gimmy also prepared an updated appraisal. That updated  
27 appraisal is dated October 2, 2017. It relies on discounted  
28 comparables from the Downtown, Midtown, and East Sacramento area

1 markets. It concludes that, as of October 2, 2017, (i) the total  
2 appraised "as is" market value of the Township Nine Property,  
3 with fee credits (valued at \$16,512,769.00) and less the cost to  
4 complete remaining infrastructure (estimated at \$9,918,500.00) is  
5 \$77,950,000.00 and (ii) the market value of the "as is" fee  
6 simple interest in the Township Nine Property exclusive of fee  
7 credits and reflecting the cost to complete the remaining  
8 infrastructure is \$61,431,500.00 (the "AGI Appraisal").<sup>2</sup>

9 Mr. Bursch testified for Copia. Mr. Bursch prepared an  
10 appraisal that Copia submitted with its initial opposition to the  
11 Debtors' motion. That initial appraisal, dated May 26, 2017,  
12

13 <sup>2</sup>In addition to the March 2016 and October 2017 appraisals,  
14 Mr. Gimmy and AGI have a long history of valuing Township Nine  
15 Property for the Debtors' current and former owners, and for  
16 Copia. Those valuations are as follows:

- 17 (a) an appraisal for Copia with a value date of  
18 January 2012 and market value opinion of  
19 \$51,400,000.00;
- 20 (b) an appraisal for Nehemiah Corporation of America  
21 ("Nehemiah") with a value date of December 24,  
22 2012, and market value opinion of \$57,200,000.00;
- 23 (c) an appraisal for Nehemiah with value date of  
24 December 20, 2013, and market value opinion of  
25 \$61,500,000.00;
- 26 (d) an appraisal for Nehemiah with a value date of  
27 December 31, 2014, and market value opinion of  
28 \$64,950,000.00;
- (e) an appraisal for Nehemiah with a value date of  
August 15, 2015, and market value opinion of  
\$64,950,000.00 without fee credits and  
\$78,160,000.00 with updated fee credit values; and
- (f) an appraisal for Nehemiah with a value date of  
December 31, 2015, and market value opinion of  
\$64,950,000.00 without fee credits and  
\$78,160,000.00 with updated fee credit values.

The appraisal in ¶(a) was prepared directly for Copia. The appraisals in ¶¶ (d) and (f) were prepared at Copia's request but paid for by Nehemiah. BRI does not have a similar history of appraising the Township Nine Property.

1 concluded that as of December 31, 2016, the market value of the  
 2 Township Nine Property, (i) with fee credits, was \$27,100,000.00,  
 3 and (ii) without fee credits, was \$12,810,000.00.

4 Mr. Bursch also prepared an updated appraisal. That updated  
 5 appraisal is dated September 26, 2017. It relies on no Downtown  
 6 and Midtown comparables, and, instead, relies exclusively on  
 7 comparables from West and East Sacramento and the River District  
 8 neighborhood. It concludes that as of September 15, 2017, the  
 9 Township Nine Property has a market value, (i) with fee credits  
 10 (valued at \$13,190,000.00) of \$46,540,000.00, and (ii) without  
 11 fee credits of \$33,350,000.00 (the "BRI Appraisal").

12 A summary of the AGI and BRI Appraisals is as follows:

13 **AGI**

<u>Appraisal Date</u>	<u>Valuation Date</u>	<u>W/ Fee Credits</u>	<u>W/O Fee Credits</u>
March 29, 2016	March 15, 2016	\$78,160,000.00	\$64,950,000.00
October 2, 2017	October 2, 2017	\$77,950,000.00	\$61,431,500.00

16 **BRI**

<u>Appraisal Date</u>	<u>Valuation Date</u>	<u>W/ Fee Credits</u>	<u>W/O Fee Credits</u>
May 26, 2017	December 31, 2016	\$27,100,000.00	\$12,810,000.00
September 26, 2017	September 15, 2017	\$46,540,000.00	\$33,350,000.00

19 The updated AGI Appraisal and the updated BRI Appraisal, and  
 20 their respective exhibits, were admitted into evidence and are  
 21 the governing appraisals and exhibits for purposes of the  
 22 December 11, 2017, final evidentiary hearing.

23 In addition to Messrs. Gimmy and Bursch, the court also  
 24 heard expert testimony and received into evidence a report from  
 25 Dean Wehrli, Senior Vice President, John Burns Real Estate  
 26 Consulting, LLC, on behalf of the Debtors. Mr. Wehrli's  
 27 testimony and report concerned the Downtown and Midtown  
 28

1 competitive market areas, the inclusion of the Township Nine  
2 Property in those market areas, and the appropriate use of a  
3 discount applicable to comparables from those market areas to  
4 value the Township Nine Property. Copia provided no similar  
5 expert testimony independent of Mr. Bursch's opinion. Alberto  
6 Esquivel, Project Manager for Capitol Station 65, LLC, also  
7 testified for the Debtors. And the court admitted into evidence  
8 a declaration of Robert Perkins for the limited purpose of  
9 establishing the disputed amount of the debt owed to Copia. The  
10 testimony of these witnesses and the exhibits are discussed in  
11 greater detail below.

12 Debtors' Exhibit Q was also admitted into evidence as  
13 Copia's business record. Exhibit Q consists of a number of Real  
14 Estate Portfolio Reports in which Copia's agent, TDA Investment  
15 Group, represented to its investor, Construction Laborers Pension  
16 Trust for Southern California, historical values of the Township  
17 Nine Property consistent with a number of AGI's prior appraisals  
18 of the property.<sup>3</sup> Those representations of value are as follows:

- 19 (1) \$40,400,000.00 (land value) for the quarter ended  
20 December 31, 2009:
- 21 (2) \$51,400,000.00 for the quarters ended December 31,  
22 2011; March 31, 2012; June 30, 2012; September 30,  
23 2012; December 31, 2012:
- 24 (3) \$57,200,000.00 for the quarters ended March 31,  
25 2013; June 30, 2013; September 30, 2013:
- 26 (4) \$61,500,000.00 for the quarters ended December 31,  
27 2013; March 31, 2014; June 30, 2014; September 30,  
28 2014:
- 29 (5) \$64,950,000.00 for the quarters ended December 31,

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<sup>3</sup>Mr. Gimmy testified that TDA is an agent of Copia. His testimony on that point was not disputed or rebutted.

1           2014; March 31, 2015; June 30, 2015; September 30,  
2           2015: and,

3           (6) \$78,000,000.00+ for the quarters ended December  
4           31, 2015; March 31, 2016; June 30, 2016; September  
5           30, 2016; December 31, 2016; March 31, 2017; June  
6           30, 2017.

7           Notably, the \$51,400,000.00, \$64,950,000.00, and  
8           \$78,000,000.00 value representations are consistent with value  
9           conclusions in the AGI appraisals that were prepared for and  
10          requested by Copia as noted in footnote 2, supra. Copia and/or  
11          its agent did not criticize or object to the methodology,  
12          assumptions, or ultimate value conclusions in any of AGI's prior  
13          appraisals of the Township Nine Property.

14          Valuation at this stage of the chapter 11 case is critical.  
15          It will determine whether the Debtors are able to borrow up to  
16          \$10,000,000.00 from Serene and grant Serene a senior lien that  
17          primes Copia's existing deed of trust and all other encumbrances  
18          on the Township Nine Property.

19          Exercising their business judgment, the Debtors have  
20          selected Serene as their debtor in possession lender. Without  
21          Serene, and the ability to grant Serene a super-priority  
22          administrative claim and senior priming lien, the Debtors could  
23          not obtain any credit or postpetition financing, unsecured or  
24          otherwise. And the Debtors made diligent efforts to do so.

25          Early on, the Debtors engaged the assistance of Tim Eppler  
26          of COF Capital Partners. Mr. Eppler is qualified in the area of  
27          real estate finance, including distressed lending and debtor in  
28          possession financing. Mr. Eppler approached six potential  
29          lenders on the Debtors' behalf in an effort to procure  
30          postpetition debtor in possession financing. The Unsecured

1 Creditors Committee also assisted in the search for other  
2 potential lenders.

3 All lenders that Mr. Eppler contacted requested a first  
4 priority and senior lien on the Debtors' assets. All lenders  
5 also offered interest rates that varied from 14% to 18%. Serene,  
6 on the other hand, offered a lower interest rate at 10% - which  
7 is actually lower than Copia's current 16% default rate. Serene  
8 also offered the Debtors terms more favorable than the other  
9 lenders contacted. For example, Serene offered the Debtors an  
10 option to convert the postpetition financing into  
11 postconfirmation financing (rather than the paying the DIP Loan  
12 in full on effective date). Serene also offered lower fees. And  
13 Serene agreed to terms for release prices for parcels of the  
14 Township Nine Property as they are sold.

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16 **JURISDICTION**

17 Federal subject matter jurisdiction is founded on 28 U.S.C.  
18 § 1334. This is a core proceeding under 28 U.S.C. §§  
19 157(b)(2)(A), (B), (L), (M), and (O). To the extent this is a  
20 matter that may ever be determined to be a matter that a  
21 bankruptcy judge may not hear and determine without consent, the  
22 parties have nevertheless consented to such determination by a  
23 bankruptcy judge. See 28 U.S.C. § 157(c)(2). Venue is proper  
24 under 28 U.S.C. § 1409.

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1 DISCUSSION

2 I. Valuation Analysis and Value Determination

3 A. Appraisal Standards

4 Valuation of property in bankruptcy a case may be determined  
5 in various contexts and for different purposes throughout the  
6 case. Fin. Sec. Assurance Inc. v. T-H New Orleans Ltd. P'ship  
7 (In re T-H New Orleans Ltd. P'ship), 116 F.3d 790, 797 (5th Cir.  
8 1997) (valuation issues arise in various contexts including  
9 establishing equity, adequate protection, and plan confirmation).  
10 In the context of the motion before the court, the court is asked  
11 to value the Township Nine Property for DIP Loan adequate  
12 protection purposes and for plan confirmation.

13 Bankruptcy courts are given considerable flexibility in  
14 resolving valuation issues. Id. at 799; see also 4 COLLIER ON  
15 BANKRUPTCY ¶ 506.03[7], at 506-50 (Alan N. Resnick & Henry J.  
16 Sommer eds., 16th ed. 2010). Valuation of property is not an  
17 exact process. See Boyle v. Wells (In re Gustav Schaefer Co.),  
18 103 F.2d 237, 242 (6th Cir.); cert. denied, 308 U.S. 579, 60  
19 (1939) ("The valuation of property is an inexact science and  
20 whatever method is used will only be an approximation[.]"). In  
21 fact, courts are often greeted with conflicting appraisals and  
22 testimony, to which weight must be assigned depending upon  
23 credibility assessments. In re Smith, 267 B.R. 568, 572 (Bankr.  
24 S.D. Ohio 2001) ("Because the valuation process often involves  
25 the analysis of conflicting appraisal testimony, a court must  
26 necessarily assign weight to the opinion testimony received based  
27 on its view of the qualifications and credibility of the parties'  
28 expert witnesses."); In re Coates, 180 B.R. 110, 112 (Bankr.

1 D.S.C. 1995) ("The valuation process is not an exact science, and  
2 the court must allocate varying degrees of weight depending upon  
3 the court's opinion of the credibility of ... [the appraisal]  
4 evidence.").

5 A bankruptcy court is not bound by valuation opinions or  
6 reports submitted by appraisers, and may form its own opinion as  
7 to the value of property in bankruptcy proceedings. See In re  
8 Patterson, 375 B.R. 135, 144 (Bankr. E.D. Pa. 2007). Indeed, the  
9 Ninth Circuit has stated that a court may reject an appraisal or  
10 not credit it with any weight whatsoever when determining value.  
11 See Sammons v. C.I.R., 838 F.2d 330, 334 (9th Cir. 1988). And as  
12 one court in the Ninth Circuit explained:

13 Complex factual inquiries such as valuation require the  
14 trial judge to evaluate a number of facts: whether an  
15 expert appraiser's experience and testimony entitle his  
16 opinion to more or less weight; whether an alleged  
17 comparable sale fairly approximates the subject  
18 property's market value; and the overall cogency of  
19 each expert's analysis. Sammons v. Comm's of IRS, 838  
20 F.2d 330, 333 (9th Cir. 1988); Ebben v. Comm's, 783  
21 F.2d. 906, 909 (9th Cir. 1986). The court does not  
22 necessarily abuse its discretion if it decides to  
23 reject an appraisal. Id.

19 In re Ahmed, 2011 WL 1004649, \*2 (Bankr. N.D. Cal. 2011); see  
20 also In re Evans, 492 B.R. 480, 508 (Bankr. S.D. Miss. 2013) ("A  
21 court may accept an appraisal in its entirety, may choose to give  
22 weight only to portions of the appraisal, or may reject the  
23 appraisal altogether.").

24 An appraisal may be rejected as unreliable when it is based  
25 on assumptions that are fundamental to the appraiser's conclusion  
26 with no anchors to reality thereby rendering the assumptions  
27 fundamentally flawed. In re Diamond Beach VP, LP, 506 B.R. 701,  
28 717-718 (Bankr. S.D. Tex. 2014). An appraisal may also be

1 rejected when its purpose is suspect. See In re Hoosier Hi-  
2 Reach, Inc., 64 B.R. 34, 38 (Bankr. S.D. Ind. 1986). And  
3 significantly, where only one of two competing appraisals is  
4 based on relevant comparables the court may reject in its  
5 entirety the other appraisal that is not. See In re Jones, 2004  
6 WL 298612, \*2 (Bankr. C.D. Ill. 2004). Indeed, "[a]ppraisals  
7 that use comparable properties that are so dissimilar to the  
8 subject property have been recognized as unreliable." In re Pod,  
9 560 B.R. 77, 83 (Bankr. E.D.N.Y. 2016) (citations omitted); see  
10 also In re Brown, 289 B.R. 235, 238 (Bankr. M.D. Fla. 2003)  
11 ("[T]he better reasoned approach is to review all of the proposed  
12 comparables, including in its analysis only those that assist the  
13 Court in its determination.").

14 B. The Appraisals

15 The AGI Appraisal and the BRI Appraisal differ dramatically  
16 with regard to the comparables that each uses to value the  
17 Township Nine Property. The AGI Appraisal relies on Downtown and  
18 Midtown comparables whereas the BRI Appraisal excludes  
19 comparables from those areas and relies on comparables from East  
20 and West Sacramento and the River District neighborhood. Mr.  
21 Bursch testified that the comparables used to value the Township  
22 Nine Property are the most important factor in each appraiser's  
23 opinion of value. The court agrees with that concept. See In re  
24 Wood, 2017 WL 562248, \*5 (Bankr. D. N.H. 2017) ("If an appraiser  
25 has chosen the 'wrong' comparable sales, i.e., properties that  
26 are not actually comparable, then the adjustments an appraiser  
27 makes to the comparable sales do not really matter.").

28 Substantial evidence supports the placement of the Township

1 Nine Property in the Downtown and Midtown market areas. Colliers  
2 International, an industry-leading global real estate company  
3 with extensive knowledge and experience in commercial and  
4 property development real estate, is cited throughout the BRI  
5 Appraisal. Colliers is a credible data source. Colliers places  
6 the Township Nine Property in the Central Sacramento submarket,  
7 the Downtown/Midtown/East Sacramento retail submarket, and the  
8 Downtown Sacramento office submarket. Mr. Bursch also  
9 acknowledged on cross-examination that the Township Nine Property  
10 is in (and within) those Downtown and Midtown market areas. And  
11 he also acknowledged on cross-examination that the Township Nine  
12 Property is within the same "CMA" - or "competitive market area"  
13 which is defined as the geographic source of competitive real  
14 estate supply - as the Downtown and Midtown market areas. In  
15 that regard, Mr. Bursch's latter acknowledgment is consistent  
16 with Mr. Wehrli's expert testimony and report, which are credible  
17 and which the court accords substantial weight. Both place the  
18 Township Nine Property in the same competitive market area as  
19 Downtown and Midtown.

20 The categorical exclusion of Downtown and Midtown  
21 comparables from the BRI Appraisal renders the BRI Appraisal  
22 unreliable and internally inconsistent. The BRI appraisal is  
23 unreliable because Downtown comparables are relevant, if not  
24 critical, to the determination of the value of the Township Nine  
25 Property. That means by excluding Downtown and Midtown  
26 comparables the BRI Appraisal uses comparables that are too  
27 dissimilar from the Township Nine Property and, in that regard,  
28 it uses the wrong comparables. That also means the analysis

1 applied to the comparables used in the BRI Appraisal really does  
2 not matter. The BRI Appraisal is also internally inconsistent,  
3 and thereby inherently unreliable, because, on the one hand, the  
4 appraisal and its author acknowledge that the that the Township  
5 Nine Property is in (and within) the Downtown and Midtown market  
6 areas and, at the same time, the appraisal excludes Downtown and  
7 Midtown comparables.

8 Mr. Bursch gave several reasons in an attempt to justify the  
9 exclusion of Downtown and Midtown comparables from the BRI  
10 Appraisal. However, the court finds and concludes that none of  
11 those reasons are credible.

12 Mr. Bursch testified that he excluded Downtown and Midtown  
13 comparables from the BRI Appraisal based on "surveys" - which  
14 were actually free-form telephone conversations - that he  
15 conducted with numerous "market participants." Mr. Bursch  
16 testified on the witness stand that he asked *each* market  
17 participant with whom he spoke their opinion about comparisons  
18 between the Downtown and Midtown market areas and the Township  
19 Nine Property, and the use of the former as comparables for the  
20 latter. Mr. Bursch was then presented with his deposition  
21 testimony where he was asked if he asked *each* "market  
22 participant" whether Downtown and Midtown market areas should be  
23 used as comparables for the Township Nine Property and his answer  
24 during his deposition was a direct "No."

25 In short, Mr. Bursch's directly contradicted himself on a  
26 critical point relevant to the appraisal process and the Township  
27 Nine Property valuation analysis. The court draws several  
28 conclusions from Mr. Bursch's conflicting testimony.

1 First, and most important, Mr. Bursch's conflicting witness  
2 stand and deposition testimony weighs negatively on his overall  
3 credibility.

4 Second, if Mr. Bursch's witness stand testimony is not true  
5 and his deposition testimony is true, *i.e.*, he did not ask each  
6 "market participant" about the Township Nine Property in  
7 comparison to the Downtown and Midtown market areas, then it  
8 would appear that Mr. Bursch contradicted himself on the witness  
9 stand in an effort to justify the exclusion of Downtown and  
10 Midtown comparables from the BRI Appraisal by creating the false  
11 impression of a unanimous opinion among "market participants"  
12 that the Township Nine Property is not comparable to the Downtown  
13 and Midtown areas.

14 Third, if Mr. Bursch's witness stand testimony is true and  
15 his deposition testimony is not true, *i.e.*, he did ask each  
16 "market participant" with whom he spoke about the use (and  
17 exclusion) of Downtown and Midtown comparables for the Township  
18 Nine Property, then his opinion of value was unduly and  
19 prejudicially influenced. Mr. Bursch also testified that one of  
20 the "market participants" with whom he spoke is a competitor of  
21 the Debtors. As the Debtors' competitor that "market  
22 participant" would have a significant financial motive and  
23 business incentive to exclude the Township Nine Property from the  
24 Downtown and Midtown market areas and thereby influence a  
25 substantial reduction in the value of the Township Nine Property.

26 Mr. Bursch also testified that he excluded Downtown and  
27 Midtown comparables from his valuation analysis in the BRI  
28 Appraisal because the Township Nine Property does not have the

1 quality and concentration of amenities that are found in the  
2 Downtown and Midtown areas. It is true that the Township Nine  
3 Property offers fewer and different types of amenities than the  
4 amenities found in the immediate Downtown and Midtown market  
5 areas. For example, whereas Downtown and Midtown offer access to  
6 bars, restaurants, grocery, retail, and entertainment the  
7 Township Nine Property offers access to parks, trails, open  
8 space, and river and light rail access. However, Mr. Bursch also  
9 testified that no one amenity is more important than another and  
10 the market does not distinguish between amenities because the  
11 market does not have the granularity to differentiate in the  
12 value of amenities. And if the market lacks the granularity to  
13 distinguish between the value of different amenities then, as Mr.  
14 Wehrli's expert testimony and report establish, it is more  
15 appropriate and reliable to include, and then discount, Downtown  
16 and Midtown comparables, as the AGI Appraisal does, rather than  
17 to categorically exclude comparables from those areas, as the BRI  
18 Appraisal does.

19 Including, and then discounting, Downtown and Midtown  
20 comparables, rather than excluding those comparables altogether,  
21 is also consistent with the "walkability" concept as it pertains  
22 to the amenities that each area offers. Both appraisers  
23 testified that "walkability" is an important consideration in the  
24 context of amenities. "Walkability" was defined to include  
25 access to amenities from within one-quarter to one mile. Mr.  
26 Bursch acknowledged that the Township Nine Property is within one  
27 mile of the central core of the central Downtown Sacramento  
28 business district. That puts many of the amenities in the

1 Downtown and Midtown areas, including the Golden 1 Arena  
2 according to Mr. Bursch, within "walkability" of the Township  
3 Nine Property. And that too undercuts Mr. Bursch's testimony  
4 that the difference in the quality and number of amenities  
5 between the Township Nine Property and the Downtown and Midtown  
6 areas warrants a total exclusion of Downtown and Midtown  
7 comparables rather than discounting comparables from those areas  
8 in the valuation analysis.

9 Three additional factors also weigh heavily against the  
10 reliability and credibility of the BRI Appraisal.

11 First, for a number of years Copia and/or its agent  
12 represented to its investor values of the Township Nine Property  
13 nearly identical to values established by AGI's prior appraisals  
14 of the property. In fact, at least three of those represented  
15 values were established by AGI appraisals that Copia directed and  
16 requested. Placed in that context, the purpose of the BRI  
17 Appraisal is suspect. Copia only became an advocate for  
18 appraisals that reduce the value of the Township Nine Property by  
19 nearly two-thirds, and then by over one-half, after the Debtors  
20 filed their chapter 11 petitions and moved to approve the DIP  
21 Loan that requires a lien senior to its deed of trust.  
22 Otherwise, Copia and/or its agent were more than willing to  
23 accept substantially higher values and to continually represent  
24 those substantially higher values to its investor without  
25 questioning or criticizing AGI's concluded values or the  
26 assumptions and methodologies that AGI used to establish the  
27 concluded values.

28 Second, and along the same lines, in its quarter ended March

1 30, 2017, Copia and/or its agent represented to its investor that  
2 the Township Nine Property was worth upwards of \$78,000,000.00.  
3 About two months later, at the end of May of 2017, Copia obtained  
4 the first BRI appraisal that purported to value the Township Nine  
5 Property at nearly one-third that amount with fee credits, *i.e.*,  
6 \$27,100,000.00, and substantially less without fee credits, *i.e.*,  
7 \$12,810,000.00. Yet, for the quarter ended June 30, 2017, almost  
8 a month after it obtained that first appraisal from BRI in May of  
9 2017, Copia and/or its agent continued to represent to its  
10 investor that the value of Township Nine Property remained at  
11 upwards of \$78,000,000.00 without any mention of the (first) May  
12 2017 BRI appraisal.<sup>4</sup> One conclusion easily drawn from that  
13 course of conduct, and the apparent concealment of material  
14 information from its investor, is that Copia and/or its agent did  
15 not view the first BRI appraisal as a reliable valuation of the  
16 Township Nine Property. And if that's the case, why then should  
17 the court view the (second) BRI Appraisal as a reliable valuation  
18 of the Township Nine Property when the (second) BRI Appraisal is  
19 merely an "update" of the first May 2017 appraisal.

20 Third, there is a substantial variance in land values  
21 between the first and second BRI appraisals. The first BRI  
22 appraisal values the Township Nine Property land, without fee  
23 credits and as of December 31, 2016, at \$12,810,000.00. The  
24 second BRI Appraisal values the Township Nine Property land,  
25

26 <sup>4</sup>Notably, the June 30, 2017, quarter end representation of  
27 value is consistent with the value established by AGI's March  
28 2016 appraisal which, in turn, is consistent with the December  
31, 2015, appraisal that AGI prepared at the request of Copia  
and/or its agent.

1 without fee credits and as of September 15, 2017, at  
2 \$33,350,000.00. That is an increase in dollars of  
3 \$20,540,000.00. And according to the court's math, that  
4 translates to a 160.3435% increase in land value over a nine  
5 month period. That increase is not realistic. Nor is it  
6 consistent with the BRI Appraisal which reflects that between  
7 December 2016 and September 2017 the Sacramento market  
8 experienced a monthly appreciation of between 5% and 6%.  
9 Assuming that Mr. Bursch's market appreciation analysis is  
10 correct, at best, one would realistically expect a corresponding  
11 increase in the land value of the Township Nine Property between  
12 the first and second BRI appraisals of between 45% and 54% - not  
13 160%.<sup>5</sup> In that regard, not only is the BRI Appraisal unreliable,  
14 but, it is unrealistic and therefore not credible.

15 The AGI Appraisal, in contrast, relies on Downtown and  
16 Midtown comparables. And although it discounts those Downtown  
17 and Midtown comparables, based on the court's conclusion that the  
18 Township Nine Property is in (and within) the Downtown and  
19 Midtown market areas, the court reiterates that it is more  
20 reliable to value the Township Nine Property by using, and then  
21 discounting, Downtown and Midtown comparables rather excluding  
22 comparables from those markets altogether. This approach is  
23 consistent with and supported by Mr. Wehrli's expert testimony  
24 and report and it is precisely what the AGI Appraisal does, *i.e.*,  
25 it discounts Downtown and Midtown comparables used to value the

26

27 <sup>5</sup>Even the highest percentage of appreciation noted during  
28 the time period is 95% which is still far below the 160% increase  
in land value between the first and second BRI appraisals.

1 Township Nine Property.<sup>6</sup>

2 Finally, a word about the Anthem sale. Copia's argument  
3 regarding the Anthem sale and its effect on the AGI appraisal is  
4 somewhat inconsistent. Mr. Bursch testified that the Anthem sale  
5 is a retail sale and the AGI Appraisal value is a bulk sale value  
6 which means one does not compare to the other. That differs  
7 substantially from the argument Copia makes in its supplemental  
8 opposition where it states as follows:

9 The Anthem PSA is clearly a strong indicator of the  
10 value for the [Township Nine] Property. It is a sale  
11 of a portion of the [Township Nine] Property. It is  
12 recent, having been executed in July, 2017. Both  
13 Anthem and Debtors are knowledgeable market  
participants. The Anthem sale is a result of arm's  
length negotiation. Debtors have represented to the  
bankruptcy court that [the] Anthem PSA is a market  
transaction.

14 Dkt. 225 at 7:27-8:3. Copia cannot have it both ways. And  
15 although this may be a case of Copia's witness not supporting  
16 Copia's argument, the argument that the Anthem sale is a relevant  
17 indicator of value is nevertheless made. Therefore, the court  
18 will address it.

19 Anthem is purchasing 11.27 net developable acres for  
20 \$17,677,000.00 and assuming \$4,398,420.00 in infrastructure  
21 development costs for a total effective purchase price (not  
22

23 <sup>6</sup>There is no evidence to suggest that the discount applied  
24 in the AGI Appraisal is illogical or unreasonable. Copia does  
25 suggest in its supplemental opposition that some of the Township  
26 Nine Property parcels were not discounted. Copia notes that the  
27 AGI Appraisal values Areas I & IV at an adjusted retail value of  
28 \$120.00 per square foot which it also notes is the same square  
foot price for comparable C-3 Downtown parcels. That is  
incomplete. Comparable C-3 Downtown parcels are valued at a  
range of between \$120.00 and \$135.00 per square foot. The  
\$120.00 adjusted retail valuation is at the lower end of that  
range and is subject to further discounts overlooked by Copia.

1 including fee credits) of \$22,075,420.00. The 11.27 net  
2 developable acres is 490,921 square feet which means, at least  
3 according to Mr. Bursch's testimony, the Anthem sale factors out  
4 to \$45.00 per square foot.

5 The total square footage of the Township Nine Property  
6 considered is 1,377,367 square feet. That means: (i) at the  
7 \$71,350,000.00 adjusted retail land value concluded in the AGI  
8 Appraisal the square foot price is approximately \$51.80;<sup>7</sup> (ii) at  
9 the \$61,431,500.00 land value (exclusive of fee credits and  
10 inclusive of estimated costs to complete infrastructure)  
11 concluded in the AGI Appraisal the square foot price is  
12 approximately \$44.60; and (iii) at the court's adjusted land  
13 value of \$59,114,105.00 (exclusive of fee credits and inclusive  
14 of adjusted costs to complete infrastructure) the square foot  
15 price is approximately \$42.92.<sup>8</sup> In contrast, the concluded land  
16 value (exclusive of fee credits) in the BRI Appraisal is  
17 \$33,350,000.00 which is approximately \$24.21 per square foot.

18 The point is, if, as Copia asserts, the Anthem sale is a  
19 market sale and as a market sale it is indicative of the value of  
20 the Township Nine Property, see Tyner v. Nicholson (In re  
21 Nicholson), 435 B.R. 622, 634 (9th Cir. BAP 2010), *abrogation on*  
22

23 <sup>7</sup>Copia maintains in its supplemental opposition that AGI  
24 Appraisal uses an \$88.00 per square foot adjusted value which  
25 results in an overvaluation of the land. The \$88.00 per square  
26 foot is an adjusted weighted average that is further discounted  
27 and adjusted down to to \$51.80 per square foot. Copia fails to  
28 account for the additional adjustments.

29 <sup>8</sup>Of course, these are averages of entire property and there  
30 are some parcels that are more valuable than others. The parcels  
31 that Anthem is purchasing are not as valuable as some of the  
32 other Township Nine Parcels.

1 other grounds noted, Ramirez v. Nationstar Mortgage, LLC, 2016 WL  
2 7189831 (9th Cir. BAP 2016), then it supports the land value  
3 established by the AGI Appraisal and further undercuts the BRI  
4 Appraisal's land value. In other words, if anything, as to the  
5 AGI Appraisal, the Anthem sale reinforces its reliability, and as  
6 to the BRI Appraisal, the Anthem sale undercuts its reliability.

7 In sum, the court finds and concludes that the Township Nine  
8 Property is in (and within) the Downtown and Midtown market areas  
9 and within the same area of competitive supply as those areas.  
10 That means Downtown and Midtown comparables are relevant, if not  
11 critical, to a reliable valuation of the Township Nine Property.  
12 That also means the wholesale exclusion of Downtown and Midtown  
13 comparables renders the BRI Appraisal, together with its  
14 concluded value and valuation analysis, unreliable.

15 The BRI Appraisal is also unreliable and not credible  
16 because it includes assumptions that are either unfounded or  
17 unsupported when tested against Mr. Bursch's cross-examination  
18 testimony. That includes its fee credit analysis discussed,  
19 infra.

20 And the purpose of the BRI Appraisal is also suspect when  
21 considered in the context of these chapter 11 proceedings,  
22 particularly, when Copia and/or its agent directed, requested,  
23 accepted, and relied upon a number of prior AGI appraisals as the  
24 source for representations to an investor without questioning or  
25 criticizing the methodology, assumptions, and value conclusions  
26 in those earlier AGI appraisals.

27 Therefore, for all the foregoing reasons, the court rejects  
28 the BRI Appraisal and gives it no weight in its valuation

1 analysis. Instead, the court adopts and relies on the AGI  
2 Appraisal as a reliable and credible valuation of the Township  
3 Nine Property, subject to the adjustments noted below.

4 C. Fee Credits

5 Now on to fee credits. In order to build on a parcel of  
6 land a developer must obtain building permits. The City of  
7 Sacramento requires builders to pay various fees in order to  
8 obtain building permits. Fee credits reduce or eliminate fees  
9 that a builder has to pay to acquire building permits. Fee  
10 credits are an additional asset that can be sold with and enhance  
11 the value of the land.

12 The BRI Appraisal discounts the fee credits available to the  
13 Township Nine Property and values those fee credits at a  
14 discounted value of \$13,190,000.00. The AGI Appraisal, on the  
15 other hand, values the Township Nine Property fee credits at face  
16 value in the amount of \$16,512.769.00. Based on the evidence  
17 presented, the court finds and concludes that valuation of the  
18 fee credits associated with the Township Nine Property at face  
19 value is more reliable.

20 Mr. Bursch testified that fee credits should be discounted  
21 because in his opinion a developer would not pay 100% of the face  
22 value of fee credits that are not used when purchased but,  
23 instead, are used for development at some future point. The  
24 court gives no weight to that opinion for at least three reasons.

25 First, Mr. Bursch testified that his discounted fee credit  
26 analysis is based on telephone conversations with "market  
27 participants." However, Mr. Bursch also testified that the  
28 "market participants" with whom he had those telephone

1 conversations had no experience with fee credits and, in fact,  
2 never dealt with fee credits associated with any development.

3 Second, Mr. Bursch considered only fee credit decreases. He  
4 acknowledged that over time the value of fee credits may actually  
5 increase. And he also testified that he did not consider that  
6 potential for increase in his discount analysis.

7 Third, discounting fee credits conflicts with historical and  
8 real-world market data unique to the Township Nine Property. Fee  
9 credits associated with the Township Nine Property have now been  
10 sold twice in the recent past. They were sold for the  
11 construction associated with the Cannery Place apartment and they  
12 were sold with the Anthem sale. In both instances, the  
13 respective buyers paid, or have agreed to pay, face value for fee  
14 credits. That is significant with regard to the Anthem sale. It  
15 closes in phases, yet, Anthem is paying full face value for fee  
16 credits it will use sometime in the future.

17 Therefore, for the foregoing reasons and consistent with the  
18 AGI Appraisal, the court values fee credits associated with the  
19 Township Nine Property at \$16,512,769.00.

20 D. Cost to Complete Infrastructure

21 Costs of completion must be factored into valuation. The  
22 parties stipulated to a gross cost to complete infrastructure of  
23 \$15,635,895.00. There are \$3,400,000.00 in grants available to  
24 offset those costs. There is a dispute over whether  
25 \$1,625,000.00 attributable to what is referred to as "Sump 111"  
26 should be treated as a grant or fee credit, or whether it should  
27 be included in or subtracted from the costs of completion. There  
28 is also a dispute over whether the infrastructure completion

1 costs of over \$4,000,000.00 that Anthem has agreed to assume in  
2 its purchase of Township Nine Property parcels should likewise be  
3 included or deducted.

4 The "Sump 111" cost was not included as a fee credit in the  
5 AGI Appraisal so it will not be included here. The court also  
6 will not deduct from the stipulated gross costs to complete the  
7 infrastructure completion costs being assumed by Anthem. The  
8 Anthem sale has not closed and the infrastructure completion  
9 costs associated with that sale have not yet been assumed which  
10 means that, as of October 2, 2017, those costs remained the  
11 Debtors' obligation.

12 Therefore, the court finds and concludes that the net cost  
13 of completion is the stipulated \$15,635,895.00 less the  
14 \$3,400,000.00 existing grants which results in a net cost of  
15 completion of infrastructure of \$12,235,895.00.

16 E. Determination of Value

17 Having rejected the BRI Appraisal as unreliable and not  
18 credible, and having adopted the AGI Appraisal subject to the  
19 infrastructure completion cost adjustment, the court values the  
20 Township Nine Property as follows:

21 (i) the total "as is" market value, as of October 2,  
22 2017, with fee credits and less the adjusted net costs  
23 to complete the remaining infrastructure of  
24 \$12,235,895.00, is  $(\$71,350,000.00 - \$12,235,895.00 =)$   
\$59,114,105.00 plus \$16,512,769.00 (value of fee  
credits) which is \$75,626,874.00; and

25 (ii) the market value of the "as is" fee simple  
26 interest, exclusive of fee credits and reflecting the  
27 cost to complete the remaining infrastructure, as of  
28 October 2, 2017, is \$59,114,105.00.

1 II. Adequate Protection

2 Now to adequate protection. The Ninth Circuit has held that  
3 a 20% equity cushion provides adequate protection. Pistole v.  
4 Mellor (In re Mellor), 734 F.2d 1396, 1401 (9th Cir. 1984)  
5 (relief from stay context). In fact, case law almost uniformly  
6 holds that an equity cushion of at least 20% constitutes adequate  
7 protection. In re Holt, 2010 WL 3294693, \*6 (Bankr. D. Mont.  
8 2010) (citing cases); see also In re McKillips, 81 B.R. 454, 458  
9 (Bankr. N.D. Ill. 1987) (surveying the cases which show that an  
10 equity cushion of more than 20% is adequate but less than 11% is  
11 not). The 20% threshold is applied to the use of cash  
12 collateral. In re McClure, 2015 WL 1607365, \*6 (Bankr. C.D. Cal.  
13 2015). And importantly, 20% is also the threshold that is  
14 applied to partially developed land. See In re C.B.G. Ltd., 150  
15 B.R. 570, 573 (Bankr. M.D. Pa. 1992).

16 The court assumes for purposes of its analysis that Copia is  
17 owed the disputed amount of \$46,787,543.00. Other encumbrances  
18 on the Township Nine Property total approximately \$597,154.00.  
19 Factoring in the proposed \$10,000,000.00 DIP Loan, encumbrances  
20 against the Township Nine Property total approximately  
21 \$57,384,697.00. With a \$75,626,874.00 valuation, at a minimum,  
22 there remains unencumbered equity of \$18,242,177.00. That  
23 translates to an equity cushion of at least 24.12%.<sup>9</sup> Therefore,  
24 the court finds and concludes that Copia's interest in, and all  
25 other encumbrances on, the Township Nine Property are adequately

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26  
27 <sup>9</sup>That amount is based on the disputed amount of Copia's  
28 claim. Of course, to the extent the Debtors are able to reduce  
that claim amount the equity cushion increases.

1 protected.

2 III. Copia's Remaining Objections

3 A. DIP Loan Terms [Copia Obj. § III.B.]

4 Copia objects to the terms of the DIP Loan as "outrageous."  
5 The court disagrees.

6 Copia's objection centers primarily on the DIP Loan interest  
7 rate. Copia appears to complain that the effective interest rate  
8 of 14% (which includes points, 10% otherwise) is too high given  
9 an apparent lack of risk. Copia cites In re Tapang, 540 B.R.  
10 701, 707 (Bankr. N.D. Cal. 2015), apparently to suggest that the  
11 applicable interest rate of the DIP Loan should be no more than a  
12 5% cramdown rate.

13 Copia's reliance on Tapang is misplaced. The 5% cramdown  
14 rate in Tapang is a postconfirmation rate. The rate here is a  
15 postpetition, preconfirmation rate. There is a difference in  
16 that there is significantly more risk to a postpetition,  
17 preconfirmation lender than there is to a postconfirmation lender  
18 where risk is diminished by the stability of a confirmed plan.  
19 See In re MPM Silicones, LLC, 2014 WL 4436335, \*27 (Bankr.  
20 S.D.N.Y. 2014) (citing 7 COLLIER ON BANKRUPTCY, ¶ 1129.05[c][i]  
21 (16th ed. 2014) ("[I]nstead of the interim and inherently more  
22 uncertain risk present in debtor-in-possession financing, the  
23 court, at confirmation, is presented with a less risky, more  
24 stable and restructured debtor."), aff'd, 531 B.R. 321 (S.D.N.Y.  
25 2015), aff'd in part, rev'd in part, and remanded, 874 F.3d 787  
26 (2d Cir. 2017). That additional preconfirmation risk justifies a  
27 somewhat higher interest rate for postpetition, preconfirmation  
28 financing. See Id. ("[L]oans imposed at confirmation resemble

1 more traditional exit or long-term financing than interim  
2 debtor-in-possession financing.”).

3 Copia states the effective interest rate on the DIP Loan is  
4 14%, the Debtors state it is 10%. In either case, the DIP Loan  
5 interest rate is below Copia’s current 16% default rate. And  
6 although perhaps somewhat significant, the interest rate offered  
7 by Serene is not outrageous. See generally ABI Commission  
8 Report: Proposed Amendments and Their Impact on Valuation, 031416  
9 ABI-CLE 163 at n.56 (noting Lyondell Chemical Co.’s \$8 billion  
10 postpetition DIP financing facility which came with a 13%  
11 interest rate and a 7% fee). Moreover, as the bankruptcy  
12 appellate panel stated in Official Committee of Unsecured  
13 Creditors v. Bank of America (In re Fleetwood Enters., Inc.), 471  
14 B.R. 319 (9th Cir. BAP 2012): “In any extension of debt  
15 financing under § 364, . . . [o]ften the debtor in possession  
16 will be able to obtain only onerous terms, which the bankruptcy  
17 court must balance against the debtor in possession’s apparent  
18 lack of alternatives.” Id., 2012 WL 2017952 at \*11 (citing 3  
19 COLLIER ON BANKRUPTCY ¶ 364.04[2][d] (Alan N. Resnick & Henry J.  
20 Sommer, eds., 16th ed. 2011)).

21 Here, there are no better alternatives for the Debtors. The  
22 Debtors made diligent and good faith efforts to obtain  
23 postpetition financing on the best terms possible. The Debtors  
24 presented evidence at the initial August 29, 2017, hearing that  
25 they discussed postpetition debtor in possession financing with  
26 numerous other potential lenders. The Unsecured Creditors  
27 Committee also assisted in a search for other potential lenders.  
28 And while other potential lenders offered the Debtors interest

1 rates between 14% and 18%, their repayment terms and fees were  
2 less favorable than the terms and fees offered by Serene. The  
3 point is, when balanced against favorable terms, the DIP Loan  
4 interest rate does not render the terms of the DIP Loan  
5 "outrageous" as Copia contends. Therefore, Copia's objection to  
6 the DIP Loan on this basis is overruled.

7 B. Violation of the Bankruptcy Code's Priority Scheme.  
8 [Copia Obj. § III.D.]

9 Copia next objects to the Debtors' use of loan proceeds from  
10 the DIP Loan to pay administrative expenses, including attorney's  
11 fees, operating expenses, and claims. Copia contends that  
12 proposed use of loan proceeds from the DIP Loan violates the  
13 Bankruptcy Code's priority scheme because the DIP Loan is  
14 effectively a disposition of its collateral which means it must  
15 be paid before any administrative expenses and, further,  
16 administrative expenses may only be paid from the proceeds of its  
17 collateral if the requirements of § 506(c) are met. The court  
18 disagrees.

19 In In re Olde Praire Block Owner, LLC, 448 B.R. 482 (Bankr.  
20 N.D. Ill. 2011), the court concluded that even if a priming lien  
21 granted to secure postpetition financing was tantamount to the  
22 disposition of an existing secured creditor's collateral thereby  
23 making the loan proceeds cash collateral those loan proceeds  
24 could nevertheless be used to pay administrative expenses because  
25 the secured creditor was adequately protected by a substantial  
26 equity cushion. Id. at 496-97. Stated another way, the court  
27 recognized that § 506(c) is inapplicable to proceeds of financing  
28 obtained from unencumbered equity under § 364(d) even if the loan

1 proceeds are or are tantamount to cash collateral under § 363 so  
2 long as there is adequate protection. In that regard, Olde  
3 Praire is consistent Sec. Leasing Partners, LP v. ProAlert, LLC  
4 (In re ProAlert, LLC), 314 B.R. 436 (9th Cir. BAP 2004), which  
5 the court finds instructive and persuasive.

6 In ProAlert, the BAP considered whether a bankruptcy court  
7 may allow the use of cash collateral pursuant to § 363 without  
8 considering whether the requirements for a § 506(c) surcharge  
9 were met. The debtor moved to use cash collateral to pay  
10 operating expenses, attorney fees, a valuation expert, and an  
11 accountant. The secured creditor consented to the use of cash  
12 collateral to pay the operating expenses but not for professional  
13 fees, and argued that the debtor was seeking to use a cash  
14 collateral motion brought under § 363 to effectuate a surcharge  
15 under § 506(c). In its order approving the use of cash  
16 collateral, the bankruptcy court wrote that "[a]nalytically, if  
17 the creditor's interest is adequately protected, then, by  
18 definition, there is no surcharge and section 506(c) does not  
19 come into play." Id. at 439. The BAP affirmed, holding that  
20 even if the requirements of § 506(c) are not met, a debtor may  
21 nevertheless use the cash collateral for administrative expenses  
22 so long as a secured creditor whose cash collateral is being used  
23 is adequately protected. Id. at 444-45; see also In re Gen. Auto  
24 Bldg., LLC, 2012 WL 6737741, at \*2 (Bankr. D. Or. 2012) ("Debtor  
25 seeks to pay its appraiser from [the lender's] cash collateral,  
26 which is governed by § 363, not § 506(c). Section 363 requires  
27 adequate protection, not benefit to the creditor.") (internal  
28 citation omitted).

1 Like Old Praire, here, the Debtors seek to use the  
2 unencumbered equity in the Township Nine Property as collateral  
3 for the DIP Loan. Even if that makes the DIP Loan tantamount to  
4 a disposition of Copia's collateral, and the loan proceeds cash  
5 collateral as Copia has argued and as the court opined during the  
6 August 29, 2017 hearing, existing encumbrances on the Township  
7 Nine Property, Copia's included, are adequately protected.  
8 Consistent with ProAlert, that means loan proceeds from the DIP  
9 Loan may be used to pay ongoing expenses in the administration of  
10 the estate without regard to § 506(c). The use of proceeds from  
11 the DIP Loan in that manner does not violate the Bankruptcy  
12 Code's priority scheme. Therefore, Copia's objection to the  
13 Debtors' motion on these grounds is overruled.

14 C. Proposed Budget is Woefully Deficient [III.E.]

15 Copia's objection to the Debtors' proposed budget focuses on  
16 the absence of any explanation of the development costs and the  
17 Debtors' budget allocation for the payment of attorney's fees.  
18 The latter is addressed above and the former is resolved by the  
19 parties' stipulation regarding the costs of completion admitted  
20 into evidence for purposes of the December 11, 2017, evidentiary  
21 hearing. Therefore, this objection to is overruled.

22 IV. § 364(c) & § 364(d) Requirements

23 As explained above, the court is persuaded that the Debtors  
24 diligently attempted and were unable to obtain credit or secure a  
25 loan, unsecured or otherwise, and they could not do so in the  
26 absence of the Serene DIP Loan. And as is also explained above,  
27 all interests in the Township Nine Property, Copia's included,  
28 are adequately protected. Therefore, the court finds and

1 concludes that the statutory requirements of § 364(c) and §  
2 364(d) are satisfied.

3 V. § 364(e) Requirements

4 The terms of DIP Loan are at least as favorable to the  
5 Debtors as those available from alternative sources the Debtors  
6 diligently pursued. The DIP Loan was negotiated in good faith  
7 and is an arm's length transaction between a sophisticated  
8 lender, on the one hand, and a significant market participant and  
9 real estate developer, on the other hand. The Debtors' selection  
10 of Serene as its postpetition lender for the DIP Loan reflects  
11 the Debtors' valid and legitimate exercise of prudent business  
12 judgment consistent with their fiduciary duties, the loan terms  
13 are fair and reasonable under the circumstances, and the loan and  
14 its terms are enforceable in accordance with applicable law. The  
15 credit extended to the Debtors by Serene under the terms of the  
16 DIP Loan shall therefore be deemed to have been extended in good  
17 faith as that term is used in § 364(e) and Serene, and its  
18 assigns, shall have protections of Bankruptcy Code § 364(e).

19

20 CONCLUSION

21 Therefore, based on the foregoing and for all the foregoing  
22 reasons;

23 IT IS ORDERED that the Motion to Approve Postpetition  
24 Financing, Grant Priming Lien, and Related Relief filed on August  
25 1, 2017, at dkt. 59, is, on a final basis, **GRANTED**.

26 IT IS FURTHER ORDERED that the Debtors are authorized to  
27 borrow up to an aggregate of \$10,000,000.00, on the terms set  
28 forth in the DIP Credit Agreement.

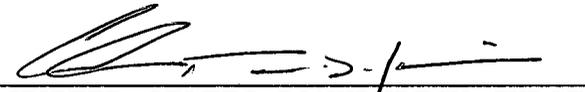
1 IT IS FURTHER ORDERED that the Debtors are authorized to  
2 make the expenditures of funds consistent with this memorandum  
3 and order and the motion.

4 IT IS FURTHER ORDERED that Serene and/or its assigns shall  
5 have and are hereby granted a super-priority administrative claim  
6 under 11 U.S.C. §§ 507(b) and 364(c)(1) and a senior and first-  
7 priority priming lien under 11 U.S.C. § 364(d) on the Debtors'  
8 real and personal property assets (subject the defined Carve-Out)  
9 generally and, in particular, on the Township Nine Property.

10 IT IS FURTHER ORDERED that Serene, and its assigns, shall be  
11 and hereby are entitled to the protections of 11 U.S.C. § 364(e).

12 IT IS FURTHER ORDERED that the continued hearing set for  
13 January 9, 2018, at 2:00 p.m. is **VACATED**. The matter is removed  
14 from calendar and no appearances are necessary.

15 Dated: January 8, 2018.

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19 UNITED STATES BANKRUPTCY JUDGE  
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