

ADEQUATE PROTECTION

§ 506(b) benefits the oversecured creditor by allowing the holder of such claim to receive interest on such

§ 362(d) assures the secured creditor of adequate protection. If not adequately protected, the creditor is entitled to relief from the stay (ie creditor could seize the property)

Adequate protection is protection only against the deterioration of the value of their collateral

§ 506 has the 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 of the claim will exceed the value of the collateral

§ 506 permits post-petition interest to be paid only out of the "security cushion", the undersecured creditor's claim. If no such cushion, falls within the general rule disallowing postpetition interest. It has been considered unfair under case law to allow an undersecured creditor to recover interest from the estate's unencumbered assets before oversecured creditors had recovered any principal.

Timbers

"The Fifth Circuit correctly held that the undersecured petitioner is not entitled to interest on its claim during the stay to assure adequate protection under 11 U.S.C. § 362(d)(1) ..."

Courts usually use the rate set statutorily by each state to be paid on judgments of its courts as the "legal rate"

Under § 1124(2), a creditor is deemed unimpaired if its claim is reinstated and damages paid for missed payments

§ 1123(d), in the context of interest on interest, a proposal in the plan to cure a default, then the amount of interest necessary to cure the default shall be determined in accordance with the underlying agreement or applicable nonbankruptcy law. The intention was to put the debtor in the same position as if the default had never occurred, in order to avoid any court-contrived windfall to the creditor. So if and only if the agreement and applicable nonbankruptcy law permit it, the debtor may have to pay interest on interest

Adequate protection payments are made when the creditor is oversecured (i.e. the value of the collateral equals or exceeds the value of the obligation). However, when the collateral value far exceeds the value of the obligation, to the extent that the diminution of value in the collateral from its use during the case would still render the creditor oversecured, adequate protection payments are not made. The existence of this large equity cushion obviates the need for adequate protection payments.

If a creditor is deemed to be undersecured (i.e. the value of the collateral is less than the value of the obligation), the creditor likely receives adequate protection payments, but only to the extent of the diminution in the value of the collateral.

"But if it turns out that the facility is under-secured, obviously, as a matter of law, those adequate protection payments are deemed allocable to principal since, under § 506 of the Code, the party is no longer entitled to post-petition interest."

In *Timbers*, the Supreme Court ruled that creditors do not get post-petition interest as adequate protection if they are under-secured **unless** there is a diminution in the value of the collateral.

If the nominally secured creditor is under-secured, it has no entitlement to post-petition interest or attorney's fees. Although by custom or ignorance there are many cases in which parties seek and Courts approve adequate protection arrangements under which the adequate protection payments are equal to the contracted-for interest and attorney's fees under the loan agreement.

An under-secured creditor is entitled to adequate protection payments but only to the extent of a diminution in the value of the senior secured lenders' interest in their collateral from the time of the petition date.

If much of the difference in the value of the senior secured lenders' interest in their collateral was not attributable to diminution in collateral value, but, rather, to inaccuracies in measurement of that value early in the case it may turn out that the so-called adequate protection payments now being made cannot in the future appropriately be applied to post-petition interest or fees, and must be applied to principal instead. And the same is true with respect to those adequate protection payments made so far.

Beware of the use of asset sale proceeds related to the sale of pre-petition collateral for secured loans. *In re SCOPAC et al.*, F. 3d, 2010 WL 4069525, at *2-3, *5-6 (5th Cir. Oct. 19, 2010) (Jones, Ch. J.) [*"Pacific Lumber I"*] and see also *In re Pacific Lumber Co.*, 584 F. 3d 229, 242 (5th Cir. 2009) [*"Pacific Lumber I"*]:

"Essentially, the court reversed the bankruptcy court's failing to include certain asset sale proceeds as part of the lenders' pre-bankruptcy collateral package when determining the amount of the group's priority claim. That claim was based on the debtor's failure to provide the required "adequate protection" for the lenders' collateral."

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