In the United States Bankruptcy Court

for the Northern District of Iowa

DONALD L. CHRISTENSEN, JUDY A. CHRISTENSEN	Bankruptcy No. X88-00395M
Debtors.	Contested No. 80206
CHRISTENSEN PUBLIC TRANSIT CO.	Bankruptcy No. X88-00580M
Debtor.	Contested No. 68086

ORDER RE: MOTIONS FOR MODIFICATION OF AUTOMATIC STAY FILED BY LIBERTY BANK & TRUST

The matters before the court are motions for modification of the automatic stays which were filed in these two Chapter 11 cases by Liberty Bank & Trust. Trial was held on May 11, 1988 on both contested matter proceedings. The matters were submitted for the consideration of the undersigned judge. The court now states the following findings of fact and conclusions pursuant to Bankr. R. 7052. This is a core proceeding under 28 U.S.C. 157(b)(2)(G).

FINDINGS OF FACT

1. Donald L. Christensen and Judy A. Christensen (Christensens), husband and wife, filed their joint voluntary petition under Chapter 11 of the Code on March 10, 1988. Christensen Public Transit Co. (COMPANY) filed its voluntary petition under Chapter 11 of the Code on April 12, 1988.

2. Christensens own all common stock in Company.

3. On March 25, 1988, Liberty Bank & Trust f/k/a Hawkeye Bank & Trust of Mason City and f/k/a American State Bank (LIBERTY) filed its motion for modification of the automatic stay in the Christensen case (Contested No. 80206).

4. Preliminary hearing on the motion was held by telephone on April 18, 1988. Final hearing was ordered to be consolidated with a final hearing on a similar motion for relief to be filed in the Company case. The motion for relief filed by Liberty in the Company chapter 11 case was filed April 21, 1988 (Contested No. 68086).

5. Liberty has sought modifications of the stays to permit it to execute on a judgment and decree of foreclosure which it obtained on December 23, 1986 against the Christensens as well as Company and their properties. The properties upon which Liberty desires to execute are parcels of real estate and motor vehicles which are owned and/or used by these debtors.

6. At the close of the hearing, the court granted relief to Liberty as requested on all property save one parcel of real estate identified by its common name of 640 South 19th Street, Mason City, Iowa. (No matching legal description was pointed out to the court.)

7. As of the dates of bankruptcies and as of the date of the hearing, the value of all personal and real property secured or mortgaged to Liberty by debtors, was less than the amount of debt intended to be secured.

8. Christensens own 640 South 19th Street, Mason City, Iowa (GARAGE), but it is used by Company for the storage and maintenance of buses and vans operated by Company.

9. There is no evidence that rent is or has been paid by Company to Christensens.

10. A portion of the Garage building is rented out to a third party for $30.00 per month.

11. Real estate taxes on the property are not current and are due and delinquent in a sum in excess of $7,800. There is currently a casualty insurance policy in force as to Garage because Liberty voluntarily paid a premium in December of 1987 in the sum of $700.

12. The Garage has a fair rental value of $900 per month, net of taxes and insurance costs.

13. A judgment and decree in favor of Liberty and against debtors was entered on December 23, 1986. Sometime prior to the entry of that judgment and perhaps in its petition initiating the state court proceeding, Liberty requested the appointment of a receiver. The appointment was denied. In its judgment and decree, the state court retained jurisdiction of the receivership question.

14. Debtors agreed at trial that if adequate protection of movant's interest in the real property or its rents and profits is required, it would pay the fair rental value of such property to the movant.

DISCUSSION

I.

Liberty seeks modification of the automatic stays in order to obtain special execution on its state court judgment. Liberty's actions in state court would also include a further request for a receiver to be appointed to collect rents and profits from Garage during the pendency of the foreclosure.

Liberty seeks the modifications of the stays on two grounds: (1) Liberty argues that there is no equity in the Garage and that it is not necessary to an effective reorganization and (2) Liberty says that it is entitled to adequate protection of its property interest, specifically its right to collect the rents and profits arising from the mortgaged premises, and absent such protection, it is entitled to a termination of the stay.

Liberty stated at the final hearing on the motions for relief that it seeks adequate protection only prospectively as to rents and profits. The court understands this to mean from the dates of the filings of its motions.

Debtors resist, arguing that the interest of Liberty in rents and profits from the real estate is not the type of property interest entitled to adequate protection under United Savings Association of Texas v. Timbers of Inwood Forest Associates, Ltd., 56 U.S.L.W. 4107, 108 S.Ct. 626 (1988).

This court must look to state law to determine the nature of property rights which may be entitled to adequate protection under 11 U.S.C. 362(d)(1). Butner v. United States, 440 U.S. 48, 52-54 (1979).

Liberty claims that its right to subject the rents and profits from Garage to the administration of a receiver for its benefit is a right entitled to adequate protection under 11 U.S.C. 362. Liberty says that interest is separate and distinct from its lien against the real estate. If that adequate protection is lacking, it says, the stay should be modified to permit continuance of foreclosure proceedings, including the appointment of a receiver.

The position of Liberty as to the property right is in accordance with Iowa law:

> The right of a foreclosing mortgagee to subject the rents and profits from the real estate under a receivership clause in the mortgage to the payment of his debt is separate and distinct from his lien on the land itself.

Ball v. Williams, 250 Iowa 216, 93 N.W.2d 723, 728 (1958).

There is no argument by Liberty that its mortgage contained a primary grant of security in the rents and profits arising from the mortgage premises.

Liberty requested the appointment of a receiver in the state court proceeding, but as of December 23, 1986 the state court had denied the request. A mortgagee such as Liberty has no lien upon rents and profits arising from mortgaged property under a clause which pledges those rents and profits as security until it has initiated an action to foreclose the mortgage and has requested the appointment of a receiver. Kooistra v. Gibford, 201 Iowa 275, 207 N.W. 399, 399-400 (1926).

The commencement of such an action and the request for the appointment of a receiver fixes the time for determining questions of priority between the mortgagee and third parties which may claim a right to the rents and profits. Id. at 400.

A later motion for a receiver in state court would also establish a "perfection" date relative to the settling of priorities.

Liberty was, therefore, perfected in the rents and profits arising from the mortgage premises sometime prior to December 23, 1986, but subject to there being no receiver appointed during the proceedings.

As of the date of the filing of the bankruptcy case, Liberty had a perfected security interest in any rents and profits arising from the mortgage property.

Bankruptcy Code 552 governs the post-petition effect of a security interest. Subsection (a) provides that property acquired by the estate or by the debtor after the commencement of the case is not subject to a lien resulting from a pre-petition security agreement. An exception to this provision of the Code is 552(b) which states in pertinent part:

> [I]f the debtor and an entity entered into a security agreement before the commencement of the case and if the security interest created by such security agreement extends to property of the debtor acquired before the commencement of the case and to proceeds, product, offspring, rents, or profits of such property, then such security interest extends to such proceeds, product, offspring, rents, or profits acquired by the estate after the commencement of the case to the extent provided by such security agreement and by

> applicable non-bankruptcy law, except to any extent that the court after notice and a hearing and based on the equities of the case, orders otherwise.

It does not matter that no receiver has yet been appointed in state court. This court is required to take "whatever steps are necessary to ensure that the mortgagee is afforded in Federal Bankruptcy Court the same protection he would have under state law if no bankruptcy had ensued." Butner v. United States, 440 U.S. 48, 56 (1979). This the court may do by ordering sequestration of the rents or profits arising from the mortgage premises, or by requiring adequate protection of debtors' right to subject the real property to a state court receivership.[(1)]

II.

The court, therefore, concludes that Liberty is entitled to adequate protection of its perfected security interest in rents and profits from the earlier date of the filing of its two motions for modification of the stay. Iowa Code 654.14 sets out the scheme in applying the rents or profits collected by a receiver in a real estate mortgage foreclosure proceeding.

The rents and profits derived from the real estate are applied in the following order:

(1) to the costs of the receivership;

(2) payment of taxes;

(3) insurance payments on the premises; and

(4) balance shall be paid as determined by the court.

This court order shall take this scheme into consideration.

III.

Liberty claims that there is no equity in the property for the estate and that the property is not necessary to an effective reorganization and therefore it has shown grounds for relief under 11 U.S.C. 362(d)(2).

It has been stipulated by the parties, that the debtors do not have equity in the real property.

It is the debtors' burden of proof to show that the property is necessary to an effective reorganization. 11 U.S.C. 362(g)(2).

This burden means that the debtor must show that the "property is essential for an effective reorganization that is in prospect." United Savings Association of Texas v. Timbers of Inwood Forest Associates, Ltd., 56 U.S.L.W. 4107, 108 S.Ct. 626 (1988).

Donald Christensen, the chief executive officer of the corporation, testified that the property was essential for the storage and maintenance of the Company's vans and buses. He further testified that he believed that the property was essential to an effective reorganization.

The evidence introduced by the debtor in support of debtors' assertion that property is necessary to an effective reorganization was slight.

However, the reorganization cases involved herein were filed by the Christensens on March 10, 1988 and by Company on April 12, 1988.

This court may allow, and does allow, a less detailed showing of the probabilities of a successful reorganization and the court finds that at this early stage of the proceeding, the debtors have met this burden. No adverse evidence was introduced by Liberty.

The court, therefore, finds that the property is necessary for an effective reorganization and that the movant should be denied relief as requested under 11 U.S.C. 362(d)(2).

CONCLUSIONS OF LAW

1. Real property commonly known as 640 South 19th Street, Mason City, Iowa is necessary to an effective reorganization of these debtors and therefore the movant should be denied relief under 11 U.S.C. 362(d)(2).

2. Liberty has a perfected security interest in the rents and profits from the premises commonly known as 640 South 19th Street, Mason City, Iowa, and this interest is entitled to adequate protection under 11 U.S.C. 361 or modification of the stay should be granted under 11 U.S.C. 362(d)(1).

ORDER

IT IS THEREFORE ORDERED that the automatic stay of 11 U.S.C. 362 as to debtors and estate's interests in the real property commonly known as 640 South 19th Street, Mason City, Iowa shall remain in effect provided that the debtors provide the following adequate protection to Liberty Bank & Trust:

1. Debtors shall pay all future insurance premiums to keep casualty insurance current on the subject property at the level at which the property was insured prior to the filing of the Chapter 11 petitions;

2. Debtors shall pay real estate taxes on the subject property which become due and owing after March 30, 1988. If the county treasurer will not accept partial payments, sums shall be placed in the account required under paragraph 3 until there is a sum in the account sufficient to pay required tax payments. Application to the court to disburse from the account for the purpose of paying taxes may be made at that time;

3. Debtors shall pay into a separate savings account at a bank depository approved for deposits by this court, the sum of $900.00 per month on the 25th day of each month effective March 25, 1988. Debtors may "catch up" the payments due March 25, April 25 and May 25 by paying two $900.00 payments on June 25, July 25 and August 25, 1988; and

4. The account shall be an interest-bearing account, and money shall not be removed from the account without further order of this court. The monies placed in the account shall remain there as adequate protection of Liberty's right to rents and profits from the mortgage premises pending the outcome of any future foreclosure proceedings, if any, permitted by this court; a confirmed plan of reorganization; or such other event warranting disbursement.

SO ORDERED ON THIS 6th DAY OF JUNE, 1988.

William L. Edmonds
Bankruptcy Judge

Filed Stamped June 6, 1988

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1. This court may not appoint a receiver, 11 U.S.C. 105(b), and generally state appointed receivers must yield possession of property in their possession upon the filing of bankruptcy by the mortgagor. 11 U.S.C. 543.