Dated: September 19, 2007
The following is SO ORDERED:

David S. Kennedy
UNITED STATES CHIEF BANKRUPTCY JUDGE

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF TENNESSEE
WESTERN DIVISION

In re

CORNERSTONE-CAMERON & STONEGATE, INC.	Case No. 07-27849-DSK
Debtor.	Chapter 11

ORDER RE THRESHOLD ISSUES ARISING OUT OF CHAPTER 11 DEBTOR'S "MOTION FOR ENTRY OF ORDER (A) AUTHORIZING DEBTOR TO USE CASH COLLATERAL ON AN INTERIM BASIS (B) PROVIDING FOR ADEQUATE PROTECTION WITH REGARD THERETO AND (C) SETTING A FINAL HEARING DATE ON THE DEBTOR'S FINAL USE OF CASH COLLATERAL" COMBINED WITH RELATED ORDERS AND NOTICE OF THE ENTRY THEREOF

INTRODUCTION

The instant contested matters, pursuant to FED. R. BANKR. P. 9014, are before the court on a motion filed under 11 U.S.C. § 363(c)(2)(B) and FED. R. BANKR. P. 4001(b) by the above-

named chapter 11 debtor in possession, Cornerstone-Cameron & Stonegate, Inc. ("Debtor" or "Debtor-in-Possession"), a not-for-profit corporation, who operates two multifamily residential rental apartment complexes located in Memphis, Tennessee and also on the objection thereto filed by the Bank of New York Trust Company, N.A., in its capacity as successor indenture trustee ("Bank"). The apartment complexes themselves are commonly known as "Autumnwood Apartments" and "Stonegate Apartments" (hereinafter collectively referred to as the "Properties"). The Properties are professionally managed by Equity Management, Inc., the Debtor's agent.

These bifurcated matters before the court arise out of the prior motion filed by the Debtor on September 6, 2007; the motion is styled, *Motion for Entry of Order (A) Authorizing Debtor to Use Cash Collateral on an Interim Basis (B) Providing for Adequate Protection with Regard Thereto and (C) setting a Final Hearing Date on the Debtor's Final Use of Cash Collateral* ("Motion to Use Cash Collateral"). Pursuant to this motion, the Debtor ultimately seeks entry of two orders. The first interim order sought by the Debtor would be to approve the use of cash collateral and the proposed adequate protection on a preliminary basis and to schedule a final hearing on the ultimate relief requested in the motion. The second order would be a final order upon the conclusion of the future and final hearing on the matter. 11 U.S.C. § 363(c)(2)(B); FED. R. BANKR. P. 4001(b). The Debtor preliminarily asserts that the rents received from the individual units of the Properties are property of the § 541(a) estate and also are cash collateral under 11 U.S.C. § 363(a) from the Properties which the Debtor operates through its agent, the professional management company. As will be seen here, the Bank initially opposed the Debtor's motion to use the rental revenues asserting that the rents were absolutely and unconditionally assigned to it prior to the filing of the chapter 11 case; and accordingly, the rents are not property of this chapter 11 case and are not subject to use by the Debtor. The Bank subsequently raised a new theory that the rents from the apartment complexes are the corpus of an express contract trust, and therefore, the rents are not property of the estate. The parties have requested the court, and the court has agreed, to conduct a bifurcated hearing to address these threshold issues involving the dichotomy between an absolute assignment of rents and an assignment of rents as additional collateral and also the issue involving the express trust theory raised later by the Bank. A bifurcated hearing was held on September 13, 2007 to address these threshold issues.

By virtue of 28 U.S.C. § 157(b)(2)(A), (K), (M), and (O) these are core proceedings. This court has jurisdiction of these matters under 28 U.S.C. §§ 1334 and 157(a) and Miscell. Order No. 84-30 (W.D.Tenn.). Based on all of the pleadings, exhibits, statements of counsel, and consideration of the case record as a whole, the court makes the following findings of fact and conclusions of law in accordance with FED. R. BANKR. P. 7052.

FINDINGS OF FACT

This bifurcated ruling addresses only the threshold issues involving whether the rents from the Properties, taking into consideration all of the underlying documentation, were absolutely assigned to the Bank before the commencement of the chapter 11 case, or whether the rents instead are additional collateral as security for the Bank; and what effect, if any, the existence of an express contract trust has on the Debtor's right to collect and use the rents in accordance with the underlying documents arising out of the parties' legal relationships. These threshold issues, as requested by the parties, should be decided before any further issues are addressed, and as such the parties have agreed to bifurcate the hearing to allow the court to decide these highly important threshold issues first before proceeding further with the case and estate administrations.

Although the parties have a difference of opinion regarding the outcome of these threshold bifurcated issues, nonetheless, the relevant background facts seemingly are not in substantial dispute and may be briefly summarized as follows. As noted, the Debtor is a not-for-profit corporation formed under applicable Tennessee law. Debtor is the leasehold owner and operator of two apartment complexes (*i.e.,* the Properties" located in Memphis, Tennessee). The Bank states, *inter alia,* that it is the successor indenture trustee under a certain trust indenture initially entered into on October 1, 1997, by First Tennessee and the Health, Educational and Housing Facility Board of the County of Shelby ("County" or "Issuer"), as amended from time to time, which authorized the issuance of up to $23,000,000 of multifamily housing revenue bonds to finance the acquisition and rehabilitation of the Properties. The Bank also asserts that as of June 30, 2007, the aggregate outstanding principal balance of the Bonds is approximately $19,580,000, plus interest due and owing and administrative expenses and fees; that the aggregate amount of accrued interest due and owing is $2,391,540; and that interest began accruing on July 1, 2005, and continues to accrue

at the per diem rate of $3,321.58.

To support its legal positions, the Bank submitted three documents to the court. The first document is entitled "Trust Indenture Between the Health, Education and Housing Facility Board of the County of Shelby, Tennessee and First Tennessee Bank National Association, Memphis, Tennessee, Trustee" and a supplement thereto (collectively the "Trust Indenture"). The second document is entitled "Lease Agreement Between the Health, Education and Housing Facility Board of the County of Shelby, Tennessee and Cornerstone-Cameron and Stonegate, Inc." ("Lease Agreement"). The final documents that were submitted as a single exhibit and are the most helpful to the decision at hand; they are the documents entitled "Deed of Trust, Security Agreement, Assignment of Leases and Rents and Fixture Financing Statement from The Health, Education and Housing Facility Board of the County of Shelby, Tennessee, as Issuer, and Cornerstone-Cameron and Stonegate, Inc., as Lessee to Percy Harvey, as Deed of Trust Trustee" (collectively "Deeds of Trust"). These final documents are essentially duplicates except that one refers to the property at Stonegate Apartments and the other refers to the property at Autumnwood Apartments.

Pursuant to the deeds of trust executed by the parties thereto on October 1, 1997, the Bank initially asserted in this chapter 11 case that the rents realized from the Properties were absolutely and unconditionally assigned and transferred to it. A license agreement also was created in the deed of trust conferring upon the Debtor a duty to collect and apply rental income and revenues to service the debt. *See* Exhibit C; Section 5.1, page 26 of the Deeds of Trust stating as follows: "[L]essee shall have a license, without joinder of Beneficiary . . . to enforce the Leases and to collect the Rents as they come due and to retain, use and enjoy the same . . . ." The Debtor, through its professional property manager, collects the rents, manages the operation of the Properties and makes debt service payments to the Bank with the revenues generated by the Properties. Apparently no debt-service payments have been made to the Bank for at least the 24 months prior to the filing of this chapter 11 case.

On July 9, 2007, the Bank commenced a civil action in the United States District Court for the Western District of Tennessee seeking the appointment of an equity receiver to collect the rents, market, and sell the Properties for the benefit of its Bondholders. Bank believes it is in an undersecured status (*i.e.*, the Properties are worth less than the outstanding debt). On August 20, 2007, the Debtor filed this chapter 11 case shortly before the scheduled status

conference hearing before the U.S. District Court for the Western District of Tennessee was to be held to address the appointment of an equity receiver that was set for the same day as the filing of this chapter 11 case. The Debtor, through its professional property manager, continues after the chapter 11 case to collect the rents. The Debtor is operating the Properties through its professional agent awaiting the outcome of a final ruling here on these threshold issues.

The Bank first asserted in these proceedings that under the existing circumstances and applicable law the Debtor had no legal rights to the rents realized from the Properties since the Debtor absolutely assigned such rents and profits generated from the Properties to the Bank prior to the filing of the chapter 11 case as set forth in the deeds of trust. The exhibits attached to the Bank's pending motion to dismiss this case or alternatively for relief from the automatic stay, case abstention, or proceeding abstention reveals that the deeds of trust, as a whole, were purportedly "absolutely assigned" in multiple places; however, the Debtor's participation in any assignment occurred only in the deed of trust instrument.

The Bank filed a supplement to its previously filed motion, styled "Supplement to the Bank of New York Trust Company, N.A.'s Motion to Dismiss and Objection to Debtor's Motion For, Among Other Things, Entry of Order Authorizing Debtor to Use Cash Collateral on an Interim Basis." In the Bank's supplement, the Bank advanced its new argument that the parties' documents had created a prepetition express contract trust within the lease agreement requiring the Debtor to hold the rents in trust for the benefit of the Bank and that the express trust "trumped" the assignment provisions whether such provisions are absolute or are as additional collateral.

The Debtor, *inter alia,* asserts legal rights to the rents and profits generated by the Properties as being, for example, "cash collateral" as contemplated under 11 U.S.C. § 363(a). Relying on the assignment language in the deed of trust and its asserted and purported ambiguity taken as a whole document, the Debtor initially asserted that the contractual language only provided the Bank with additional collateral and security for the indebtedness and not an absolute assignment of rents. The Debtor suggests that the assignment language previously relied upon by the Bank conveys only a security interest in the rents in favor of the Bank. Simply stated, the Debtor primarily argues regarding the rent assignment question that the Bank cannot have it both ways. The Bank initially took the position that it obtained a

prepetition absolute assignment of the rents and that the rent assignment is separate and distinct from the security interest created within the same document as to other collateral. Moreover, the Bank, as noted earlier, now asserts that the Debtor has no right to the rents because the rents from the Properties are held in an express contract trust for the Bank.

DISCUSSION

The Bankruptcy Code very broadly defines what constitutes property of the estate as including all legal or equitable interests of the debtor in real or personal property as of the commencement of the case, wherever they are located and by whomever they are held. See 11 U.S.C. § 541(a)(1); *In re Johnston,* 209 F.3d 611, 613 (6th Cir.2000); *U.S. v. Whiting Pools, Inc.,* 462 U.S. 198, 103 S.Ct. 2309, 76 L.Ed.2d 515 (1983). Specifically, "[p]roceeds, product, offspring, rents, or profits of or from property of the estate . . . ." are expressly included in this broad definition. *See* 11 U.S.C. § 541(a)(6). It is emphasized here that a possessory interest is also property of the § 541(a) estate. *See also In re Convenient Food Mart No. 144, Inc.*, 968 F.2d 592, 594 (6th Cir. 1992) (finding that "possessory interests in real property fall within the ambit of the protections provided by the automatic stay").

"Cash collateral" is defined in 11 U.S.C. § 363(a) as "cash, negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents whenever acquired in which the estate and an entity other than the estate have an interest and includes the proceeds, products, offspring, rents, or profits of property and the fees, charges, accounts or other payments for the use or occupancy of rooms and other public facilities . . . ."

Under 11 U.S.C. § 363(c)(2), cash collateral includes only property "in which the estate and an entity other than the estate have an interest . . . ." *See, e.g., In re Kingsport Ventures, L.P.,* 251 B.R. 841, 845-46 (Bankr.E.D.Tenn.2000) (citing 11 U.S.C. § 363(a)); *see also In re 5877 Poplar, L.P.*, 286 B.R. 140 (W.D. Tenn. 2001). Thus, the property or cash collateral sought to be collected and used by the Debtor must first be classified as property of the estate under 11 U.S.C. § 541(a) before the Debtor can collect and use the rents in this case. Ordinarily, rental proceeds from apartment complexes are cash collateral and can be collected and used by the debtor in possession (or trustee) if sufficient adequate protection exists. *See, e.g., In re Epstein*, 26 B.R. 354 (Bankr. E.D. Tenn. 1982).

In order to determine whether the Debtor here may collect and use the rents in

accordance with the existing contractual provisions, the court must first address the threshold issues raised by the Bank and Debtor. For example, if the rents were held in an express contract trust or absolutely assigned to the Bank, a legal transfer of title to the rents may vest with the Bank, and arguably the Debtor has no interest in the rents; and accordingly, the rents arguably would not be property of the estate. If the rents are not property of the estate, then the rents also are arguably not "cash collateral;" the Debtor in such an event would be unable to collect and use the rents as cash collateral if the rents are held in trust or if the rents were absolutely assigned to the Bank. Whether the Debtor is able to collect and use the rents in accordance with the parties' prepetition contractual arrangements is crucial to whether the Debtor will be able to go forward and seek to meaningfully reorganize under chapter 11 of the Bankruptcy Code or liquidation in an orderly fashion in an effort to obtain a maximization of the values of the Properties. It is noted that a Congressional policy favoring reorganization over liquidation has existed in America since 1938. "The use of cash collateral from the [debtor's] security property is critical to the successful reorganization of the debtors." *In re Epstein*, 26 B.R. 354, 358 (Bankr. E.D. Tenn. 1982).

As further noted, the Bank filed a supplement to its objection to the Debtor's collection and use of the rent funds from the Properties arguing that an express contract trust exists. Pursuant to the terms of the trust mechanism, the Debtor is required to collect and hold the rent revenues in trust for the benefit of the Bank. After the Bank filed its objection to the instant motion, but before the bifurcated hearing here, the Bank discovered the express contract trust language contained in the lease agreement and the trust indenture documents. At the bifurcated hearing, the Bank argued that the trust language, in essence, "trumps" the absolute assignment clause and that legal theory. Essentially, the Bank advanced two theories upon which it can prevail: (1) that the rental proceeds were absolutely assigned to the Bank; and (2) that the rental proceeds were to be held in an express contract trust for the benefit of the Bank. The court will address each theory in turn as follows.

Absolute Assignment of Rents/Assignment of Rents as Additional Collateral Dichotomy

Issues regarding the dichotomy involving absolute assignment of rents or an assignment of rents as additional collateral have been lurking "[f]or more than one hundred years . . . caus[ing] confusion, increased transaction costs, litigation, and in some cases

injustice." Julia Patterson Forrester, *Still Crazy After All These Years: The Absolute Assignment of Rents in Mortgage Loan Transactions*, 59 FLA. L. REV. 487, 488 (2007). Both state courts and bankruptcy courts seemingly have struggled with the "characterization of an absolute assignment of rents as a transfer of title to rents or a security interest." *Id*. at 519-20. In technical form, an absolute assignment of rent is a transfer of legal title. In substance, however, the absolute assignment of rents may in reality and law operate as a security interest, after sifting through the form. An assignment of rents as additional collateral is a different or special type of security interest. In that sense, a true absolute assignment is akin to a legal fiction. *See Fed. Deposit Ins. Corp v. Int'l Prop. Mgmt., Inc.*, 929 F.2d 1035, 1033 (5th Cir. 1991); Forrester, *The Absolute Assignment of Rents in Mortgage Loan Transactions*, 59 FLA. L. REV. at 513.

Understandably, a finding that a debtor has absolutely assigned its interest in rents has serious factual and legal consequences. An effective absolute assignment of rents, in essence and as a practical matter, strips the debtor's ability to collect and use rents and obtain meaningful chapter 11 relief; this result summarily thwarts and otherwise frustrates the rehabilitative goal and policy of Congress favoring rehabilitation over liquidation in bankruptcy. Professor Julia Patterson Forrester further explains:

> Bankruptcy courts holding that an absolute assignment of rents gives a lender ownership of rents rather than a security interest are simply incorrect. Although the form of the transaction may indicate a transfer of title to rents, the substance of such a transaction is a security interest. Some of these courts are following state law precedent on the theory that property rights are a matter of state law. They should however, 'look to the substance of state law rights, not merely the label that state law places on them.'
>
> The better-reasoned bankruptcy opinions look to the substance of the transaction and to factors such as the borrower's right to collect rents until default, the lender's obligation to apply rents to payment of the debt, and the termination of the assignment of rents upon payment of the loan in full. If the borrower has any remaining property rights in the rental stream under state law, bankruptcy law dictates that the rental stream be treated as part of the bankruptcy estate.
>
> When a court holds that rents covered by an absolute assignment are owned by the lender, the debtor-in-possession does not have the rents available for operation and maintenance of the mortgaged property, as would be the case if rents were treated as cash collateral. If rents are unavailable for operation and maintenance of the property, almost no hope of reorganization exists for a borrower in Chapter 11. If the debtor has no

> equity in the property and there is not 'a reasonable possibility of a successful reorganization within a reasonable time,' the lender is entitled to relief from the automatic stay. Therefore, the borrowers' efforts to reorganize under the protection of Chapter 11 will be frustrated even in those cases where a reorganization might otherwise have been successful. This result defeats the policies behind the Bankruptcy Code and Chapter 11, is simply an injustice.

Forrester, *The Absolute Assignment of Rents in Mortgage Loan Transactions*, 59 FLA. L. REV. at 520-22 (citations omitted). Consequently, a finding that an assignment of rents is absolute should require a clear showing that the parties so intended. *Federal Deposit Ins. Corp. v. Int'l Prop.,* 929 F.2d 1033, 1036, 1038 (5th Cir. 1991) (explaining that courts ordinarily are reluctant to construe assignments as absolute, especially when such a result fails to reflect the intent of the parties).

A judicial determination of whether an absolute assignment occurred in this case requires analysis of the underlying assignment itself and the intent of the parties on a case-by-case basis. "When the lender has received a purported absolute assignment of rents, careful review of the intent and practices of the parties and of applicable nonbankruptcy law will be appropriate to determine whether the assignment is truly absolute or is absolute only in form." 3 Collier on Bankruptcy ¶ 363.03[3] (15th ed.1997); *In re Turtle Creek,* 194 B.R. 267 (Bankr. N.D. Ala.1996); *In re Dacey,* 80 B.R. 206 (D.Nev.1987).

Assignments of rents are interests in real property requiring an examination of the details of their creation and a definition in accordance with law of the situs of the property or state law where the property is located. *In re Jason Realty, L.P.,* 59 F.3d 423, 427 (3rd Cir.1995) (citing *Butner v. United States,* 440 U.S. 48, 55, 99 S.Ct. 914, 59 L.Ed.2d 136 (1979)). Bankruptcy courts, however, are not, *ipso facto,* necessarily bound by the parties' labels contained in contractual language; the court, especially as an equity court, may look behind the mere labels designated by the parties and look to the substance of the matter. *Compare and see, for example, Long v. Calhoun (In re Calhoun)*, 715 F.2d 1103, (6th Cir. 1983) (finding that bankruptcy court should look behind language of the parties' or trial judge's characterization of a loan assumption). In fact, a bankruptcy court is not compelled, in appropriate cases, to follow the parties' labeling once countervailing federal concerns are triggered. *Butner*, 440 U.S. at 55 (explaining that "[u]nless some federal interest requires a different result" bankruptcy courts are to apply state law when analyzing issues of state law,

such as property rights).

Courts in Tennessee distinguish grants of security interests and absolute assignments as two entirely distinct methods for creating credit against collateral from which a party may borrow funds. *See, e.g., In re Kingsport Ventures, L.P.,* 251 B.R. 841, 846 (Bankr.E.D.Tenn.2000) (citing *American Trust & Banking Co. v. Twinam,* 187 Tenn. 570, 216 S.W.2d 314, 319 (1948); *Nashville Trust Co. v. First Nat'l Bank,* 123 Tenn. 617, 134 S.W. 311, 314 (1911); *In re BVT Chestnut Hill Apartments, Ltd.,* 115 B.R. 116, 117 (Bankr.M.D.Tenn.1990); *In re Harbour Town Assocs., Ltd.,* 99 B.R. 823, 824 (Bankr.M.D.Tenn.1989)). Tennessee, however, recognizes the presumption that an assignment operates as security for a debt. *In re 5877 Poplar*, 268 B.R. 140, 146, 148; *Kingsport Ventures, L.P.,* 251 B.R. at 846-47 (acknowledging that "an assignment of rents is presumed to be a pledge of rents as security.")(quoting *Harbour Town Assocs., Ltd.,* 99 B.R. at 824; *BVT Chestnut Apartments, Ltd.,* 115 B.R. at 117). The determination of whether an assignment of rents is absolute or merely a pledge of security requires close scrutiny and a thorough analysis of the contractual language and provisions of the assignment.[1]

If a purported absolute assignment of rents also provides that the rents additionally are given as "security" or as "additional collateral," this court has found that such an assignment may not always be an absolute one. *See 5877 Poplar*, 268 B.R. at 146-47. "Statements within the assignment that the assignment was intended to secure a debt is strong evidence that the assignments are in fact a pledge of security, even if the assignment is referred to as absolute." *Kingsport Ventures, L.P.,* 251 at 847 (citing *BVT Chestnut Hill Apartments, Ltd.,* 115 at 117; *Harbour Town Assocs., Ltd.,* 99 at 825).

General principles of Tennessee contract law arguably apply here in the interpretation of an assignment clause. *Kingsport Ventures, L.P.,* 251 B.R. at 847. Courts ordinarily must interpret contracts as written, even where its terms seem harsh or unjust absent proof of fraud

[1] *Kingsport Ventures, L.P.,* 251 at 847; *see also In re JP Realty, II, Inc.*, 2003 Bankr. LEXIS 1719 *11-13 (June 5, 2003, M.D. Tenn. 2003) (explaining that there are four items that indicate an absolute assignment: (1) that the language of the assignment is clear and unambiguous and states that the assignment is not intended to be additional or collateral security; (2) that the assignment grants debtor nothing more than a revocable license in the rents; (3) that the assignment does not require the beneficiary to take any action to collect rents after an event of default; (4) that the assignment gives the beneficiary "total discretion regarding the application of rents collected by it.")

or mistake. *Gray v. Estate of Gray,* 993 S.W.2d 59, 64 (Tenn. Ct. App. 1998), *permission to appeal denied,* (Tenn.1999). It is fundamental that ambiguous language in a contract is construed against the drafter. *In re Delta America Re Insurance Co.,* 900 F.2d 890 (6th Cir.1990). Ambiguity results, under Tennessee law, when the terms in the contract may fairly be understood more ways than one. *See, e.g., Memphis Hous. Auth. v. Thompson*, 38 S.W.3d 504, 512 (Tenn. 2001) (citing *Carter v. State*, 952 S.W.2d 417, 419 (Tenn. 1997)). In this case, it appears that the Issuer was the drafter of the documents – not the Bank or the Debtor.

In *Kingsport Ventures, L.P., supra,* the assignment in question existed in an independent document entitled, "Assignment of Leases and Rents," containing paragraph headings in bold fonts (*i.e., 1. Present Assignment, 2. Remedies of Assignee, etc.*). The fact that the assignment in *Kingsport Ventures, L.P.*, existed in a separate and independent document from the mortgage instrument distinguishes this case from *Kingsport Ventures. See In re Jason Realty, L.P.,* 59 F.3d 423, 428 (3rd Cir.1995) (holding that an absolute assignment existed because an independent assignment document was executed, separate from the mortgage instrument, which "impressed" the court and facilitated the court's conclusion that rents were not estate property or cash collateral). The assignment in this case exists only in the security agreement/deed of trust.

Like the parties in *Kingsport Ventures, L.P.,* the Bank here granted the Debtor a license to collect rents in the assignment and instructions on how and when to process collected rents. The deed of trust provision grants the lessee "a revocable license to possess and control the Premises and to collect such rents, issues, and profits . . . ." This, alone, however, is not uncontroverted proof that the parties intended an absolute assignment. There are additional factors that more accurately describe the intent of the parties.

In *Kingsport Ventures, L.P.*, the beneficiary of the assignment gave the lender immediate right to possession of all rents upon written notice of default. The assignment in this case provides that upon default "the Beneficiary may, but shall not be obligated to, at any time without notice, . . . enter upon and take possession of the Premises . . . ." In the instant case, the assignment clause calls for <u>action</u> on the part of the Bank, further evidence that the assignment in this case is not absolute. Rather, the rents are actually assigned as additional security.

The assignment language in the deed of trust in this case states that the "assignment of

rents . . . will operate as a present and absolute assignment from Lessee to the Beneficiary, and not merely the passing of a collateral security interest." Deed of Trust, Art. V, section 5.1. Importantly, in this case, the assignment exists only in the security instrument/deed of trust. The assignment was not executed in a separate, independent document. Consequently, the assignment in this case bears greater resemblance to the failed purposed absolute assignment in *5877 Poplar*, 268 B.R. 140 (Bankr. W.D. Tenn. 2001). In *5877 Poplar*, this court found that the absence of a separate, independent document assigning the rents was evidence that the parties did not intend a true assignment. *In re 5877 Poplar*, 268 B.R. at 148. Instead, the parties in substance intended that the rents act as additional collateral.

The "granting clauses" in the deed of trust state that "the Lessee hereby grants to the Beneficiary a security interest in all of the Lessee's right, title and interest therein . . . namely: . . . . 6. Rents. All of the Issuer's and Lessee's right, title and interest in and to all rents, income, issues, uses, profits, proceeds . . . and products of, all replacements and substitutions for, and other rights and interest now or hereafter belonging to, any of the foregoing." Deed of Trust, Granting Clauses, pg. 3-4. This language clearly grants the Bank a security interest in the rents. Yet, in Article V, the assignment clause, of the same document, the parties attempt to create an absolute assignment. Article V states that "the foregoing assignment of rents . . . will operate as a present and absolute assignment from Lessee to the Beneficiary, and not merely the passing of a security interest . . . ." The language contained in the granting clause and in the assignment is in conflict.

The inconsistent language contained within the deed of trust prohibits this court, under the totality of the particular facts and circumstances and applicable law, from concluding that the assignment here was absolute when it concomitantly provides for the rents as, for example, additional security. Furthermore, the presumption that an assignment operates as security for a debt complicates the Bank's burden of rebutting the presumption despite the reference to the assignment as "absolute" in the deed of trust. The use of such language discussed above and the language identifying rents or premises as collateral on page 4 of the deed of trust compels the court to honor the presumption and apparent intent of the parties that the assignment serves as a pledge of security and not an absolute assignment. Thus, the Bank under this dichotomy has failed to rebut the presumption under applicable Tennessee law that the assignment of rents is presumed to be a pledge of rents as security. Accordingly,

the court at this stage of the Order must find that the rents generated and realized by the Properties constitute "cash collateral" under the broad definition contained in section 363(a) and a proper construction of 11 U.S.C. § 541(a)(1) and (6).

In summary, the court finds, considering a totality of the particular facts and circumstances and applicable law, that the rental assignment in the deed of trust fails to constitute an absolute assignment of rents; instead, it is an assignment of rents as additional collateral. (The Bank's express contract trust theory will be addressed below.)

Express Contract Trust Theory

Now, the court will address the express trust contract theory that the Bank subsequently raised in these matters. The Bank's newly discovered theory to support its position is that the express contract trust language of the parties' documents "trumps" its absolute assignment theory and, therefore, the Bank should prevail without resort to the assignment dichotomy.

Applicable State law ordinarily determines whether certain funds are held in an express trust and are excluded from the debtor's bankruptcy estate. *See Cannon v. J.C. Bradford & Co. (In re Cannon)*, 277 F.3d 838, 849 (6th Cir. 2002) (citing *Barnhill v. Johnson*, 503 U.S. 393, 398 (1992)). Under Tennessee law, three factors usually must be present in order to create an express trust: "(1) a trustee who holds trust property and who is subject to the equitable duties to deal with it for the benefit of another, (2) a beneficiary to whom the trustee owes the equitable duties to deal with the trust property for his benefit, and (3) identifiable trust property." *In re Cannon*, 277 F.3d at 850 (citations omitted). At the very least, "there must be a grantor or settlor who *intends* to create a trust; a corpus (the subject property); a trustee; and a beneficiary." *Id*. (citing *Myers v. Myers*, 891 S.W.2d 216, 218-19) (Tenn. Ct. App. 1994)) (emphasis in the original). The trustee has legal title to the trust property, while the beneficiary holds equitable title. *In re Cannon*, 277 F.3d at 850.

While the court is mindful of the formalities and requirements to create an express trust, the court, however, finds it is unnecessary here to determine definitively at this stage of the case whether the parties have actually created an express trust so as to completely exclude these rents from any use by the Debtor or its agent. The parties in this case have a unique relationship that is worth dissecting. The Bank is the indentured trustee of the Health and

Housing Facility Board of Shelby County (*i.e.*, the Issuer). The County owns the Properties, which are subject to a payment in lieu of taxes program, through money obtained from the issuance of bonds. The Bank has underwritten the bonds. The County leased the Properties to the Debtor who apparently is controlled by a national, non-profit organization. The Debtor is authorized, *inter alia,* to hire a professional management company to manage the property including, for example, the collection of rents for the Debtor and benefit of the Bank. The Debtor hired Equity Management to manage the Projects. Equity Management apparently maintains an excellent reputation with both the Debtor and the Bank.

As property manager, Equity Management, for example, collects and deposits the rents, sues tenants seeking money judgments for any unpaid rents, initiates any necessary eviction proceedings against tenants who fail to pay rent, and disburses certain funds and proceeds forwarded to it by the Bank from the previously collected rental incomes. The rent payments collected by it are to be deposited for the Bank within two days of receipt. That is, Equity Management Company, the Debtor's agent pending further order of the court, shall collect the rents, remit them within two days to the Bank, who shall remit back such rentals to Equity Management as are appropriate for disbursement in accordance with the contractual terms. Lease Agreement, Art. IV, section 4.2(a). The Bank actually disburses the funds pursuant to a so-called "waterfall" provision located in the indentured trust document. Trust Indenture, Article V, section 5.04. Equity Management, the Debtor's agent, receives a payment under the provision to cover overhead expenses and the like. *Id*. The Bank services the bond holders. Interestingly, the Debtor itself apparently receives no money pursuant to the "waterfall" provision. In substance it seems that the Debtor's only actual role in this process is that it retains the leasehold in the Properties. The Debtor, while it receives no direct monies, is obligated, however, to service the debt to the Bank from the collection of the rents by Equity Management. Exactly how the Debtor benefits from this arrangement is not totally clear to the court at this time.[2] Nonetheless, this evidently is the agreed upon contractual arrangement. Because of the nature of the parties' relationships and further because of the true character of their agreement, the court finds that it is unnecessary under these circumstances to judicially

[2] Apparently, this type of arrangement, though somewhat rare, is attractive to particular investors, in this case the bondholders, because of certain tax benefits that are not relevant to the outcome of these proceedings.

determine at this time whether the rent payments in question are actually trust funds. *Compare* FED. R. BANKR. P. 7001(2).

Assuming *arguendo* that the parties created a valid express contract trust, the Debtor still has, for example, the right to collect the rent payments realized from the Properties, through its agent, Equity Management, pursuant to the trust indenture. The parties agree that this arrangement is a "live" contract – *i.e.*, the contractual arrangement and rights have NOT been terminated at this time. Consequently, the Debtor has a right under the contractual arrangement to*, inter alia,* have its agent collect the rents and submit those rents in its possession to the Bank; and the Debtor also has the right, through its agent, to receive from the Bank the allowance for, for example, overhead expenses. These contractual rights have not been terminated and currently are in tact. *Compare* 11 U.S.C. § 365; FED. R. BANKR. P. 6006. Pending further order of the court, the parties are bound to these contractual terms and conditions including the contractually created trust in favor of the Bank – just as existed before the filing of the Debtor's chapter 11 petition.

Conclusion

Based on all the foregoing, the court finds and concludes as follows:

- Regarding the absolute assignment/assignment as additional collateral dichotomy-theory, the rental revenues realized from the two apartment complexes (*i.e.*, the Properties) are additional collateral and may be characterized as "cash collateral" under 11 U.S.C. § 363(a) which revenues, as property of the § 541(a) estate, the Debtor may, along with its agent, collect and process in accordance with the existing contractual documents. See 11 U.S.C. §§ 1107, 1108, 541(a), 362(c)(2)(A)-(B); FED. R. BANKR. P. 4001(b). That is, the Debtor's professional management company, as its agent, may collect the rents and within two days after collection transmit the rental incomes to the Bank for the latter to use and disburse to the bondholders and the Debtor c/o the professional management company in accordance with the underlying agreement.

- If the Bank's trust theory indeed "trumps" the absolute assignment/assignment as additional collateral, nonetheless, until the underlying contractual provisions are terminated or

modified by the court, the Debtor,[3] through its professional management company, may still collect the rents and within two days thereafter transmit the rental incomes to the Bank for the latter to disburse to the bondholders and the Debtor c/o its agent in accordance with the underlying agreements. Accordingly,

IT IS ORDERED AND NOTICE IS HEREBY GIVEN that hearings shall be held on October 2, 2007, at 1:00 p.m. to further consider the Debtor's instant motion and also to initially consider the Bank's pending motion seeking to dismiss this chapter 11 case under 11 U.S.C. § 1112(b) or alternatively for relief from the automatic stay under 11 U.S.C. § 362(d), for case abstention under 11 U.S.C. § 305, or proceeding abstention under 28 U.S.C. § 1334(c)(1).

IT IS FURTHER ORDERED that the Bankruptcy Court Clerk shall promptly cause a copy of this Order and Notice to be sent to the Debtor and the Bank and their attorneys; the United States Trustee for Region 8; Stephanie Cole, Esquire, 147 Jefferson, 8th Floor, Memphis, Tennessee, 38103, the attorney for Memphis Light, Gas & Water; all creditors; and other parties in interest.

[3] 11 U.S.C. § 1107(a) places a chapter 11 debtor in possession in the shoes of a chapter 11 reorganization trustee in nearly every way. The chapter 11 debtor is statutorily cloaked with the same statutory rights and powers of a chapter 11 trustee. The debtor is required to perform the functions and duties of a chapter 11 trustee with limited exemption not applicable here. 11 U.S.C. § 1106. Of course, the chapter 11 debtor, like a chapter 11 trustee, also is subject to limitations and conditions as the court prescribes. *Cf. Wolf v. Weinstein*, 372 U.S. 633, 649-650 (1963); see also 11 U.S.C. § 1108.