BANKRUPTCY—WHETHER DEBTOR'S PROPOSAL TO SELL SECURED CREDITOR'S COLLATERAL ADEQUATELY PROTECTS A SECURED CREDITOR'S BARGAINED-FOR INTEREST REQUIRES COURT DETERMINATION OF THE VALUE OF THE CREDITOR'S SECURED INTEREST, THE RISK TO THAT VALUE UPON APPROVAL OF DEBTOR'S PLAN, AND WHETHER THE CREDITOR IS AFFORDED THE INDUBITABLE EQUIVALENT OF SUCH VALUE UNDER DEBTOR'S PROPOSAL.—*In re Martin* (8th Cir. 1985).

Debtors Ray and Joan Martin were North Dakota farmers who had filed business reorganization petitions pursuant to Chapter Eleven of the United States Code.[1] Having subsequently been unable to secure financing from various local lending institutions, the Martins filed motions to use cash collateral in bankruptcy court.[2] They proposed to sell stored grain mortgaged to the Commodity Credit Corporation (CCC), and to use the proceeds to pay their operational expenses incurred in 1984.[3] The Martins planned to give the CCC a first lien on their 1984 crop and an assignment of the proceeds from their federal crop insurance policies in return for the CCC's permission to sell the mortgaged grain.[4]

---

1. *In re* Martin, 761 F.2d 472, 473 (8th Cir. 1985). Chapter Eleven of the United States Code was designed to "deal with the reorganization of a financially distressed business enterprise, providing for its rehabilitation by adjustment of its debt obligations and equity interests." S. REP. No. 989, 95th Cong., 2d Sess. 9, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5787, 5795; *see also* H.R. REP. No. 595, 95th Cong., 2d Sess. 6, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5963, 5968.

2. *In re* Martin, 761 F.2d at 473. Chapter 11 U.S.C. section 363(a) defines "cash collateral" as encompassing "cash, negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents in which the estate and an entity other than the estate have an interest, such as a lien." S. REP. No. 989, 95th Cong., 2d Sess. 55, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5787, 5841; *see also* H.R. REP. No. 595, 95th Cong., 2d Sess. 344-45, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5963, 6301. The definition of "cash collateral" set out in 11 U.S.C. section 363(a) does not expressly cover the proceeds from the sale of "non-cash" collateral; but, "if 'non-cash' collateral [subject to a lien] is disposed of and the proceeds come within the definition of 'cash collateral' . . . the proceeds would be cash collateral as long as they remain subject to the original lien." S. REP. No. 989, 95th Cong., 2d Sess. 55, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5787, 5841; *see also* H.R. REP. No. 595, 95th Cong., 2d Sess. 345, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5963, 6301.

A debtor "may not use, sell or lease cash collateral except upon court authorization after notice and a hearing, or with the consent of each entity that has an interest in such collateral." S. REP. No. 989, 95th Cong., 2d Sess. 55, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5787, 5842; *see also* H.R. REP. No. 595, 95th Cong., 2d Sess. 345, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5963, 6301; *see generally* 11 U.S.C. § 363(c)(2)(B) (1982). Hence, in order to obtain permission to sell the grain mortgaged to the CCC and use the proceeds therefrom, the Martins were required to file motions requesting the court's authorization to sell the grain and use the proceeds to finance their 1984 operations. 11 U.S.C. § 363(c)(2)(B) (1982).

3. *In re* Martin, 761 F.2d at 473.

4. *Id.* The "first lien" language was apparently employed to insure that the CCC would

Hearings were held on the Martins' separate motions requesting the authorization both to sell the grain mortgaged to the CCC and to use the collateral therefrom to finance their 1984 crops.[5] Before ruling on these motions, the bankruptcy court was presented with estimates of the Martins' 1984 crop yield and value based upon the historical performance of their farm.[6]

According to these estimates, the harvested value of the Martins' 1984 crop was expected to exceed the amount of the CCC's collateral which the Martins wished to sell.[7] On the basis of this information, the bankruptcy court concluded that the Martins' proposal was sufficient to ensure that "it [was] virtually certain . . . that [the CCC] will be insured a return of its interest,"[8] and therefore granted the Martins' motions in separate orders.[9]

The CCC's notice of appeal to the United States District Court for the District of North Dakota resulted in a stay of the bankruptcy court's order pursuant to Bankruptcy Rule 8005.[10] The district court subsequently re-

---

have first priority in claiming proceeds from the future 1984 crop. *Id.* at 474. The Martins had obtained a federal crop insurance policy on their 1984 crop, pursuant to 7 U.S.C. section 1508. *Id.* at 475. The policy guaranteed up to seventy-five percent of the Martins' crop yield in the event of a crop failure due to "unavoidable causes." *Id. See generally* 7 U.S.C. § 1508 (1982). The policy did not cover crop losses due to "neglect or malfeasance of the producer. . . or the failure of the producer to follow established good farming practices." *In re* Martin, 761 F.2d at 475 (citing 7 U.S.C. § 1508(a) (1982)).

5. *In re* Martin, 761 F.2d at 473.

6. *Id.*

7. *Id.* at 473-74.

8. *In re* Martin, 761 F.2d at 474 (quoting *In re* Nikolaisen, 38 Bankr. 267, 270 (Bankr. D.N.D. 1984)). In *Nikolaisen*, the debtors, husband and wife, filed a motion requesting the use of cash collateral to finance their 1984 spring crop. *In re* Nikolaisen, 38 Bankr. at 268. The debtors in *Nikolaisen* also wished to obtain the requisite funds by selling grain mortgaged to the CCC. *Id.* In return, the debtors proposed granting the CCC a first lien upon their 1984 crops, in addition to assigning to the CCC any proceeds from a federal crop insurance policy held by the debtors. *Id.* The bankruptcy court granted the debtors' request for the use of cash collateral, finding that the first loan on the 1984 crop and the assignment of any proceeds from the debtors federal crop insurance policy adequately protected the CCC's secured interest. *Id.* at 270.

9. *In re* Martin, 761 F.2d at 474. The individual orders authorized the sale of the grain held under the CCC's mortgage and the Martins' use of the cash collateral created thereby. *Id.* The Martins were authorized, however, to use the cash collateral only up to the amount of the federal crop insurance policy assigned to the CCC. *Id.*

10. *Id.* Bankruptcy Rule 8005, entitled "Stay Pending Appeal," provides:

> A motion for a stay of the judgment, order or decree of a bankruptcy court, for approval of a supersedeas bond, or for other relief pending appeal must ordinarily be made in the first instance in the bankruptcy court . . . . A motion for such relief, or for modification or termination of relief granted by the bankruptcy court, may be made to the district court . . . but the motion shall show why the relief, modification, or termination was not obtained from the bankruptcy court. The district court . . . may condition the relief it grants under this rule on the filing of a bond or other appropriate security with the bankruptcy court.

Bankr. Rule 8005, 11 U.S.C.A. (1984).

versed the bankruptcy court, holding that the proposal offered by the Martins did not provide the CCC with adequate protection of its security interest.[11]

The bankruptcy court's order permitting the Martins to use the cash collateral from the sale of the grain mortgaged to the CCC was apparently stayed to protect the value of the CCC's secured interest. *See In re* Martin, 761 F.2d at 474. *See also In re* Victory Const. Co., Inc., 9 Bankr. 570, 573 (Bankr. C.D. Cal. 1981) ("The essence of the protection under Rule 8005 . . . is the maintainance of the *status quo*: the avoidance of impairment, erosion, or dimunition of the property rights and interests of the parties stayed, i.e., decrease in the value of the interest affected.").

11. *In re* Martin, 761 F.2d at 474. The district court, in reversing the bankruptcy court's finding that the CCC's interest was adequately protected, cited *In re* Berg, 42 Bankr. 335 (D.N.D. 1984). *In re* Martin, 761 F.2d at 474. In *Berg*, the debtors requested authorization to use cash collateral to finance their spring 1984 crop operations. *In re* Berg, 42 Bankr, at 336. The cash collateral to be used was to come from the proceeds received upon the sale of stored grain which was subject to a mortgage held by the CCC. *Id.* In exchange, the debtors proposed to give the CCC a first lien on their 1984 crop, and to assign to the CCC the proceeds from a federal crop insurance policy held by the debtors. *Id.* The bankruptcy court entered an order authorizing the debtor's use of the cash collateral. *Id.*

The CCC appealed the bankruptcy court's decision in both *Berg* and *Nikolaisen*, and the district court consolidated the appeals. *In re* Berg, 42 Bankr. at 336. The CCC argued that a lien on future crops was "purely speculative in nature" and was "subject to the uncertainties of weather and other natural phenomenon." *Id.* at 337. Therefore, assigning the CCC the proceeds from the debtors' federal crop insurance policies would not provide adequate protection to the CCC. *Id.* The debtors, on the other hand, argued that adequate protection was intended merely to provide secured creditors with protection against unreasonable risks, given the facts of individual cases. *Id.*

The debtors asserted that the district court should look to the commercial setting to determine whether the CCC's interest would be adequately protected. *Id.* The debtors stated that "[b]ecause lending institutions commonly make loans to farmers secured by a lien on crops to be grown, such a lien, plus an assignment of Federal Crop Insurance proceeds, is the indubitable equivalent of a lien on existing crops." *Id.*

The district court in *Berg* held that a lien on a future crop, in addition to an assignment of unrealized federal crop insurance proceeds, did not provide adequate protection to the CCC. *Id.* at 338. The court distinguished the cases relied upon by the debtors, noting that each of those cases dealt with existing collateral. *Id.* On the contrary, the promise of collateral that might exist in the future was found to provide the secured creditor with no collateral at all. *Id.* Because a secured creditor is able to "inspect, protect and control" a crop already harvested, a lien on a future crop was found to be less valuable to the secured creditor than a lien on an existing crop. *Id.* Moreover, "existing collateral is capable of being liquidated at any time, whereas a future crop must first be planted, grown and harvested." *Id.*

The district court, citing generally to the provisions of 7 U.S.C. section 1508(a) regarding farmers' federal crop insurance, also rejected the debtor's argument that the assignment of the debtors' federal crop insurance proceeds protected the CCC from possible crop failure. *Id.* The *Berg* court noted that while federal crop insurance protected against other types of losses, it could not protect the CCC from potential "management errors or poor husbandry practices" by the debtors. *Id.* In addition, the court stated that federal crop insurance insured only against those losses associated with the yield of the crop, and could not protect the CCC against possible losses in the marketplace due to decreased prices or discounts caused by grain of inferior quality. *Id.* Finally, the *Berg* court noted that the CCC was not a party to the debtors' federal crop insurance policies, and "should not have its interests dependent on the terms and inter-

The Martins appealed to the United States Court of Appeals for the Eighth Circuit, arguing that the evidence sufficiently established that the value of the lien given the CCC under their proposal exceeded the value of the grain then held by the CCC as collateral.[12] The Martins asserted that the protection afforded to the CCC under their proposal would be inadequate *only* in the event that their 1984 crop failed.[13] In addition, the Martins argued that their offer to assign the CCC their federal crop insurance proceeds adequately protected the CCC's secured interest against the risk of a crop failure because the proposal authorized the Martins to use cash collateral only up to the amount of their coverage under their federal crop insurance policy.[14]

In response, the CCC argued that the value of a future crop, even if insured, is not the same as a crop already harvested and stored.[15] Furthermore, the CCC maintained that the Martins' proposal did not afford adequate protection against a possible decrease in the future market price for crops.[16] In addition, the CCC asserted that Martins' federal crop insurance policy covered only crop failures resulting from "unavoidable causes," and did not cover failures due to the "neglect or malfeasance of the producer . . . or to the failure of the producer to follow established good farming practices."[17]

The Eighth Circuit Court of Appeals *held,* remanded.[18] Whether a debtor's proposal to sell a secured creditor's collateral and use the cash proceeds therefrom adequately protects the secured creditor's bargained-for interest requires a court determination of the value of the creditor's secured interest, the risk to that value if the debtor's plan is approved, and a determination of whether or not the debtor's proposal protects the secured creditor's value to such an extent that the creditor is afforded the indubitable equivalent of his claim. *In re Martin,* 761 F.2d 472 (8th Cir. 1985).

The Eighth Circuit's decision in *Martin* is particularly significant because the court stated with clarity the standard of review that it would employ when reviewing the issue of adequate protection of a secured creditor's interest.[19] No single standard was evident from previous bankruptcy and circuit court decisions on the adequate protection question.[20] Some courts had held that adequate protection was a conclusion of law subject to de novo

---

pretation of a contractual agreement to which it never intended to be a party." *Id.*

12. *In re* Martin, 761 F.2d at 475.
13. *Id.*
14. *Id.*
15. *Id.*
16. *Id.*
17. *Id.* (citing 7 U.S.C. § 1508 (1982)); *see also supra* note 4.
18. *In re* Martin, 761 F.2d at 478.
19. *In re* Martin, 761 F.2d at 474.
20. *Id.*

review,[21] while others held that it was a question of fact not to be disturbed on appeal unless clearly erroneous.[22] In *Martin*, the Eighth Circuit Court of Appeals joined those courts holding that adequate protection is a factual determination to be overturned by an appellate court only if the decision by the trial court was found to have been clearly erroneous.[23]

In reaching its conclusion, the Eighth Circuit specifically identified two issues.[24] Initially, the *Martin* court inquired "whether the bankruptcy court had applied the correct legal standard in finding the [Martins'] offer of a substitute lien in the 1984 crop along with an assignment of Federal Crop Insurance proceeds adequately protected CCC's security interest."[25] If this was the case, the second issue was "whether [the bankruptcy court's] determination of adequate protection was clearly erroneous."[26]

The *Martin* court, in examining the second of the two issues, found that the bankruptcy court had erred in deciding that the CCC had been afforded adequate protection under the debtors' proposal.[27] Ironically, it made this determination *without* applying the clearly erroneous standard of review which it had purported to adopt for the examination of lower court findings regarding adequate protection.[28]

The Eighth Circuit held that the bankruptcy court's error was the result of a misunderstanding of the law applicable to the issue of adequate protection, as opposed to an erroneous factual determination.[29] More specifically, the bankruptcy court's error occurred because it failed to apply the standard of adequate protection required by 11 U.S.C. section 361(3).[30] Overall, the appellate court did not question the factual determination of

---

21. *Id. See also, e.g., In re* Comer, 723 F.2d 737, 739 (9th Cir. 1984) (bankruptcy court's conclusions of law subject to de novo review); *In re* Philadelphia Consumer Discount Co., 37 Bankr. 946, 949 (E.D. Pa. 1984) (question of adequate protection is a matter of law, requiring independent evaluation); *In re* Schaller, 27 Bankr. 959, 962 (W.D. Wis. 1983) (bankruptcy judge's finding that proposals for use of cash collateral were too speculative to provide secured creditor adequate protection is a conclusion of law).

22. *In re* Martin, 761 F.2d at 474. *See also, e.g., In re* George Ruggiere Chrysler-Plymouth, Inc. 727 F.2d 1017, 1019 (11th Cir. 1984) (adequate protection determination not to be overturned absent clear error); *In re* Jim Kelly Ford Ltd., 14 Bankr. 812, 816 (N.D. Ill. 1980) (question of what protection is "adequate" is a determination of fact not to be disturbed unless clearly erroneous).

23. *In re* Martin, 761 F.2d at 474.

24. *In re* Martin, 761 F.2d at 475. The Eighth Circuit also dealt briefly with the question of mootness. *Id.* at 474. The court found that although the 1984 harvest had been completed prior to the Martins' appeal, the main issues were "capable of repetition yet evading review," and were not moot. *Id.*

25. *In re* Martin, 761 F.2d at 475.

26. *Id.*

27. *Id.*

28. *Id.*

29. *Id.*

30. *Id.*

the bankruptcy court under the adequate protection standard applied.[31] Rather, the court took issue with the standard itself.[32]

In *Martin*, the court of appeals stated that "an appellate court has the power to correct errors of law, including 'a finding of fact that is predicated on a misunderstanding of the governing rule of law.' "[33] Hence, the court was able to find error in the bankruptcy court's decision requiring adequate protection, despite the fact that the opinion did not address the issue of whether the bankruptcy court had "clearly erred" in determining that the CCC's interest had been adequately protected.[34]

By reaching the adequate protection issue in the *Martin* case, the court provided itself with an opportunity to clearly state the appropriate formula for reaching decisions regarding adequate protection. Furthermore, by treating the adequate protection question as a question of fact, the eighth circuit set precedent for lower courts in its jurisdiction. The signal to the lower courts is that in the future, they should apply the *Martin* guidelines to the facts of a case when ruling on adequate protection questions. If the *Martin* guidelines are followed, the holdings of the lower courts will be affirmed on appeal absent a clearly erroneous determination of fact.

In order to substantiate its analysis and conclusion in *Martin*, the Eighth Circuit examined the legislative history underlying the adequate protection concept, finding that Congress had intended to "insure that the secured creditor receives the *value* for which he bargained."[35] Because the

---

31. *See In re* Martin, 761 F.2d at 475.

32. *Id.*

33. *In re* Martin, 761 F.2d at 475 (quoting Bose Corp. v. Consumer Union of the United States, 104 S. Ct. 1949, 1960 (1984)). *See also* Inwood Laboratories v. Ives Laboratories, 456 U.S. 844, 855 n.15 (1982) ("Of course, if the trial court bases its findings upon a mistaken impression of applicable legal principles, the reviewing court is not bound by the clearly erroneous standard." (citation omitted)); Pullman-Standard v. Swint, 456 U.S. 273, 287 (1982) ("[I]f a [trial] court's findings rest on an erroneous view of the law, they may be set aside on that basis.").

34. *In re* Martin, 761 F.2d at 475.

35. *Id.* at 474 (citing S. REP. No. 989, 95th Cong., 2d Sess. 53, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5787, 5839 (emphasis added)); *see also* H.R. REP. No. 595, 95th Cong., 2d Sess. 339, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5963, 6295. The Senate Report clearly states the rationale underlying 11 U.S.C. section 361, which mandates adequate protection of secured creditors:

> This section [11 U.S.C. section 361] and the concept of adequate protection are based as much on policy grounds as on constitutional grounds. Secured creditors should not be deprived of the benefit of their bargain. There may be situations in bankruptcy where giving a secured creditor an absolute right to his bargain may be impossible or seriously detrimental to the policy of the bankruptcy laws. Thus, this section recognizes the availability of alternate means of protecting a secured creditor's interest . . . Though the creditor might not be able to retain his lien upon the specific collateral held at the time of filing, the purpose of the section is to *insure* that the creditor receives the *value* for which he bargained.

S. REP. No. 989, 95th Cong., 2d Sess. 53, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5787,

value the secured creditor had bargained for was to be determined on a case-by-case basis,[36] the court reasoned that in order to protect that value, adequate protection was also to be decided on a case-by-case basis.[37] The policy advanced by case-by-case treatment was "[permitting] the debtors 'maximum flexibility in structuring a proposal for adequate protection.' "[38]

Looking to 11 U.S.C. section 361, which sets forth the requirements of adequate protection for the creditor, the *Martin* court noted three alternative methods available to a bankrupt debtor for adequately protecting a secured creditor's interest where the debtor wished to use, sell, or lease collateral constituting the secured creditor's interest.[39] The third alternative under 11 U.S.C. section 361 is to permit the court to approve a debtor's adequate protection proposal if it provided the secured creditor with the *indubitable equivalent* of its interest.[40] This provision was the focus of the court's opinion in *Martin*.[41]

5839; *see also* H.R. REP. No. 595, 95th Cong., 2d Sess. 339, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5963, 6295 (emphasis added); *See also, e.g., In re* American Mariner Indus., Inc., 734 F.2d 426, 434-35 (9th Cir. 1984) (court recognized Congress' goal of assuring secured creditors the benefit of their bargains through the adequate protection concept).

36. *In re* Martin, 761 F.2d at 474. The Eighth Circuit noted that Congress intended the courts' determination as to the value of a secured creditor's bargain to be "a flexible concept," adaptable to the circumstances of various cases. *Id.* (citing H.R. REP. No. 595, 95th Cong., 2d Sess. 339, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5963, 6295); *see also* S. REP. No. 989, 95th Cong., 2d Sess. 54, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5787, 5840.

37. *In re* Martin, 761 F.2d at 474. The Eighth Circuit stated that because value was determined on an individual case basis, adequate protection of the determined value would have to be decided on a case-by-case basis as well. *Id.*

38. *Id.* (quoting *In re* American Mariner Indus., Inc., 734 F.2d 426, 435 (9th Cir. 1984)). The *American Mariner* court also recognized that the adequate protection concept was not rigid, stating that in order to give effect to the policies underlying 11 U.S.C. sections 361 and 362, the debtor was to be accorded "maximum flexibility" in designing an adequate protection proposal. *In re* American Mariner Indus., Inc., 734 F.2d at 435. The flexibility in favor of the debtor was not unlimited, however; the adequate protection proposal of the debtor was to be constructed in order to protect the secured creditor's bargained-for rights to the extent possible under the facts of the individual case. *Id.*

39. *In re* Martin, 761 F.2d at 476. The court noted that 11 U.S.C. section 361(1) permitted a debtor to make periodic cash payments to a secured creditor in return for the use of cash collateral. *Id.* In addition, the court stated that section 361(2) allowed a debtor to grant the secured creditor additional or replacement liens on the debtor's property, in return for authorizing the debtor's use of the proceeds from the sale of the collateral representing the secured creditor's interest. *Id.* Chapter 11 U.S.C. sections 361(1) and (2) were "designed to compensate for any decrease in value of a secured creditor's interest resulting from the use, sale or lease of the [secured] property." *Id.*

Under the third alternative set forth in 11 U.S.C. section 361(3), debtors are given flexibility as to the range of acceptable proposals for providing adequate protection. *Id.* Chapter 11 U.S.C. section 361(3) permits the court to approve "such other relief . . . as will result in the realization by [the creditor] of the indubitable equivalent of [its] interest in such property." *Id.* *See generally* 11 U.S.C. § 361 (1985).

40. *See* 11 U.S.C. § 361(3) (1985).

41. *See In re* Martin, 761 F.2d at 476.

The concept of indubitable equivalence originated in a bankruptcy case decided by Judge Learned Hand in 1935,[42] and was included in the text of 11 U.S.C. section 361 as a legislative compromise in enacting that section.[43] After reviewing the legislative history of 11 U.S.C. section 361, the court in *Martin* stated that a debtor's plan of reorganization, insofar as it related to adequate protection, should come as close as possible to providing the creditor with the value he had bargained for given the circumstances of the case.[44] The court noted that when a bankrupt debtor wishes to use, sell or lease secured collateral, the court, upon the creditor's request, shall "prohibit or condition such use, sale or lease as is necessary to provide adequate protection of [the creditor's] interest."[45] Ironically, the court also stated that

---

42. *See In re* Murel Holding Corp., 75 F.2d 941 (2d Cir. 1935). Judge Hand explained that:

> Adequate protection must be completely compensatory, and that payment ten years hence is not generally the equivalent of payment now. Interest is indeed the common measure of the difference, but a creditor who fears the safety of his principal will scarcely be content with that; he wishes to get his money, or at least his property. We see no reason to suppose that the statute was intended to deprive him of that in the interest of junior holders, unless by a substitute of the most *indubitable equivalence*.

Id. at 942 (emphasis added).

43. When 11 U.S.C. section 361 was proposed, the House and Senate versions were different in significant areas. *In re* Martin, 761 F.2d at 476. Both contained identical subsections now codified as 11 U.S.C. section 361(1) and section 361(2). *Id.* The House bill delineated two additional methods in which a debtor could provide adequate protection of a secured creditor's interest. *Id.*

The House bill granted an administrative expense priority to the secured creditor for any amount lost from permitting use of cash collateral. *Id.* (quoting H.R. REP. No. 595, 95th Cong., 2d Sess. 340, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5963, 6296). The Senate removed the provision, on grounds that "such protection is too uncertain to be meaningful." *Id.* (quoting S. REP. No. 989, 95th Cong., 2d Sess. 54, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5787, 5840). The House version also allowed the courts to approve plans providing the secured party protection "that will result in the realization by the [secured party] of the value of its interest in the property involved. *Id.* (quoting H.R. REP. No. 595, 95th Cong., 2d Sess. 340, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5963, 6296). The Senate version did not contain this section. *Id.* (quoting S. REP. No. 989, 95th Cong., 2d Sess. 54, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5787, 5840).

In *Martin*, the Eighth Circuit found that although the final version of 11 U.S.C. section 361(3) is similar to the original bill proposed by the House, the additional requirement that adequate protection must assure the secured creditor of receiving the "indubitable equivalent" of his interest was "conspicuous." *Id.* Its inclusion was perceived as legislative compromise in passing the bill. *Id.*

44. *Id. See supra* note 38.

45. *Id.* at 475-76. The Eighth Circuit referred to 11 U.S.C. section 363(3)(1985). That section provides that:

> Notwithstanding any other provision of this section, at 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 [debtor], the court shall prohibit or condition such use, sale, or lease as is necessary to provide adequate protection of such interest.

Id.

a reorganization plan could be confirmed by the court, despite a secured creditor's objections, if the plan was found to have provided the creditor with "the indubitable equivalent of his claim."[46]

The Eighth Circuit then set forth a three-step procedure for determining whether a debtor's proposal for adequate protection has satisfied the "indubitable equivalence" standard:

> In any given case, the bankruptcy court must necessarily (1) establish the value of the secured creditor's interest, (2) identify the risks to the secured creditor's value resulting from the debtor's request for use of cash collateral, and (3) determine whether the debtor's adequate protection proposal protects value as nearly as possible against risks to that value consistent with the concept of indubitable equivalence.[47]

In employing its three-step analysis, the court found that in approving the Martin's proposal, the bankruptcy court had failed to correctly establish the value of CCC's interest.[48] On remand, the bankruptcy court was in-

---

46. *In re* Martin, 761 F.2d at 476 (quoting *In re* Monnier Bros., 755 F.2d 1336, 1338 (8th Cir. 1985)). Perhaps one of the major reasons for the dichotomy noted in the text is that *Monnier Brothers* is clearly distinguishable on its facts. In *Monnier Brothers*, an over-secured creditor appealed from a judgment of the United States District Court for the District of South Dakota. *In re* Monnier Bros., 755 F.2d at 1337. The judgment modified and affirmed the bankruptcy court's confirmation of the debtor's reorganization plan, which had been affirmed by the bankruptcy court over the objections of the secured creditors. *Id.* The main issue in *Monnier Brothers* was what interest rate would insure that an over-secured creditor would receive any remaining unpaid principal plus any accrued contract rate of interest, when the creditor was holding an accelerated real estate mortgage claim against the land of a bankrupt debtor. *Id.* at 1338.

The Eighth Circuit Court of Appeals relied on 11 U.S.C. section 1129 in its ruling in *Monnier Brothers*. *Id.* Chapter 11 U.S.C. section 1129(b)(2)(A)(iii) provides that "a plan of reorganization may be confirmed over the objections of a secured creditor if the plan affords the creditor the 'indubitable equivalent' of his claim." 11 U.S.C. section 1129(b)(2)(A)(iii); In re Monnier Bros., 755 F.2d at 1338.

Hence, the focus of the court in *Monnier Brothers* was different from that in *Martin* in three important aspects: first, the land securing the mortgage in *Monnier Brothers* was in existence at the time the plan was submitted, unlike the unplanted crop in *Martin*; second, the court was construing the language of 11 U.S.C. section 363 in *Martin*, and the language of 11 U.S.C. section 1129 in *Monnier Brothers*; and third, the creditor in *Monnier Brothers* was over-secured, the issue being essentially only an equitable interest rate, whereas in *Martin*, there was potential that the creditor was *under*-secured, and the issue was essentially whether a plan submitted by the debtor rectified the situation.

47. *In re* Martin, 761 F.2d at 476-77.

48. *Id.* at 477. The court noted that although the Martins' computations showed that the value of the lien offered on the 1984 crop was in excess of the amount of cash collateral they sought, their calculations failed to consider expected future market prices, and did not include evidence of past proven yields. *Id.* The *Martin* court stated that the expected market price at the time of the 1984 harvest was an essential factor in calculating the value of the 1984 crop. *Id.* The value of the 1984 crop in turn was required in order to determine whether a security interest in that crop would provide the CCC with the indubitable equivalent of the grain already harvested. *Id.*

structed that it could consider an interest award to reduce the risk to the CCC's secured interest associated with fluctuating market prices, and to compensate the CCC for any delay in repayment due to the Martins' proposal for use of the secured collateral.[49]

The *Martin* court further found that the bankruptcy court had failed to adequately identify the risks to the CCC's value connected to a crop not yet in existence.[50] On remand, the Eighth Circuit provided a list of risk factors for the bankruptcy court to examine in making this evaluation.[51]

In sum, the bankruptcy court was instructed on remand to apply the three-step analysis outlined by the Eighth Circuit for determining whether the Martins' proposal provided the CCC with adequate protection consistent with the indubitable equivalence standard of "such relief as will result in the [creditor's] realization of value."[52] If the tests were met, the Martins' request for the use of the CCC's collateral was to be granted.[53] If the tests were not met, but the Martins' proposal could be modified to meet the "indubitable equivalence" standard while remaining beneficial to them, the

---

49. *Id.* The *Martin* court noted that, by analogical reasoning, an interest award had been required in *Monnier Brothers* to protect a mortgagor's bargained-for value under a plan of reorganization. *Id.* (citing *In re* Monnier Bros., 755 F.2d at 1338-40).

50. *Id.* The Eighth Circuit took note of the fact that a crop failure due to anything other than "unavoidable consequences" within the definitions of the Martins' federal crop insurance policy would destroy protection of the CCC's interest. *Id.* In addition, the court found that "the policy itself disclaims any liability for crop failure resulting from the farmer's neglect or failure to follow good husbandry practices." *Id. See also supra* note 4.

51. *Id.* Noting that the list was "by no means exclusive, but merely illustrative," the considerations listed were:

> anticipated yield in light of the productivity of the land; the husbandry practices of the farmer, including his proven crop yields from previous years; the health and reliability of the farmer; the condition of the farmer's machinery; whether there are encumbrances on the machinery which may subject it to being repossessed before the crop is harvested; the potential encumbrances on the present or future crop by other secured creditors; the availability of crop insurance and the risk of crop failure not covered by the crop insurance; and the anticipated fluctuation in market price of the farmer's crop.

Id.

52. *Id. See also id.* at 477 (quoting *In re* Sheehan, 38 Bankr. 859, 864 (Bankr. D.S.D. 1984)).

53. The bankruptcy court was to consider the value of the CCC's interest in light of the risks arising from the Martins' proposal. *See supra* notes 47 & 51 and accompanying text. The bankruptcy court was then required to determine whether the Martins' proposal adequately protected the value of the CCC's interest under the indubitable equivalent standard. *See supra* text accompanying note 52. The *Martin* court stated that:

> If the debtor's proposal provides adequate protection, the request for use of cash collateral should be granted by the bankruptcy court. If the debtor's proposal can be modified to provide for adequate protection while still remaining useful to the debtor, the debtor's request should be granted under the modified plan. If adequate protection cannot be afforded under any circumstances, the debtor's request for use of cash collateral should be denied by the bankruptcy court.

In re Martin, 761 F.2d at 477-78.

modified plan was to be approved.[54] If adequate protection could not be afforded the CCC *under any circumstances*, however, the Martins' proposal was to be denied by the bankruptcy court.[55]

The language of the last alternative for the bankruptcy court's consideration on remand indicates a position of extreme deference to a debtor's adequate protection proposal.[56] Before a district court is to reject a debtor's adequate protection proposal, the court must find that adequate protection of the value of the secured party's interest could not be afforded under any circumstances even if the plan were amended.[57]

Permitting a debtor to use the proceeds from the sale of secured collateral, if the secured creditor can be adequately protected in *some* conceivable set of circumstances, may very well be an attempt by the Eighth Circuit to keep debtors from being permanently precluded from using such cash collateral. As noted previously, the issue of adequate protection is a question of fact,[58] which the Eighth Circuit subjects to very limited review on appeal.[59] It therefore follows that a debtor deemed unable to provide adequate protection at the district court level within the Eighth Circuit has little hope of a reprieve at the appellate court level.

Moreover, the *Martin* opinion is significant because it suggests a possible trend among the courts within its jurisdiction. The *Martin* decision indicates an increased willingness by the Eighth Circuit Court of Appeals to grant the lower courts in the circuit vast discretion in determining whether adequate protection has been provided to a secured creditor. This discretion is manifested when the courts apply the indubitable equivalence standard to the issue of adequate protection, rather than conditioning or prohibiting the sale of secured collateral upon the request of the secured creditor.[60] Because a court may confirm an adequate protection proposal over the objections of the secured creditor, a secured creditor can no longer be certain of the value of his bargain after the execution of a security agreement. The secured creditor therefore suffers a significant increase in risk because he lacks control over the value of his bargain with the debtor. In essence, the secured creditor is at the mercy of the court should the court choose to apply the indubitable equivalence standard.

By treating the lower court holdings as conclusions of fact, the eighth circuit has essentially permitted the lower courts within its jurisdiction to substitute their concept of an "indubitable equivalent" of the value of a secured creditor's bargain for the creditor's understanding of the value he bar-

---

54. *See supra* note 53.
55. *Id.*
56. *Id.*
57. *See, e.g., supra* note 53.
58. *See supra* note 23 and text accompanying notes 19-23.
59. *See supra* note 23 and accompanying text.
60. *See supra* note 46 and accompanying text.

gained for when he entered into the security agreement with the debtor. Because this scheme is treated as a conclusion of fact, the secured party has little chance of successfully challenging a finding of adequate protection on appeal to the Eighth Circuit.[61] The end result is that the secured creditor has little input as to what value should be adequately protected.

Hence, there is potential for an adequate protection decision prejudicial to the secured creditor or detrimental to his interest any time a court applies the indubitable equivalence standard. As a result, the secured party will be subjected to an increased risk of uncollectability when a court allows the use of secured collateral in any case. In *Martin*, the Eighth Circuit was alert to these potential problems and attempted to set guidelines which balanced with these problems the importance of maintaining flexibility in the application of adequate protection standards.[62] These guidelines are intended to promote the use of business reorganization provisions, while at the same time protecting the secured creditor's interest.[63]

In the wake of the *Martin* decision, the secured creditor must accept all of the risk associated with allowing the debtor to use secured collateral, while having only minimal input into the protection and disposition of the collateral, as noted above.[64] When looking to *Martin* for guidance in ruling upon an adequate protection issue, courts would do well to keep in mind "the Congressional goal of affording the secured creditor the benefit of *his* bargain."[65]

August B. Landis

61. *See supra* note 23 and text accompanying notes 19-23.
62. *See supra* notes 18-19 and accompanying text.
63. *In re* Martin, 761 F.2d at 476.
64. *See supra* text accompanying note 59.
65. *See supra* note 35.