

U.S. BANKRUPTCY COURT
District of South Carolina

Case Number: 09-04624

ORDER

The relief set forth on the following pages, for a total of 10 pages including this page,
is hereby ORDERED.

FILED BY THE COURT
11/19/2009




US Bankruptcy Court Judge
District of South Carolina

**UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF SOUTH CAROLINA**

IN RE:

Ray Lyle Covington,

Debtor(s).

C/A No. 09-04624-HB

Chapter 11

ORDER

THIS MATTER came before the Court for hearing on November 12, 2009, pursuant to the Motion of Branch Banking and Trust Company (BB&T) for relief from the automatic stay of 11 U.S.C. §362. After considering the testimony and documentary evidence, proffers of evidence and after careful consideration, the Court enters the following **ORDER**:

Findings of Fact

1. Ray Lyle Covington filed for Chapter 11 protection on June 23, 2009. No trustee has been appointed in the case.
2. Covington filed a Motion to Extend the Exclusivity period for filing a plan of reorganization and has received a brief extension until November 27, 2009.
3. On October 14, 2009, BB&T filed a Motion for Relief from Stay involving property located at 2507 Devine Street in Columbia, South Carolina.
4. Covington's schedules list various parcels of income producing and investment property. Covington is also a real estate agent in Columbia, South Carolina. Since 2003 he has operated a franchise of Weichert Realtors. This business associates numerous real estate agents and provides a portion of Covington's personal income. The business pays rent to Covington for its business location, 2507 Devine Street, of \$3,500.00 per month. Covington testified that this rent is paid to him as the owner of the

property from Weichert and that the rent is above market rate, but he pays it on advice of his accountant. He testified that the costs and disruption to his business that would result from a move from that location would be devastating, and that for this reason and others the property is necessary for an effective reorganization.

5. Covington offered into evidence projections of the income and expenses for this property as set forth below:

Property:	2507 Devine Street	
Income Rents:	42000	Rents are high because
		Weichert rents subject
		on normal market \$30,000.00
Expenses:		
Advertising	0	
Auto and Travel	0	
Cleaning and Maintenance	1200	
Insurance	1200	
Commission	4200	
Repairs	2500	
Supplies	0	
Taxes	4725	
Utilities	0	
Regime Fees	0	
Pest Control	600	
Vacancy Rate (Two Months)	7000	
Total Expenses	21425	
Mortgage Payments:		
Principal	185000	
Interest Only 2% for 15 years	3700	
Net Cash Flow:	18875	

6. Covington offered into evidence a draft of a disclosure statement that included a summary of a draft plan of reorganization. The document stated that "Debtor has obtained an appraisal on this property and its estimated that the 'Income Approach' value is between \$179,344 to \$201,762. In the best of circumstances in this economy if a person were to purchase the property without expectation of a return on the investment, the most that could be anticipated is \$371,581."

7. BB&T's Certification of Facts lists total debt encumbering the property in excess of \$531,000.00, with an explanation that this is the combined amount due on the three notes held by BB&T. Covington's draft plan states that BB&T holds three claims secured by the property as follows: first lien, \$186,522.81; second lien, \$287,642.00; third lien, \$49,254.39. In addition to mortgages on the real estate, BB&T claims a lien on the rents from 2507 Devine Street to secure the obligations. Since filing, Covington has collected the rents from the building without payment to BB&T and without the permission of that lender or of the Court.

8. Covington states in the draft disclosure statement that he thinks the property is worth \$185,000.00. BB&T's first lien exceeds this amount. Covington's draft proposes to pay the value of BB&T's first lien, which he states is \$185,000.00, plus 2% interest annually, by making monthly interest only payments with a balloon payment due at the end of 180 months. The draft states that BB&T's second and third mortgages are unsecured as a result of the value of the property and will be paid as general unsecured claims.

9. As indicated in the projections set forth in paragraph 5 above, the market rent for this property may be \$30,000.00 annually rather than the \$42,000.00 currently being paid by Weichert to Covington. The exhibit indicates a "net cash flow" after expenses for the property of \$18,875.00¹ per year if the proposed plan treatment is approved (expenses include \$3,700.00 per month "interest only 2% for 15 years"). At the asserted market rate of \$30,000.00 annually this number drops considerably, and a higher

¹ A review of the numbers contained in the projections of the income and expenses for the 2507 Devine Street property suggests that Covington made a calculation error in his favor. The projected net cash flow appears off by \$2,000.00.

interest rate, valuation, or an amortization of the debt rather than a balloon payment could consume any "net cash flow."²

10. In the draft Covington proposed similar repayments terms—2% interest only payments with a balloon note at the end of a 180 month term—on various other obligations. He testified that this was simply a "wish list" of terms that he would hope to have, but he was willing to pay more. He conceded that the prime rate of interest exceeds 2%.

11. The draft proposes to pay 1% to general unsecured claims. Covington offered evidence indicating that this distribution may be proposed in a higher amount depending on any recovery from a lawsuit and the amount of claims in this class.

12. Covington offered a market analysis of 2507 Devine Street from an independent third party as follows:

Based on the above "Income Approach (Office)" assessment you can see that an "investor" who may have an interest in purchasing the property, in order to achieve a reasonable return on investment, would be able to pay approximately \$179,344 to \$201,762. In addition, the "Income Approach" is slightly higher if the property is sold as a retail income property for a range of \$313,666 to \$352,875. A "user" not necessarily having to achieve a required return on investment may be willing to pay, from a comparable standpoint, as much as \$371,581 or \$157.25 (the average comp) PSF. However, the market has changed since these comparables were sold.

In order to maximize the sales price of the property we would recommend targeting those logical "users" that typically have demand for such properties and who need an office or retail in a high traffic corridor. These "users" may be comprised of associations, attorneys, mortgage & real estate offices, gift store or small boutiques.

Based on the above assessment and considering that the property could be used for retail or office use, I would recommend the property be valued in a range of **\$368,628 (\$156 PSF) to \$401,710 (\$170 PSF).**

² \$185,000.00 amortized for 180 months at a modest 5% yields payments of approximately \$1,463.00 per month, and \$17,556.00 per year. Based on this payment Covington's "net cash flow" would be \$3,019.00 per year at the \$42,000.00 rent rate, and -\$8,981.00 per year at the \$30,000.00 "normal market" rate.

13. Covington listed the 2507 Devine Street property on his schedules as having a value of \$185,000.00 under the "Current Value" entry, including the following explanation:

Business Office, rented by Weichert Realtors located at 2507 Devine Street, Columbia, SC 29205; TMS No R11312-03-06; Tax value \$207,800; 2009 Online appraisal based on comps \$256,000. Debtor believes property is worth \$185,000 in today's market.

14. BB&T's Motion seeks relief from stay pursuant to 11 U.S.C. § 362(d)(1) and (2). The Motion alleges that Covington has failed to make payments to BB&T. The Motion includes a Certification of Facts that stated a value of \$256,000.00 with the following footnote regarding that amount:

1 The stated value is from the Debtor's schedules as to which he is bound by various theories of estoppel. Movant reserves the right to have the property valued at a greater value than set forth herein and would assert that the value of the property is in excess of the value claimed by the Debtor but not of sufficient value to create equity sufficient to cover the indebtedness of the Movant.

15. Covington presented his monthly operating reports into evidence. Those reports indicate income from rental properties with little debt service deducted because he is paying only limited debt service to mortgage holders. The reports also include income from his business Weichert Realtors, but there was very little evidence presented to indicate the income and expenses of that company, debt structure, or sustainability of that company and its associated personal and rental income stream to Covington.

16. Covington testified that he has offered adequate protection payments to this and other creditors but those offers have not been accepted. Covington testified that currently the market for his property is poor and the realty is not appreciating.

Discussion and Conclusions of Law

BB&T has the burden of proof regarding equity in the property; Covington has the burden of proof on all other issues. 11 U.S.C. §362(g).

Section 362(d)(2) provides the following regarding when stay relief may be granted:

[W]ith respect to a stay of an act against property under subsection (a) of this section, if—

- (A) the debtor does not have an equity in such property; and
- (B) such property is not necessary to an effective reorganization.

BB&T has met its burden of proving that Covington has no equity in the property after considering all debts owed to BB&T that encumber the property and any of the values before the Court. To defeat the creditor's Motion under § 362(d)(2), Covington must show that the property located at 2507 Devine is necessary to an effective reorganization. Covington has presented sufficient evidence to show that the property in question is necessary if he is to reorganize, but he must also establish "that there is 'a reasonable possibility of a successful reorganization within a reasonable period of time.'" *In re Mullock*, 404 B.R. 800, 805-06 (Bankr. E.D. Pa. 2009). In other words, it is not enough to show "that if there is conceivably to be an effective reorganization, this property will be needed for it; but that the property is essential for an effective reorganization *that is in prospect*." *United Sav. Asso v. Timbers of Inwood Forest Assocs.*, 484 U.S. 365, 375-76 (U.S. 1988).

From the evidence presented, the Court is certainly skeptical about Covington's reorganization prospects in today's real estate market under the draft plan. However, Covington has offered some evidence that he can continue towards some form of reorganization utilizing this particular property, his business location, and in fact that he

has little chance of a reorganizing without it. The evidence shows that Weichert Realtors is currently, regularly paying rent on the property to him. He also offered evidence that the business is producing additional income for him at this time. The continuation of this income was not considerably challenged by BB&T at this hearing. Covington testified that this income stream would be severely damaged or eliminated with the loss of the 2507 Devine Street property. Further, Covington proposed at the hearing that he was willing to alter the draft plan to surrender property that is not necessary to an effective reorganization, and to incorporate the Court's rulings on this matter and others heard by the Court on the same day.³ Weighing all of the evidence presented, Covington has met his burden of proving that the property located at 2507 Devine Street is necessary for an effective reorganization.⁴ He has shown that this "property is essential for an effective reorganization *that is in prospect*" and he has until November 27, 2009, the end of the exclusivity extension, to formulate a final plan including this property. Therefore, BB&T is not entitled to relief pursuant to § 362(d)(2).

11 U.S.C. §362(d)(1) provides the following:

(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay—

(1) for cause, including the lack of adequate protection of an interest in property of such party in interest.

BB&T also argues that Covington has used its cash collateral, the rents of 2507 Devine, since the filing of this case without BB&T's consent or court order and that this conduct

³ Relief from stay has been granted regarding several properties since the hearing on this matter.

⁴ The Court cautions the Debtor that the evidence certainly does not prove that the plan set forth in the draft disclosure statement is feasible or confirmable.

is inappropriate and constitutes cause for relief under §362(d)(1).⁵ See 11 U.S.C. §363; *In re R & G Props.*, 2009 Bankr. LEXIS 2100 (Bankr. D. Vt. July 6, 2009); *In re FCX, Inc.*, 54 B.R. 833, 838 (Bankr. E.D.N.C. 1985) (holding that debtors are “prohibited from using cash collateral without court approval or the consent of the secured creditor . . .”). The Bankruptcy Code’s “[u]se of the word ‘cause’ suggests an intention that the bases for relief from the stay should be broader than merely lack of adequate protection.” 3-362 Collier on Bankruptcy P 362.07. “Because the Bankruptcy Code provides no definition of what constitutes ‘cause,’ the courts must determine when discretionary relief is appropriate on a case-by-case basis.” *Cloughton v. Mixson*, 33 F.3d 4, 5 (4th Ct. App. 1994).

Covington has collected the rents from the property and used BB&T’s cash collateral without consent or authority from the Court. As a result and based on other facts set forth above, cause exists for “terminating, annulling, modifying, or conditioning” the automatic stay pursuant to § 362(d)(1). Of these choices, the Court elects to keep the automatic stay in place at this time, conditioning its continuance on BB&T’s adequate protection. Covington has had the use of the rents from this property since before the filing of this case without making scheduled payments to BB&T. The Court finds that the rents from the property should be paid to BB&T, without any reduction for expenses, for the months of November, December, and January. The first payment for November of \$3,500.00 shall be made on or before November 30, 2009. The second and third payments shall be due on the 15th of each month in December and January. Exact application of those funds to BB&T’s mortgage(s) shall be determined by

⁵ Covington filed a Motion to Use Cash Collateral on November 11, 2009. A hearing is scheduled for December 10, 2009.

agreement of the parties, by a confirmed plan or by further order of this Court. Payments shall be made payable to BB&T and delivered to Steve Licata, attorney for BB&T in this matter, unless the parties agree to the contrary in writing. Should Covington fail to make the payments as set forth herein on the date that they are due, BB&T may file an Affidavit detailing the default and a proposed order granting relief from the automatic stay.

IT IS THEREFORE, ORDERED:

1. The automatic stay shall remain in effect at this time on the following conditions: The rents due from Weichert Realtors to Lyle Ray Covington should be delivered to Steve Licata, attorney for BB&T in this matter, unless the parties agree to the contrary in writing, as follows: \$3,500.00 on or before November 30, 2009; \$3,500.00 on or before December 15, 2009; and \$3,500.00 on or before January 15, 2010. Should Covington fail to make the payments as set forth herein, delivered to Mr. Licata **on or before the date that they are due**, BB&T may filed an Affidavit detailing the default and a proposed order granting relief from the automatic stay.

2. Take notice that the Court will hold a hearing on **January 15, 2010, at 9:30 a.m. in the J. Bratton Davis Federal Courthouse, 1100 Laurel Street, Columbia, SC 29201-2423**, to review the adequate protection terms set forth herein and if necessary, the Debtor's progress towards confirmation of a plan of reorganization.