SO ORDERED,

Judge Neil P. Olack
United States Bankruptcy Judge
Date Signed: June 15, 2016

The Order of the Court is set forth below. The docket reflects the date entered.

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF MISSISSIPPI

IN RE:

PIONEER HEALTH SERVICES, INC. ET AL.,	**CASE NO. 16-01119-NPO**
	JOINTLY ADMINISTERED
DEBTORS.	**CHAPTER 11**

ORDER DENYING COMMUNITY CAPITAL BANK OF VIRGINIA, AS SERVICING AGENT FOR VCC 08-05, LLC AND VIRGINIA COMMUNITY CAPITAL, INC.'S MOTION TO COMPEL ADEQUATE PROTECTION

This matter came before the Court for hearing on May 20, 2016 (the "May 20 Hearing"), and June 3, 2016 (the "June 3 Hearing" or, together with the May 20 Hearing, the "Hearings"), on the Community Capital Bank of Virginia, as Servicing Agent for VCC 08-05, LLC and Virginia Community Capital, Inc.'s Motion to Compel Adequate Protection (the "Motion") (Dkt. 126) filed by Community Capital Bank of Virginia, as Servicing Agent for VCC 08-05, LLC (the "VCC Lender") and Virginia Community Capital, Inc. (the "Community Capital Lender" or, together with the VCC Lender, the "Lenders") and the Answer, Objection and Response to Community Capital Bank of Virginia, as Servicing Agent for VCC 08-05, LLC and Virginia Community Capital, Inc.'s Motion to Compel Adequate Protection (Dkt. 282) filed by the Debtors, Pioneer Health Services, Inc. *et al.* (the "Debtors"), in the above-referenced bankruptcy

case (the "Bankruptcy Case"). At the Hearings, the Lenders were represented by Michael Allen Condyles and Kristina M. Johnson, the Debtors were represented by Craig M. Geno, and the Official Committee of Unsecured Creditors of Pioneer Health Services, Inc., *et al.* (the "Committee") was represented by Darryl Scott Laddin and Sean C. Kulka. At the end of the May 20 Hearing, the Court instructed the parties to submit letter briefs addressing whether the Lenders are entitled to adequate protection under 11 U.S.C. § 363(e) in the absence of evidence that their collateral is decreasing in value. The Lenders submitted their letter brief (the "Lender Brief") on May 27, 2016, and the Debtors submitted their response to the Lender Brief on June 2, 2016 (the "Debtor Brief"). After considering the pleadings, evidence, and arguments of counsel, the Court denied the Motion from the bench at the June 3 Hearing. This Order memorializes and supplements the Court's bench ruling.

Jurisdiction

This Court has jurisdiction over the subject matter of and the parties to this proceeding pursuant to 28 U.SC. § 1334(b). This matter is a core proceeding arising under 28 U.S.C. § 157(b)(2)(A) and (O). Notice of the Motion was proper under the circumstances.

Facts

Pioneer Health Services, Inc. and certain of its affiliates, including Pioneer Health Services of Patrick County, Inc. in Case No. 16-01120-NPO ("Pioneer of Patrick County"), filed chapter 11 petitions for relief on March 30, 2016. On April 6, 2016, the Court entered an order (Dkt. 44) authorizing joint administration of the chapter 11 cases pursuant to FED. R. BANKR. P. 1015(b), with the Bankruptcy Case as the lead case.

VCC Lender Notes

Pioneer of Patrick County is indebted to the VCC Lender in connection with two (2) promissory notes dated May 3, 2013, in the original principal amounts of $4,919,798.00 and $1,870,202.00 (Lender Exs. 1-2) (the "VCC Lender Notes"). The VCC Lender Notes are secured by certain real property located at 18688 Jeb Stuart Highway, Stuart, Virginia 24171 (the "Hospital") pursuant to the Deed of Trust, Security Agreement, Assignment of Leases and Rents and Fixture Filing (Lender Ex. 4) recorded on May 6, 2013. The VCC Lender Notes are further secured by a Bank Account Pledge Agreement which grants a security interest in a debt service escrow account held by Community Capital Bank of Virginia (Lender Ex. 6) (the "Debt Service Account"). The security interest in the Debt Service Account is perfected in accordance with the Pledged Account Control Agreement by and between the VCC Lender, Pioneer of Patrick County, and Community Capital Bank of Virginia (Lender Ex. 7).

Under the VCC Lender Notes, Pioneer of Patrick County is required to make monthly interest-only payments to the VCC Lender until maturity. (Lender Ex. 3). The payoff allegedly due the VCC Lender is $6,952,780.35 (at the non-default interest rate) as of May 20, 2016 (Lender Ex. 14). Pioneer of Patrick County stopped making payments on the VCC Lender Notes in February 2016. (Lender Exs. 15-16).

Community Capital Lender Note

Pioneer of Patrick County is also indebted to the Community Capital Lender in connection with a promissory note dated May 8, 2014, in the original principal amount of $141,000.00 (Lender Ex. 9) (the "Community Capital Lender Note"). The Community Capital Lender Note is also secured by the Hospital. Under the Community Capital Lender Note, Pioneer of Patrick County is required to make monthly principal and interest payments. (*Id.*).

The payoff allegedly due the Community Capital Lender is $107,246.90 (at the non-default interest rate) as of May 20, 2016. (Lender Ex. 14). Pioneer of Patrick County stopped making payments on the Community Capital Lender Note in February 2016. (Lender Ex. 16).

Collateral

Pioneer of Patrick County is delinquent on its real estate taxes related to the Hospital. According to the Lenders, Pioneer of Patrick County owes real estate taxes in the collective amount of $51,972.77 due through April 15, 2016. (Mot. ¶ 17).

With respect to the value of the Lenders' collateral, the Debtor's bankruptcy schedules show that the "net book value" of the Hospital is $7,196,492.21. (Sch. A/B: Assets-Real and Personal Prop. at 4, Lender Ex. 17). According to the Lenders, the balance in the Debt Service Account as of April 5, 2016, was $216,742.14. (Mot. ¶ 10). Although the Debtor and Committee challenge any attempt to equate the fair market value of the Hospital with its "net book value," there is no dispute that the Lenders are oversecured creditors. According to the Lenders at the May 20 Hearing, their security cushion,[1] computed as a loan to value ratio, was four percent (4%). The Lenders filed the Motion under 11 U.S.C. § 363(e),[2] arguing that they are entitled to adequate protection because their security cushion in the Hospital continues to erode as postpetition interest[3] and real estate taxes continue to accrue.

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[1] In this Order, "security cushion" refers to the equity in property above the creditor's lien, that is, the difference between the value of the property and the sum of the amount of the creditor's liens and all liens senior in priority to the creditor's lien. *See In re Young*, No. 7-11-12554, 2011 WL 3799245, at *12 n.17 (Bankr. D.N.M. Aug. 29, 2011).

[2] All code sections refer to the Bankruptcy Code (the "Code") found at title 11 of the U.S. Code unless otherwise noted.

[3] At the May 20 Hearing, the Lenders calculated loan payments using both default and non-default interest rates. (Lender Exs. 14 & 16). At this juncture, the Court will reserve ruling on the appropriate rate of interest.

Discussion

An entity that has an interest in property may request adequate protection under § 363(e). That section provides, in pertinent part:

> [A]t any time, on request of an entity that has an interest in property used, sold, or leased, or proposed to be used, sold, or leased, by the trustee, the court, with or without a hearing, shall prohibit or condition such use, sale, or lease as is necessary to provide adequate protection of such interest.

11 U.S.C. § 363(e). From the examples listed in § 361, "adequate protection" required by § 363(e) is measured by the "decrease in the value of the entity's interest" in property of the estate. Section 361 provides:

> When adequate protection is required under section . . . 363 . . . of this title of an interest of an entity in property, such adequate protection may be provided by—
>
> > (1) requiring the trustee to make a cash payment or periodic cash payments to such entity, to the extent that the . . . use, sale, or lease under 363 of this title . . . results in a decrease in the value of such entity's interest in such property;
> >
> > (2) providing to such entity an additional or replacement lien to the extent that such stay, use, sale, lease, or grant results in a decrease in the value of such entity's interest in such property; or
> >
> > (3) granting such other relief, other than entitling such entity to compensation allowable under section 503(b)(1) of this title as an administrative expense, as will result in the realization by such entity of the indubitable equivalent of such entity's interest in such property.

11 U.S.C. § 361.

Section 506(a) divides claims into two (2) categories, secured and unsecured. Section 506(a) provides that an allowed claim is "a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property . . . and is an unsecured claim to the extent that the value of the such creditor's interest . . . is less than the amount of such allowed claim." 11 U.S.C. § 506(a). An oversecured creditor's right to postpetition interest is governed

by § 506(b), which allows interest to a creditor holding a secured claim, but only "[t]o the extent that an allowed secured claim is secured by property the value of which [after recovery of expenses] is greater than the amount of such claim." 11 U.S.C. § 506(b).

The parties do not dispute that the Lenders are oversecured creditors entitled to postpetition interest and that as the postpetition interest accrues, the Lenders' security cushion is being depleted. The narrow legal issue raised by the Lenders at the Hearings was whether they are entitled to adequate protection for accruing postpetition interest in order to preserve their security cushion. Equally important, an issue that was not raised at the Hearings was whether the Lenders are entitled to adequate protection because of the declining value of their collateral.

The Code does not define "adequate protection." The U.S. Supreme Court in *United Savings Association of Texas v. Timbers of Inwood Forest Associates, Ltd*., 484 U.S. 365 (1988), determined that "adequate protection" was intended by Congress to prevent a loss in the value of a secured creditor's interest in property of the bankruptcy estate during the pendency of a bankruptcy case. *Id*. at 370-71. The key holding of *Timbers* is that the phrase "'value of such creditor's interest'" in § 506(a) means 'the value of the collateral.'" *Timbers*, 484 U.S. at 372.

Although the Lenders showed at the Hearings that the size of their security cushion is decreasing as the postpetition interest accrues, the Court finds that the Lenders are not entitled to preservation of their postpetition interest accrual. In other words, the Court agrees with the Debtors' counsel that the Lenders are not entitled to an "evergreen" security cushion. (Debtor Br. at 2). "Even more important for our purposes than § 506's use of terminology is its substantive effect of denying undersecured creditors postpetition interest on their claims—*just as it denies oversecured creditors postpetition interest to the extent that such interest, when added*

to the principal amount of the claim, will exceed the value of the collateral." *Id*. (emphasis added).

As thoughtfully explained in *In re Young*, 2011 WL 3799245, at *8, the principles set forth in *Timbers* preclude a secured creditor from obtaining adequate protection to compensate it from erosion of its security cushion by postpetition interest accrual for at least the following reasons:

> (1) Payment of postpetition interest as adequate protection to maintain a security cushion does not serve the purpose of protecting a secured creditor from a decline or threatened decline in the value of the estate's interest in property that is the creditor's collateral.
>
> (2) Because a secured creditor is paid postpetition interest out of its security cushion, the payment of postpetition interest reduces the amount of the security cushion.
>
> (3) If payment of postpetition interest had no effect on the amount of the creditor's security cushion, the amount of postpetition interest accrual would not be limited by the amount of the security cushion contrary to § 506(b) and *Timbers*.

Id., at *8.

In the Lender Brief, the Lenders cite thirteen (13) cases in support of their contention that the erosion of a security cushion as the result of accrued postpetition interest is a sufficient basis for awarding adequate protection—even in the absence of any evidence of the collateral's declining value. None of these cases, however, directly supports their position. Two (2) of the cases were decided before *Timbers* and, thus, are of limited value. *See In re Jenkins*, 36 B.R. 788 (Bankr. S.D. Fla. 1984); *Ingersoll-Rand Fin. Corp. v. 5-Leaf Clover Corp. (In re 5-Leaf Clover Corp.)*, 6 B.R. 463 (Bankr. S.D.W. Va. 1980). Only one (1) of the cases actually mentions *Timbers*. *See In re Columbia Gas Sys., Inc*., Nos. 91-803, 91-804, 1992 WL 793232 (Bankr. D. Del. Feb. 18, 1992). And in that case, the bankruptcy court simply viewed the

discourse in *Timbers* as irrelevant to the issue of adequate protection for oversecured creditors, and, therefore, did not reach the issue presented here. In the only case decided by Fifth Circuit Court of Appeals, *Mendoza v. Temple-Inland Mortgage Corp. (In re Mendoza)*, 111 F.3d 1264 (5th Cir. 1997), the discussion cited in the Lender Brief took place in a separate opinion concurring in part and dissenting in part with the majority decision. There, a district court judge, sitting by designation, noted that "in determining whether a secured creditor's interest is adequately protected, most courts engage in an analysis of the property's 'equity cushion'—the value of the property after deducting the claim of the creditor seeking relief from the automatic stay and all senior claims." *Mendoza*, 111 F.3d at 1272 (quoting *Nantucket Investors II v. Calif. Fed. Res. Bank (In re Indian Palms Assoc., Ltd.)*, 61 F.3d 197, 207 (3d Cir. 1995)). The point being made by the district court judge was not that that a debtor is entitled to adequate protection of its security cushion but that a security cushion may provide adequate protection for the declining value of collateral under certain circumstances. This point is also made in the other cases cited in the Lender Brief, but is not dispositive of the issue raised by the Lenders.

A security cushion is not a goal of adequate protection. Rather, the goal of adequate protection is to preserve the value of the collateral encumbered by the creditor's lien. *See In re Lane*, 108 B.R. 6 (Bankr. D. Mass. 1989); *Orix Credit Alliance, Inc. v. Delta Res., Inc. (In re Delta Res., Inc.)*, 54 F.3d 722 (11th Cir. 1995) (oversecured creditor's interest in property which must be adequately protected encompassed decline in value of the collateral only, rather than perpetuating the ratio of the collateral to the debt). Under these facts, the Lenders are not

entitled to adequate protection. Accordingly, the Court concludes that the Motion should be denied.

IT IS, THEREFORE, ORDERED that the Motion is hereby denied.

##END OF ORDER##