

# In the United States Bankruptcy Court

## for the Northern District of Iowa

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LEON F. FUNKE and  
KAREN FUNKE

*Debtor(s).*

Bankruptcy No. 93-21255-KD

Chapter 12

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### ORDER

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This matter came on for hearing September 9, 1993 pursuant to assignment. Debtors Leon and Karen Funke were present at the hearing represented by counsel, Brian Peters. Attorney Clifton Jessup represented Connecticut General. Trustee Carol Dunbar also participated and joins in the Motion to Dismiss.

The matters before the Court are: (1) a Motion to Dismiss and Request for Sanctions; and (2) a Motion for Relief from Automatic Stay and Request for Sanctions. Both Motions were filed by Connecticut General Life Insurance Company.

#### STATEMENT OF FACTS

The Court adopts the Statement of Relevant Facts set out in Connecticut General's Brief, as follows:

On March 14, 1980, Connecticut General made a loan to the Debtors evidenced by that certain Promissory Note in the original principal amount of \$265,000 executed by the Debtors and delivered to Connecticut General (the "Note").

The Note is secured by a first Mortgage Lien held by Connecticut General on the Debtors' Real Property located in Dubuque County, Iowa, as more specifically described in that certain Farm Mortgage dated March 14, 1980, executed by the Debtors and delivered to Connecticut General (the "Farm Mortgage").

Prior to the Debtors filing their first bankruptcy case, on October 20, 1988, Connecticut General, as holder of the Note and Farm Mortgage, initiated foreclosure proceedings in the Dubuque County District Court against the Debtors. On or about March 8, 1989, the Debtors commenced a Chapter 11 bankruptcy case by filing a voluntary petition in the United States Bankruptcy Court for the Northern District of Iowa in order to prevent Connecticut General from foreclosing on the Farm Mortgage. The Debtors' first bankruptcy case was styled In re Leon F. Funke and Karen Funke, Debtors, Case No. L 89-00327-D.

In the first bankruptcy case, on August 31, 1989, the Debtors and Connecticut General entered into a Stipulation and Agreement for Adequate Protection and Satisfaction of Secured Claim under the Plan (the "Stipulation"). The Stipulation became the basis for the Debtors' Chapter 11 Plan filed in the first case.

This Court entered an Order Confirming the Debtors' Plan of Reorganization in the first bankruptcy case on February 7, 1990. The Order confirming the Debtors' Plan of Reorganization incorporated the terms and conditions of the Stipulation by reference.

Pursuant to the Confirmed Plan, the Stipulation gave a specific remedy to Connecticut General in the event of a default by the Debtors. The Stipulation provided as follows:

If the default is not cured within three (3) months after the due date of the payment, the Funkses hereby consent to Connecticut General's use of the Alternative Non-Judicial Voluntary Foreclosure Procedure pursuant to Iowa Code Section 654.18 which permits an expedited foreclosure procedure and acquisition of

title by Connecticut General.

On September 1, 1992, Debtors were required to make a quarterly payment in the amount of \$11,000.00 to Connecticut General as prescribed under the Confirmed Plan (see, Exhibit D, the Stipulation, pages 2-3, paragraph 1).

The Debtors defaulted under the terms of the Stipulation. Specifically, the Debtors failed to make the required payments under the Stipulation and failed to pay real estate taxes for several years.

After the Debtors' default, Connecticut General contacted Debtors' counsel and pursuant to the Confirmed Plan, requested that the Debtors execute certain documents necessary to expedite the Non-Judicial Foreclosure pursuant to Iowa Code Section 654.18. The Debtors refused and failed to execute such documents as required to implement the Debtors' Plan and in accordance with the Stipulation.

After the Debtors and Debtors' counsel refused to execute the Non-Judicial Foreclosure documents, Connecticut General requested that this Court reopen the Debtors' first bankruptcy case and hear Connecticut General's Motion for Enforcement of Remedy Under Confirmed Plan of Reorganization (the "Motion for Enforcement").

The Debtors' first bankruptcy case was subsequently reopened by order of this Court dated May 6, 1993. Notice of the Order Reopening Estate was served upon the Debtors and Debtors' counsel. Connecticut General then sought relief under its Motion for Enforcement. Pursuant to the Motion for Enforcement, Connecticut General requested that the Court issue an Order to aid Connecticut General in the implementation of the Confirmed Plan by directing the Debtors to execute and to deliver certain non-judicial foreclosure documents to Connecticut General in accordance with the default remedy contained in the Stipulation and incorporated into the Debtors' Confirmed Plan.

On June 23, 1993, the Court held a hearing on Connecticut General's Motion for Enforcement. The Debtors objected to the Motion for Enforcement. Both Connecticut General and the Debtors presented Briefs and/or oral arguments to the Court regarding the Motion for Enforcement. The Court took the matter under advisement.

On July 12, 1993, the Court entered an Order on the Motion for Enforcement wherein the Court ordered the Debtors to execute and to deliver the Non-Judicial Foreclosure Documents to Connecticut General no later than July 26, 1993 (the "Order on Motion for Enforcement").

Two business days prior to the date by which the Debtors were required to sign and to deliver to Connecticut General the Non-Judicial Foreclosure Documents, and without appealing the Order on Motion for Enforcement, the Debtors commenced their second bankruptcy case. [ ]

After the Debtors filed their second bankruptcy case, on August 3, 1993, Connecticut General filed its Motion to Dismiss Chapter 12 Case and Request for Sanctions (the "Motion to Dismiss") and its Motion for Relief from the Automatic Stay and Request for Sanctions (the "Motion for Relief") which are currently pending before the Court.

On or about August 21, 1993, the Debtors filed their Resistance to Motions dated August 2, 1993 by Connecticut General (the "Resistance"). The Resistance alleges a change in circumstances due to a drop in the price of milk. [ ]

Connecticut General asserts that Debtors' Chapter 12 petition constitutes a bad faith filing which warrants dismissal. It argues that the new petition is an attempt to avoid the Court's Order on the Motion for Enforcement and to prejudice creditors in favor of Debtors' sons who are now operating the farm. Connecticut General seeks dismissal for lack of good faith, relief from the automatic stay for lack of good faith, dismissal for failure to follow the confirmed plan and dismissal for lack of change in circumstances to justify the second petition. It also seeks Rule 9011 sanctions against Debtors and their attorney.

Trustee's Joinder in Motion to Dismiss states that from statements at the § 341(a) Meeting of Creditors it is apparent that Debtors do not meet the income test of § 101(18)(A) for eligibility for Chapter 12. Trustee Dunbar states that Debtors admit that they have very little to do with the farming operations and do not intend to reorganize or continue farming.

Debtors filed a resistance to Connecticut General's motions. They assert that Connecticut General would receive a

windfall if it is allowed to continue with nonjudicial foreclosure. They state that milk prices have dropped dramatically since the time of confirmation of the prior Chapter 11 plan which constitutes a substantial change in circumstances.

## JURISDICTION OF THE COURT

This Court has jurisdiction over this matter pursuant to 28 U.S.C. § 1334. This matter is a core proceeding as defined by 28 U.S.C. § 175(b)(2)(A), (G), and (O). The Court has the authority to enter a final order granting the relief requested by Connecticut General pursuant to 28 U.S.C. § 157(b)(1); 11 U.S.C. §§ 362(d)(1) and 1208(c).

## CHAPTER 12 ELIGIBILITY

Only a family farmer with regular annual income may be a debtor under Chapter 12. 11 U.S.C. § 109(f). "Family farmer" is defined at § 101(18)(A), in pertinent part, as follows:

individual or individual and spouse engaged in a farming operation . . . [who] receive from such farming operation more than 50 percent of such individual's or such individual and spouse's gross income for the taxable year preceding the taxable year in which the case

. . . was filed.

In determining Chapter 12 eligibility, there must be some indicia of involvement on the part of the debtors in the farming activity which generates the income they seek to have credited toward satisfaction of the income requirement of § 101(18)(A). In re Easton, 883 F.2d 630, 635 (8th Cir. 1989). Debtors must have some significant degree of engagement in, play some significant operational role in, or have an ownership interest in the farming operation. Id. at 636.

Debtors herein have failed to prove that they received 50 percent of their income in the prior taxable year from the farming operation. Arguably, they are involved in and play some operational role in the farming and dairy operation on their property. The extent of their involvement, however, is limited. Mr. Funke works essentially full time as a district sales manager for Jacques Seed Co. Debtors have indicated that their two sons are in charge of the operation. Debtors do have an ownership interest either directly or indirectly through a business entity known as "Funke Acres". The status of this business entity is unclear. It is categorized by Debtors as a farm corporation. Mr. Funke testified that it went into effect in March of 1993. However, there are no corporate records establishing that this is a viable corporation organized under the corporation laws of the State of Iowa. This entity does list four shareholders of whom each Debtor is listed as having an ownership interest of 36.69%. This entity did file a corporate income tax return for 1992 in which it reported \$28,960 in income. This income is composed of capital gains from the sale of farm animals and farm income. The livestock, machinery, crops, and other farm income all appear to be derived from assets which were initially part of the reorganization in Debtors' Chapter 11 Bankruptcy. The business records do not reflect that salaries were paid to Debtors. These business records also fail to reflect any dividend or income distribution to Debtors.

At the same time, Debtors' individual 1992 income tax return establishes that Debtors did not receive 50% of their income from the farm operations. Total farm income or loss as reported on their individual tax return (Form 1040, Line 19) is a loss of \$15,146. Other income (Form 1040, Lines 7-18) totals \$45,182. Therefore, even assuming that a proportionate share of the income from the corporation were somehow attributable to the Funke's, their net farm income would still be approximately \$6,000. This is arrived at by giving them the benefit of 73.38% of the income of the corporation which is their combined ownership interest. This income would, therefore, be \$21,250. The personal loss from farm operations is \$15,146 leaving a net farm income under the most favorable interpretation possible of \$6,104.

As indicated, this is the most favorable treatment of these facts which is possible under this record. Little justification is shown for the establishment of this business entity. The records of the State of Iowa fail to establish this as a viable corporate entity. The corporation lists assets which are appropriately subject to the reorganization plan under the previously approved Chapter 11 Plan. Mr. Funke testified that he received no income from this business entity. Nevertheless, giving Debtors the benefit of every doubt, their income derived from the farm operation is still less than 50% of Debtors' gross income. Thus, even if the Court were to include that portion of the corporate income as Debtors'

farm income, the Debtors still fail to meet the eligibility requirements of § 101(18)(A). Based on the failure to meet eligibility requirements under their Chapter 12 Petition, the Debtors' Petition must be dismissed.

### BAD FAITH FILING

Even though the Court has determined that the Debtors do not meet the income eligibility requirements of Chapter 12, the Court will address the issue of a bad faith filing. Debtors may not file a Chapter 12 petition while their previous Chapter 11 proceeding is still pending. See In re Miller, 122 B.R. 360, 365 (Bankr. N.D. Iowa 1990). In this case, the Court entered a final decree in Debtors' Chapter 11 on September 28, 1990. The order reopening the case was entered May 6, 1993. Thus, the Chapter 11 was still "pending" on July 22, 1993 when Debtors filed their Chapter 12 petition.

Even if the Chapter 11 is viewed as being closed when the Chapter 12 petition was filed, the question remains whether a Chapter 12 filing may follow the confirmation of a previously filed Chapter 11 case. Miller considered this issue. There is no *per se* prohibition against successive filings. Id. at 366. "One of the most troubling aspects of filing a new Chapter 11 or Chapter 12 after substantial consummation of a previously confirmed Chapter 11 plan is the [§ 1127(b)] prohibition against modifying a confirmed plan that has been substantially consummated." Id. A successive Chapter 12 case cannot be used to evade the § 1127(b) prohibition.

In Miller, the plan originally confirmed in the Chapter 11 case was a negotiated plan. The court found that "[t]he debtors are attempting to use this Chapter 12 filing to avoid what they now perceive to be a bad deal." Id. at 367. See also In re Utne, 146 B.R. 242, 249 (Bankr. D.S.D. 1992) (successive Chapter 12 plan is essentially an impermissible de facto modification of a Chapter 11 plan after confirmation; debtor cannot take exact debt of creditor addressed in Chapter 11 case and now reorganize it again under the broader provisions of Chapter 12).

Debtors argue that their change in circumstances, i.e. increase in milk prices, militates against a finding of bad faith filing. Filing of successive petitions may be indicia of bad faith where there is no bona fide change in circumstances that justifies multiple filings or where subsequent filings are designed to frustrate statutory requirements or abuse the bankruptcy process. In re Coones Ranch, Inc., 138 B.R. 251, 258 (Bankr. D.S.D. 1991). The kind of "changed circumstances" must be positive changes, e.g. that the debtor's financial circumstances and ability to perform a plan have improved. In re Huerta, 137 B.R. 356, 368 (Bankr. C.D. Cal. 1992). Negative changes in circumstances do not allow the debtor to refile after the breach of a plan. "And, of course, when a bankruptcy case is filed, even a first case, only to prevent or forestall foreclosure and without the intention of financial rehabilitation, the case should be dismissed as having been filed in bad faith." Id. at 369.

Debtors' circumstances are nearly indistinguishable from those existing in Miller. The Chapter 11 plan included a stipulation between the parties. Debtors now appear to feel they made a bad deal and wish to forestall foreclosure with their Chapter 12 filing. This would result in reorganizing again Connecticut General's exact debt which was subject to the Chapter 11 stipulation. This is an impermissible modification of a confirmed plan. "[F]iling of a successive Chapter 11 or Chapter 12 after substantial consummation of a previously confirmed Chapter 11 case for the sole purpose of renegotiating previously agreed upon plan treatment is an impermissible motive for filing the successive case." Miller, 122 B.R. at 367. The Court concludes that Debtors' Chapter 12 petition has not been filed in good faith. This conclusion constitutes a second ground for dismissal of this petition.

### SANCTIONS

Debtors have essentially admitted that they filed their Chapter 12 petition to delay Connecticut General's remedy of nonjudicial foreclosure in order to save the farm for their sons. This Chapter 12 filing is an attempt to circumvent the Court's Order on Motion for Enforcement requiring them to sign the documents necessary for the nonjudicial foreclosure. The Court concludes that the successive filing was for the improper purpose of delay. See Weiszhaar Farms, Inc. v. Livestock State Bank, 113 B.R. 1017, 1021 (D.S.D. 1990) (finding, on similar facts, improper purpose of delay by circumventing order authorizing sale of collateral). The dilatory purpose behind the Chapter 12 filing is an "improper, sanctionable purpose" under Rule 9011. Id. at 1022 (sanctions of \$50,000 awarded against debtor's attorney not excessive).

Although Debtors' conduct is sanctionable, the Court will not impose sanctions on either Debtors or their counsel. As noted in In re Cross Timbers Ranch, Inc., 155 B.R. 215, 219 (Bankr. W.D. Mo. 1993), it is understandable that farmers will do all they can to save their way of life, especially where the farm property has been in the family for a substantial length of time. Such individuals' optimism and love for the land can lead them to feel their plans to reorganize are feasible. Id. The Court is loath to penalize Debtors' dilatory conduct in light of the fact that they are already losing their farm. There is no evidence that Debtors' counsel committed any specific impropriety. Based on the foregoing considerations, the Court will not impose sanctions in this case at this time. However, the Court advises the Debtors and counsel for the Debtors that the Court's reluctance to impose sanctions at this time should not be construed as authorization to utilize the bankruptcy process for any purpose for which the Bankruptcy Code was not intended.

**WHEREFORE**, Connecticut General's Motion to Dismiss this Chapter 12 case and the Motion for Relief from the Automatic Stay are GRANTED.

**FURTHER**, for the reasons set forth herein, it is the determination of this Court that the Debtors are not eligible for Chapter 12 relief under § 101(18)(A).

**FURTHER**, for the reasons set forth herein, it is the determination of this Court that Debtors' Chapter 12 Petition was not filed herein in good faith.

**FURTHER**, for the reasons set forth herein, Connecticut General's Requests for Sanctions are DENIED.

**FURTHER**, for the reasons set forth herein, the Debtors' Chapter 12 Petition is hereby DISMISSED.

**SO ORDERED** this 21st day of October, 1993.

Paul J. Kilburg  
U.S. Bankruptcy Judge