THREE EASY PIECES:

Lesser Known 2005 Bankruptcy Amendments Affecting Real Property[*]

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Single Asset Real Estate Cases – The Ceiling Has Come Off

In 1994, Congress dealt with single asset real estate cases by giving mortgagees an additional ground for relief from the automatic stay, section 362(d)(3). To avoid a mortgagee's getting stay relief for the asking 90 days after the order for relief, the so-called "single asset real estate" debtor defined in section 101(51B), had to have either filed a plan of reorganization that had a "reasonable probability of being confirmed within a reasonable period of time," or commenced monthly interest payments on the value of the mortgagee's interest. These interest payments were computed at a "fair market rate." It was not clear whether the rents could be used to make the payments.

The principal change is in the definition of "single asset real estate" in section 101(51B), and it is that the debt limit has come off. It used to be that a property with mortgages exceeding $4 million was not considered single asset real estate. Thus, some of the more famous properties, whose owners attempted to push the limits on new value plans, *see Bank of America National Trust & Savings Association v. 203 N. LaSalle Limited Partnership*, 526 U.S. 434 (1999), were exempt from this "plan or pay" requirement. Now, that is no longer the case. There is now also a specific exemption for exemption for family farmers. The basic test for determining whether there is single asset real estate is whether the real property in question consists of a single property or project (other than residential property with fewer than four residential units) which generates substantially all of the gross income of the debtor, and on which no substantial business is conducted by the debtor other than operating the real property. Therefore, irrespective of size, the likely candidates are still residential and commercial buildings. Hotels are exempt, because of the additional income-generating services provided. Motels (without these services) are also likely candidates for single asset real estate status.

On the "pay" option of the "plan or pay" requirement in section 363(d)(3), there are two changes of note. First, the interest rate is now the "applicable nondefault contract rate." This replaces the "fair market rate," and removes litigation over the determination of the rate based on market factors. Contract interpretation issues, if there is more than one nondefault contract rate, may still persist. Second, the statute now expressly states that cash collateral in the form of

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"rents or other income generated . . . by or from the property" may be used to pay this debt service.

In addition, if there is a dispute whether the debtor is subject to the single asset real estate rules, the "plan or pay" requirement in section 362(d)(3) now becomes operative on the later of 90 days after the order for relief or 30 days after the court determines that the single asset real estate rules apply.

The changes described above were all recommended by the National Bankruptcy Review Commission in 1997 (recommendations 2.6.1 and 2.6.2).

Individual Serial Filers and the Vanishing Automatic Stay

Several provisions of the 2005 Amendments address the problem of the abuse created by serial filings and the automatic stay. The problem for mortgagees of real property is especially acute, if the debtor is the subject of a new filing just after the mortgagee has succeeded in getting the old case dismissed, or getting relief from the stay. Besides new section 362(d)(4), which allows for relief from the stay against real property if the petition was "part of a scheme to delay, hinder and defraud" and permits the bankruptcy court to enter an in rem order with respect to the real property, which will be valid for two years, and enforceable in subsequent bankruptcies within the period by an exception to the automatic stay in new section 362(b)(20); there are two new provisions governing serial filings by individuals. (The fraudulent serial filer provisions apply to all kinds of debtors.) These new provisions are placed in section 362(c), which deals with the automatic termination of the automatic stay.

New section 362(c)(3) automatically terminates the automatic stay 30 days after the filing of the case, if the individual debtor has been a debtor in a dismissed case within the prior year, other than a chapter 7 case dismissed under section 707(b), for failing the "means test" or constituting some other abuse of chapter 7, and refiled under another chapter. New section 362(c)(4) provides that the automatic stay never takes effect, if the individual debtor has been a debtor in two or more dismissed cases within the prior year, other than "a case refiled under section 707(b)" [sic]. It should be noted that in each instance, the prior cases must have been dismissed. Thus, except as noted below, these provisions do not deal with problems arising from simultaneous cases.

Despite the automatic termination in section 362(c)(3) and the never-take-effect provision in section 362(c)(4), an application can be made to continue or impose the stay, and the court may grant such application, if at a hearing completed within the 30-day period after the filing, it is demonstrated that the new case is filed in good faith as to the creditors who are to be stayed. There is a rebuttable presumption of bad faith, if there has been: (I) more than one case concerning the debtor within the year; (II) the dismissal of the prior case was based on the debtor's failure to comply with an order directing the amendment of the petition or some other document, to provide adequate protection, or to perform under a confirmed plan; or (III) there has not been a substantial change in the financial personal affairs of the debtor and there is no

reason to conclude that the debtor will either be granted a chapter 7 discharge or confirm a chapter 11 or 13 plan. There is also a rebuttable presumption of bad faith assertable by any creditor who had made a lift-stay motion in a prior case and that motion either was still pending or resulted in relief for the creditor. Rebutting the presumption requires clear and convincing evidence.

New section 362(i) countermands the presumption of bad faith in section 363(c)(3) (only one other filing for the debtor within the year), but not section 363(c)(4) (more than one other filing within the year), if the earlier dismissal was due to the creation of a debt repayment plan.

New section 362(j) provides that, on request of a party in interest, the court shall issue an order declaring that the automatic stay has been terminated or never took effect.

Real Property Tax Liens
Ad Valorem or Not Ad Valorem? That Is the Question

In 1994 by adding section 362(b)(18), Congress legislatively overruled a decision that prevented real property tax liens from attaching post-petition because of the automatic stay. This provision, however, only covered ad valorem taxes. An amendment to section 362(d)(18) now extends the coverage to statutory liens for "a special tax or special assessment on real property whether or not ad valorem."

Nevertheless, ad valorem tax liens continue to occupy a special place in the Bankruptcy Code. Section 724(b), which automatically subordinates tax liens to priority claims in chapter 7 cases, now has an exception for those liens that are ad valorem, whether on real or personal property. Section 506(c), which allows the trustee to recover from a secured creditor's collateral that reasonable and necessary costs of preserving or disposing of such collateral, now expressly includes "the payment of all ad valorem taxes."

Taxes incurred by the estate, "whether secured or unsecured, including property taxes, for which liability is in rem, in personam or both" are now expressly made administrative expenses, by an amendment to section 503(b)(1)(B)(i). Moreover, governmental units are not required to file requests for the payment of administrative expenses for such taxes, or for any fines, penalties or reductions in credit relating to such taxes, as a condition of their allowance, under new section 503(b)(1)(D).

Despite the additional protection for such tax liens and expenses, the foundations of which are in the recommendations of the National Bankruptcy Review Commission, nothing has been done to section 502(b)(3), which disallows a claim to the extent that it is "a tax claim assessed against property of the estate . . . [and] such claim exceeds the value of the interest of the estate in such property"; or to 506(d), which voids liens that secure "a claim against the debtor that is not an allowed secured claim." It is therefore still the case that such taxes cannot exceed the value of the property.