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**Non-Income Producing Properties that Never Operated may be Single Asset Real Estate
Under the Bankruptcy Code**

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Cite as: *Non-Income Producing Properties that Never Operated may be Single Asset Real Estate Under the Bankruptcy Code*, 15 ST. JOHN'S BANKR. RESEARCH LIBR. NO. 30 (2023).

Introduction

Section 101 of title 11 of the United States Code (the “Bankruptcy Code”) includes a definition for a single asset real estate (“SARE”). A debtor that owns SARE is subject to certain special rules. In particular, the automatic stay will be lifted, upon the request of a secured creditor as to the SARE unless the debtor has either (i) begun making payments with interest at the nondefault rate to the secured creditor or (ii) has filed a plan of reorganization which has a reasonable possibility of being confirmed within a reasonable period of time.¹ This article addresses whether a property that never operated and never produced any income may be SARE. Part I examines the three elements of SARE set forth in the statute and will briefly consider the challenges courts face when applying them. Part II discusses case law that indicates when non-income producing properties that never operated may be SARE. Part III illustrates case law that suggests circumstances where courts may arrive at the opposite outcome.

I. Single Asset Real Estate is Comprised of Three Elements.

Section 101(51B) of the Bankruptcy Code defines SARE as:

“[1] real property constituting a single property or project, other than residential real property with fewer than 4 residential units, [2] which generates substantially

¹ See 11 U.S.C. § 362(d)(3) (2018).

all of the gross income of a debtor who is not a family farmer [3] and on which no substantial business is being conducted by a debtor other than the business of operating the real property and activities incidental thereto.”²

The burden to prove whether a property is SARE rests with the secured creditor seeking to have the stay lifted based on a preponderance of evidence standard.³ Courts have concluded that the SARE elements are “ambiguous” because they do not account for developing, non-income producing properties.⁴ Consequently, courts are tasked with applying the SARE elements on a “case by case” basis.⁵ In analyzing SARE status, courts will often consider “(1) the use of the properties; (2) the circumstances surrounding the acquisition of the properties . . . ;(3) the location of the properties and proximity of the properties to one another; and (4) any plans for future development, sale or abandonment of the properties.”⁶

II. Non-Income Producing Properties that Never Operated *can* be SARE.

A. Courts favor SARE designations on real property under construction.

In *In re Source Hotel*, a district court held that a hotel under construction that never previously operated was SARE.⁷ There, the parties did not dispute that the hotel fulfilled the first SARE element because the hotel under construction was a single project.⁸ However, the parties disagreed as to (i) whether the hotel generated substantially all of the debtor’s gross income and (ii) whether the debtor conducted any substantial business other than operating real property.⁹ As to the former, the court was persuaded by the holding in *In re Oceanside* that found that

² 11 U.S.C. § 101(51B); see *In re Scotia Pac. Co.*, 508 F.3d 214, 220 (5th Cir. 2007) (dividing the statute into elements); *In re Philmont Dev. Co.*, 181 B.R. 220, 223 (Bankr. E.D. Pa. 1995).

³ See *In re Alvion Props., Inc.*, 538 B.R. 527, 532 (Bankr. S.D. Ill. 2015).

⁴ See *In re CBJ Dev.*, 202 B.R. 467, 471 (B.A.P. 9th Cir. 1996); *In re Source Hotel, LLC*, 606 F. Supp. 3d 952, 963 (C.D. Cal. 2022) (explaining that ambiguity in the statute is “demonstrated by the fact that reasonable courts . . . have disagreed about whether [undeveloped or partially developed real property] ‘generates substantially all of the gross income’ of a debtor who has no income”).

⁵ See *In re CBJ Dev.*, 202 B.R. at 471.

⁶ *In re Hassen Imports P’ship*, 466 B.R. 492, 514 (Bankr. C.D. Cal. 2012).

⁷ *In re Source Hotel, LLC*, 606 F. Supp. 3d at 963.

⁸ See *id.* at 962.

⁹ See *id.* at 957, 961.

“undeveloped land that generates no income” was SARE.¹⁰ As to the latter, the *Source Hotel* court held that the present tense used in the SARE statute (i.e., “is being conducted”) meant the analysis should be determined in the present.¹¹ There, the hotel was not then conducting business or operating.¹² The lack of business or operations at the time, however, did not preclude the property from being SARE.¹³ Instead, according to the court, non-income producing properties that never operated qualify as SARE.¹⁴

The Bankruptcy Court for the District of New Jersey established a high bar for construction projects to prove they conduct more than “incidental activities” under the SARE statute.¹⁵ In *In re Kara Homes, Inc.*, affiliated debtors were in the business of acquiring and developing lands to sell single-family homes.¹⁶ The development of these homes included development plans, designs, and marketing fees.¹⁷ Each property was managed individually, while all employees were employed by Kara Homes.¹⁸ Finally, all individual developments shared common spaces, amenities, and roadways.¹⁹ Based on these facts, the construction lenders filed a motion to lift the automatic stay arguing that the property was SARE.²⁰ The debtors, in turn, sought denial of SARE status on the grounds that they were conducting “substantial other business” other than incidental activities towards managing real property.²¹ However, the court disagreed and held the activities involved in the development of each SARE property were

¹⁰ *See id.* at 958; *see In re Oceanside*, 192 B.R. 232, 234 (Bankr. S.D. Cal. 1996) (“If the debtor has no income, then substantially all of its income could be said to be generated by the property . . . [i]f the debtor has no ‘gross income’, then the debtor is obviously not conducting ‘substantial business’ on the property, or anywhere else for that matter.”).

¹¹ *See In re Source Hotel, LLC*, 606 F. Supp. 3d at 962.

¹² *See id.* at 963.

¹³ *See id.*

¹⁴ *See id.*

¹⁵ *See In re Kara Homes, Inc.*, 363 B.R. 399, 405 (Bankr. D.N.J. 2007); 11 U.S.C. § 362(d)(3).

¹⁶ *See* 363 B.R. at 405.

¹⁷ *See id.*

¹⁸ *See id.*

¹⁹ *See id.*

²⁰ *See id.* at 402.

²¹ *See id.*

merely incidental to the collection of revenue from the sale of the single-family homes.²²

Therefore, the court in *In re Kara Homes* favored granting SARE designations to construction projects and established a significant threshold for surpassing the statutory definition of conducting “incidental” business.²³

B. Intentions to develop another project on land that is SARE may be insufficient to avoid a SARE designation.

Additionally, courts have continuously held that SARE includes “raw, undeveloped land” when the debtor has only “intentions” to develop multiple projects on the property.²⁴ In *In re Sargent Ranch, LLC*, the debtor owned “6,400 acres on 14 separate parcels of land” with development plans “includ[ing] sand excavation, wildlife habitat, mitigation, liquid asphalt extraction, solar energy production and others.”²⁵ However, none of these plans had commenced, and the debtor’s sole income from the property was from a cell tower lease, a cattle grazing lease, and a hunting lease.²⁶ The court concluded the debtor’s property was SARE because it found no case law holding vacant property to not be SARE, and the three leases did not substantiate conducting significant business other than the operation of real estate.²⁷

III. Non-Income Producing Properties that Never Operated *may not* be SARE.

A. Non-income producing properties that suspended substantial other business activity on the subject property may not be SARE.

²² *Id.* at 406. (“[A] ‘single asset real estate’ case is one in which the debtor performs functions intrinsic to owning and developing the real estate and not one where the debtor generates income from other activities not incidental thereto.”).

²³ *See* 11 U.S.C. § 362(d)(3).

²⁴ *See In re Humble Place Joint Venture*, 936 F.2d 814, 819 (5th Cir. 1991); *In re Sargent Ranch, LLC*, 10-00046-PB11, 2010 WL 3189714, at *3 (Bankr. S.D. Cal. Aug. 6, 2010) (“[I]ntentions do not constitute projects.”); *In re Webb MTN, LLC*, 07-32016, 2008 WL 656271, at *6 (Bankr. E.D. Tenn. Mar. 6, 2008) (holding a development plan that would not have been SARE once it was constructed was SARE because the plan had not yet come to fruition).

²⁵ *See In re Sargent Ranch, LLC*, 2010 WL 3189714, at *1.

²⁶ *See id.*

²⁷ *See id.* at *4.

The United States District Court for the Eastern District of Virginia held that a property that had temporarily halted operations that would otherwise negate SARE status was not SARE because those operations were only temporarily inoperative.²⁸ In *In re CBJ Dev.*, a sixty-three room, full-service hotel could not qualify as SARE because the hotel provided amenities such as maid and linen services.²⁹ Additionally, maintaining a gift shop, restaurant, and bar on the property amounted to conducting “substantial other business activity” on the property—even though they were inoperative.³⁰ The fact that the stores were temporarily closed for renovation was not sufficient to evidence a lack of business activity, especially because the debtor intended to reopen when renovations were complete.³¹

B. A non-income producing property that shares operations with another property may not be SARE.

The United States Bankruptcy Court for the Central District of California held “non-contiguous” real properties are not SARE unless together, they function under a “common scheme.”³² Moreover, the court emphasized the difference between “common ownership” and a “common [property] border.”³³ In this case, the debtor was involved in the acquiring, developing, and leasing of ten properties across two cities.³⁴ However, the court explained that “the exclusion of any property from the common scheme precludes a finding that a single project exists.”³⁵ Some of the debtor’s properties operated while others did not.³⁶ This fact alone

²⁸ See *In re CBJ Dev.*, 202 B.R. 467, 470 (B.A.P. 9th Cir. 1996).

²⁹ See *id.*; but cf. *In re LDN Corp.*, 191 B.R. 320, 325 (Bankr. E.D. Va. 1996) (holding that a motel is SARE).

³⁰ See *In re CBJ Dev.*, 202 B.R. at 472.

³¹ See *id.*

³² *In re Hassen Imports P’ship*, 466 B.R. 492, 507–08 (Bankr. C.D. Cal. 2012); *In re Philmont Dev. Co.*, 181 B.R. 220, 224 (Bankr. E.D. Pa. 1995).

³³ *In re Hassen Imports P’ship*, 466 B.R. at 508 (opining the fact that the properties owned by the debtor had a common president was not dispositive in proving all properties were a “single project”).

³⁴ See *id.* at 496.

³⁵ *Id.* at 510.

³⁶ See *id.*

sufficed to demonstrate the properties were not part of the same common scheme.³⁷ Moreover, the court explained that debtor’s acquisition of the properties “at different times for different purposes” suggests they should not be regarded as a single project pursuant to the statute.³⁸ Therefore, courts will not conclude that non-contiguous properties with the same owner are SARE if all properties do not function in unity under a common scheme.³⁹

C. *Courts may decline SARE status on a property when there have been only minimal efforts to fulfill development plans.*

The United States Bankruptcy Court for the Southern District of Illinois emphasized not “every instance [of] raw land awaiting potential development is a ‘single project’.”⁴⁰ In *In re Alvion Properties, Inc.*, the debtor owned two different properties, a mineral tract and a fee simple tract, which had been out of operation for approximately eight years before the debtor filed for Chapter 11 bankruptcy.⁴¹ The debtor had previously expressed its plans to develop multiple projects on the subject property, however, none of them came into fruition.⁴² The court could not base its analysis off the debtor’s speculative plans because the debtor must “ha[ve] at least begun the efforts necessary for the development of a plan.”⁴³ Here, the court declined to find a non-income producing property that previously operated was SARE because the debtor’s real property was comprised of two properties that did not constitute a “single project.”⁴⁴ The court’s analysis, however, indicates that if a non-income producing property takes minimal steps

³⁷ *See id.*

³⁸ *Id.* at 512.

³⁹ *Cf. In re Aspen Club & Spa, LLC*, Nos. 18-14158-JGR, 19-14200-JGR, 19-14158-JGR, 2019 Bankr. LEXIS 2825, at *3 (Bankr. D. Colo. July 23, 2019) (holding that a tennis and racket club that operated condominiums, townhouses, affordable housing, personal training, sports medicine, salon, food and beverage services, and other amenities on the same property were SARE because they served a “single project”).

⁴⁰ *In re Alvion Props.*, 538 B.R. 527, 535 (Bankr. S.D. Ill. 2015) (refusing to expand the statutory definition of SARE); *see also In re Scotia Pac. Co.*, 508 F.3d 214, 225 (5th Cir. 2007) (emphasizing the need to adhere to the language of the SARE statute).

⁴¹ 538 B.R. at 529.

⁴² *See id.* at 536.

⁴³ *Id.* (“While the Debtor may have every intention of developing multiple projects on the property, the evidence proves that those intentions are at best speculative and have not come to fruition.”).

⁴⁴ *Id.*

towards a project that would otherwise bar the debtor from being SARE, then it may be enough to overcome a movant's SARE petition.⁴⁵

IV. Conclusion

A SARE is a non-residential property with less than four units that serves as the main source of income of the debtor and has no other operations on the property other than those incidentally related to the operation of the property.⁴⁶ SARE may also include a non-income producing property that never operated. Courts are likely to find such property to be SARE when there are no more than mere intentions to develop other projects on the property.⁴⁷ Moreover, if any other activity exists on the subject property, the threshold to surpass the SARE statute's definition of "incidental activities" is substantial.⁴⁸ Additionally, nothing more than "minimal efforts" to begin development of other projects will likely be insufficient to avoid a SARE finding.⁴⁹ A court is more likely to find that a non-income producing property is not SARE if substantial other business on the property has only been temporarily halted.⁵⁰ Likewise, a non-income producing property that shares operations with another property may not be SARE.⁵¹

⁴⁵ *See id.*

⁴⁶ *See* 11 U.S.C. § 101(51B).

⁴⁷ *See In re Sargent Ranch, LLC*, 10-00046-PB11, 2010 WL 3189714, at *2 (Bankr. S.D. Cal. Aug. 6, 2010).

⁴⁸ *See In re Kara Homes, Inc.*, 363 B.R. 399, 405 (Bankr. D.N.J. 2007) (development plans, designs, marketing fees, controlled management operations, and common amenities and roadways were all incidentally related to the construction project).

⁴⁹ *In re Alvion Props.*, 538 B.R. 527, 536 (Bankr. S.D. Ill. 2015).

⁵⁰ *See In re CBJ Dev.*, 202 B.R. 467, 470 (B.A.P. 9th Cir. 1996).

⁵¹ *See In re Hassen Imports P'ship*, 466 B.R. 492, 508 (Bankr. C.D. Cal. 2012).