

**IN THE UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF ARKANSAS
LITTLE ROCK DIVISION**

IN RE: KAREN MAY

**4:02-bk-14785 E
CHAPTER 7**

**ORDER DENYING REGIONS BANK'S
MOTION FOR RELIEF FROM STAY**

Motions for Relief From Stay filed by Regions Bank (“**Regions**”) and First Arkansas Valley Bank, S.A. (“**FAVB**”) were heard on June 11, 2002, and the Court took the matters under advisement. The Chapter 7 Trustee, M. Randy Rice, Esq., appeared and opposed the motions. James V. Coutts, Esq. appeared for Regions. John R. Peel appeared for FAVB. The Debtor, Karen May, was also present.

The Trustee and FAVB subsequently settled FAVB’s motion and an agreed Order resolving FAVB’s motion was entered by this Court on July 2, 2002. This Order decides Regions’ motion for relief from stay. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(G), and the Court has jurisdiction to enter a final judgment in this matter.

FACTUAL BACKGROUND

The Debtor filed this chapter 7 bankruptcy on April 30, 2002. This matter concerns two parcels of real estate in Pope County owned by the Debtor, “**Ruth Lane**” and “**Lakeridge Estates**,” in which Regions asserts a security interest (collectively referred to as the “**Properties**”). Prior to Debtor’s bankruptcy filing, Regions initiated foreclosure suits on these Properties in the Circuit Court of Pope County, and seeks relief from stay to continue those actions.

Ruth Lane

Ruth Lane consists of approximately eight acres in Pope County. This property is also commonly referred to as “Maple Springs Road” according to its legal description. On March 9, 2001, Debtor borrowed \$50,099.50 from Regions and mortgaged Ruth Lane as collateral for the loan. Debtor borrowed the money individually and executed the mortgage as grantor. However, Debtor did not own Ruth Lane at the time she executed the mortgage. Debtor testified that at the time the mortgage was given, Ruth Lane was actually owned by her son, Bradley J. Shoptaw, and her daughter, Robyn S. Shoptaw. On March 28, 2002, Debtor’s son and daughter transferred Ruth Lane to their mother by quitclaim deed. Debtor testified that this transaction was intended to give Regions a valid first mortgage on Ruth Lane.

Debtor valued Ruth Lane at \$135,000.00 on her bankruptcy schedules. Mr. Blake Tarpley, vice president of Regions Bank in Russellville, testified that the Debtor owed approximately \$47,000.00 in principal and interest on the Ruth Lane loan. Regions’ acknowledged that Ruth Lane was worth approximately \$85,000.00 and that the parties had agreed there was equity in Ruth Lane.

Lakeridge Estates

Lakeridge Estates consists of one and a half lots in Pope County. Russellville Title & Closing, Inc. (“**Russellville Title**”) borrowed \$169,730.09 from Regions on May 19, 2000 and mortgaged Lakeridge Estates as collateral for the loan. The original note matured on May 19, 2001, and the outstanding balance of \$162,961.80 was refinanced with a new maturity date of May 19, 2003. The mortgage was subsequently modified to reflect the extended maturity date. Debtor executed a personal guarantee in favor of Regions guaranteeing the loan to Russellville Title. Russellville Title was a company solely owned by Debtor; its corporate status is now revoked.

Although Debtor executed the note and mortgage on behalf of Russellville Title as its President, neither Russellville Title nor Debtor held title to Lakeridge Estates at the time Debtor executed the mortgage. Like the Ruth Lane property, Lakeridge Estates was transferred to Debtor by her son and daughter by quitclaim deed on March 28, 2002.

Debtor valued Lakeridge Estates at \$30,000.00 on her bankruptcy schedules. Tarpley testified that the Debtor currently owed approximately \$171,000.00 in principal and interest on the Lakeridge Estates loan. Debtor listed the property for sale with Moore & Company Realtors for \$33,500.00 on May 10, 2001. The Debtor testified that she was “confident” the property was worth no more than \$30,000.00 or \$33,500.00. Mr. Tony Moore of Moore & Company Realtors testified that no offers had been made on the property following its listing, and that the lack of offers indicates that the property is not worth the listing price of \$33,500.00. Moore testified that he believed the listing price should be lowered to \$18,000.00 in order to sell the property based on current market conditions. The Trustee offered no evidence of a different value for the property.

DISCUSSION

With respect to Ruth Lane, Regions seeks relief from stay so that it can proceed with a state court foreclosure action and “quick sell” the property. Regions does not allege the Debtor has no equity in Ruth Lane or that it lacks adequate protection, but that the costs of litigation with respect to Ruth Lane continue to rise, and therefore, Regions wants to quickly move forward with a foreclosure sale of the property. With respect to Lakeridge Estates, Regions asserts that it is entitled to relief from stay because the Debtor has no equity in the property and Regions lacks adequate protection.

The Trustee argues that relief from stay should be denied because there is equity with respect

to Ruth Lane, and there are questions regarding the validity of Regions' security interests in both Properties. Specifically, because the mortgages were not executed by the owner of the Properties, and title was later acquired by Debtor within 90 days prior to her bankruptcy filing, the Trustee needs time to pursue possible avoidance actions in bankruptcy court to determine the validity of Regions' liens.

While Regions acknowledges that there may be an issue with respect to the validity of Regions' security interests in the Properties, it contends that those issues are "state court questions" which should be decided in the Pope County Circuit Court where Regions previously filed foreclosure suits against Debtor. However, Regions did not develop this argument by presenting evidence that the state court is the most appropriate place to determine such issues. Neither did Regions assert that it is moving for relief from stay so that it can determine the validity of its security interests in state court.¹ In fact, in its pleadings, Regions notes that Debtor has not defended the Pope County foreclosure suits and is in default in those actions. Accordingly, it does not appear that the validity of Regions' security interests are or will be an issue that is tried in the state court.

I. LEGAL STANDARDS AND BURDENS OF PROOF.

Relief From Stay "For Cause" – Adequate Protection.

Relief from the automatic stay may be granted "for cause" under 11 U.S.C. § 362(d)(1). "Cause" may include, but is not limited to, the lack of adequate protection of a secured party's interest in property. The concept of adequate protection is intended to protect an entity's interest in

¹Relief from stay "for cause" under 11 U.S.C. § 362(d)(1) may include relief from stay to allow litigation involving the debtor to proceed in a nonbankruptcy forum under certain circumstances. *In re Blan (Blan v. Nachogdoches County Hospital)*, 237 B.R. 737 (B.A.P. 8th Cir. 1999).

property from a decline or threatened decline in value. See *In re Anthem Communities/RBG, LLC*, 267 B.R. 867, 871 (Bankr. D. Colo. 2001); *United Sav. Ass'n v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 370 (1988). A creditor may show that it lacks adequate protection by presenting evidence of no equity in the property, depreciating property values, the non-payment of taxes or other senior liens, the failure to insure the property, an increase in secured debt due to interest accruals or otherwise, the failure to maintain the property, or other factors jeopardizing the creditor's position. See *In re Anthem Communities/RBG, LLC*, 484 U.S. at 871; *In re Marchand*, 61 B.R. 81, 84 (Bankr. E.D. Ark. 1986). What constitutes adequate protection is a factual issue to be decided on a case-by-case basis. See *In re Martin*, 761 F.2d 472, 474 (8th Cir. 1985). However, 11 U.S.C. § 361 provides that adequate protection may be provided by making periodic cash payments to the secured creditor, providing the creditor with additional or replacement liens or other relief that will result in the realization by the creditor of the "indubitable equivalent" of the creditor's interest in the property.

Relief From Stay – Lack of Equity in Property That Is Not Necessary For An Effective Reorganization.

Relief from the stay against property may also be granted under 11 U.S.C. § 362(d)(2) if a two-prong test is met. First, the debtor must have no equity in the subject property, and second, the subject property must not be necessary to the debtor's reorganization. However, if a creditor proves that there is no equity in the subject property in a Chapter 7 case, the stay should be lifted because there can be no question that the property is not necessary for an effective reorganization where the debtor only seeks to liquidate her assets. See *In re Knight Jewelry*, 168 B.R. 199 (Bankr. W.D. Mo. 1994); *In re Roxrun Estates, Inc.*, 74 B.R. 997 (Bankr. S.D.N.Y. 1987).

Burden of Proof

Regardless of whether a creditor moves for relief under subsection (d)(1) or (d)(2), the creditor must first establish the validity and perfection of its security interest and the amount of the debt and other allowable costs secured by its claim. *See In re Irving A. Horns Farms Inc.*, 42 B.R. 832, 836 (Bankr. N.D. Iowa 1984). *See also First Nat'l Bank of Denver v. Turley*, 705 f.2d 1024 (8th Cir. 1983) (“To obtain relief from stay under 11 U.S.C. § 362(d), a creditor must show the court that its interest in the debtor’s property is sufficiently clear and in need of protection to justify exempting it from the normal course of bankruptcy proceedings.”) Once a creditor has established the validity and perfection of its security interest and the amount of the debt and other allowable costs secured by its claim, the creditor carries the ultimate burden of proof with respect to a debtor’s equity, and the debtor opposing stay relief has the burden on the remaining issues. 11 U.S.C. § 362(g). *See also First Nat'l Bank in Sioux City v. Dahlquist (In re Dahlquist)*, 34 B.R. 476, 481 (Bankr. D.S.D. 1983).

II. ANALYSIS.

Applying the legal standards and burdens of proof outlined above, Regions must make a *prima facie* case that it is entitled to relief from stay under § 362(d)(1) or § 362(d)(2). To do this, Regions must first prove that it has a valid security interest in the Properties, and then prove that Debtor has no equity in the Properties or that it otherwise lacks adequate protection in the Properties.

Ruth Lane

Regions did not make a *prima facie* case that it has a valid security interest in Ruth Lane. Regions introduced a promissory note and mortgage showing that the Debtor borrowed funds from Regions and mortgaged Ruth Lane as collateral for that loan; yet, Debtor testified she did not own Ruth Lane at that time. Furthermore, the Trustee introduced quitclaim deeds showing that Ruth Lane

was transferred to Debtor more than a year after she mortgaged the property. Although the transfer of title to Debtor just before her bankruptcy filing may have cured Regions' security interest under Arkansas' after-acquired title statute (Ark. Code Ann. § 18-12-601), the substance of the transaction may constitute an avoidable preference under bankruptcy law such that Regions does not in fact have a valid security interest in Ruth Lane that would entitle it to relief from stay. *See, e.g., In re Russell*, 29 B.R. 332 (Bankr. E.D.N.Y. 1983) (perfection of security interest within three months of debtors' petition constituted a voidable preference). Finally, Regions failed to state any grounds entitling it to relief from stay in any case. It did not allege that it lacked adequate protection and acknowledged that there was equity in the property.

Lakeridge Estates

Regions also failed to make a *prima facie* case that it has a valid security interest in Lakeridge Estates. Although Regions established that Debtor took out a loan and mortgaged Lakeridge Estates as collateral for that loan on behalf of Russellville Title, Debtor testified that neither she nor Russellville Title held title to the property. Additionally, the Trustee introduced quitclaim deeds showing that the property was transferred to Debtor nearly two years after the loan was made. Again, because the transaction that may have validated Regions' mortgage may not withstand a preference action in bankruptcy court, Regions has failed to show that it has a valid security interest in Lakeridge Estates.

The Court further finds that had Regions' established a valid security interest in Lakeridge Estates, it would be entitled to relief from stay because the Debtor and Moore's testimony established the value of Lakeridge Estates as under \$33,500.00, well below the approximate \$171,000.00 currently owed Regions. The Trustee failed to offer any evidence to rebut these values.

CONCLUSION

Regions failed to meet its burden of proof that it has a valid security interest in the Properties, and accordingly is not entitled to relief from stay. The Court does not make any finding as to whether Regions has a valid security interest in the Properties or the priority of that security interest with respect to the Trustee; the validity and priority of Regions' mortgages should be decided in the context of an adversary proceeding pursuant to Fed. R. Bankr. P. 7001. For the reasons stated herein,

Regions' Motion for Relief from Stay is **DENIED**.

IT IS SO ORDERED.

HONORABLE AUDREY R. EVANS
UNITED STATES BANKRUPTCY JUDGE

DATED: _____

cc: Mr. M. Randy Rice, Esq., Chapter 7 Trustee
Mr. James V. Coutts, Esq. for Regions
Mr. John R. Peel, Esq. for FAVB
Mr. William Skelton, Esq. for debtor
U.S. Trustee