

In the United States Bankruptcy Court

for the Northern District of Iowa

RODNEY E. WESTERBERG and
ROGENE P. WESTERBERG

Debtor(s).

Bankruptcy No. X86-02743M

Chapter 12

Contested No. 4212

ORDER RE: DEBTORS' MOTION TO SELL REAL ESTATE FREE AND CLEAR OF LIENS AND TO REQUIRE RELEASE OF MORTGAGE OR OTHER REAL ESTATE

Debtors Rodney and Rogene Westerberg ask the court for permission to sell approximately 90 acres of real estate free and clear of all liens with the liens to attach to the proceeds. The proposed sale is to the Iowa Department of Natural Resources (IDNR). Debtors ask that after payment of reasonable closing costs, they be permitted to pay the proceeds of sale to John Hancock Mutual Life Insurance Company (JOHN HANCOCK), the holder of a first mortgage on the property. Debtors ask also that Liberty Bank and Trust Company, formerly known as Forest City Bank and Trust (LIBERTY BANK), be required to release its mortgage against all of the debtors' real estate, not just the parcel proposed to be sold.

Liberty Bank objects to the motion only so far as it asks the court to require it to file a release of its mortgage on all debtors' land. To permit the sale, it is willing to give a partial release to the extent of the parcel to be sold.

Hearing on the motion was held December 13, 1994, in Sioux City. Thomas L. Fiegen appeared for the debtors. Robert P. Cooper appeared for Liberty Bank.

Debtors own approximately 520 acres of farm ground. They seek to sell 90 acres of it to the IDNR. Prior to filing this chapter 12 case, the 520 acres were encumbered by various liens. These liens included a first priority mortgage held by John Hancock and a second priority mortgage held by Liberty Bank. Liberty Bank also held a perfected security interest in debtors' machinery, equipment and crops.

Debtors proposed a plan of reorganization on June 24, 1988; it was confirmed on July 22, 1988. Judgment of confirmation entered July 25, 1988. Under the plan, debtors were to make three annual payments to the trustee of \$7,500.00 each for dividend payments to class 6, the unsecured creditors. A plan modification approved February 15, 1990, permitted debtors to make the second \$7,500.00 payment after initially proposed but on or before December 31, 1990, the date of the final installment.

Liberty Bank was identified as a class 4 claimant. The class was described as follows: "Class 4 claims shall be the allowed secured claim of the Forest City Bank & Trust Company, secured by a security interest in the Debtors' farm machinery, equipment, and crops." (Plan, section 2.05).

The treatment of Liberty Bank's claim was stated under section 3.05 of the plan. It stated that the claim was secured by machinery valued at \$96,055.00, a replacement lien on livestock valued at \$65,000.00 and by crops. The total secured claim to be treated under the plan was valued at \$161,055.00 (Plan, section 3.05(a)). The plan provided an initial payment on the secured claim of \$20,000.00 and amortization of the balance over seven years (Plan, sections 3.05(c) and (d)). Section 3.05(c) of the plan stated:

The liens and encumbrances upon the property securing this claim shall remain as valid liens and

encumbrances to the full extent of the unpaid balance of the allowed secured claim until such time as said allowed secured claim is paid in full.

Also, debtors agreed to provide Liberty Bank with a post-confirmation replacement lien on crops and livestock to protect Bank for debtors' use of Bank's collateral during the plan (Plan, section 3.05 (f)).

Section 3.08(d) of the plan provided that "[t]o the extent that a creditor holding a Class 2 through Class 5 claim is unsecured, such creditor shall be treated as a creditor holding a Class 6 claim to the extent of any deficiency." Although Liberty Bank apparently held a second mortgage against debtors' real estate, the lien of Bank was not compensated by the plan, either through retention or payment.

At the time of the hearing on the motion, debtors were delinquent in their plan payments for the class 6 unsecured creditors and the payments to Liberty Bank on account of its class 4 claim. Debtors say if they can sell the 90 acres and pay down the first mortgage debt to John Hancock, they likely will be able to refinance the debt against the remaining 430 acres so that they can pay off John Hancock and complete their payments to the trustee for class 6 unsecured creditors.

Because Liberty Bank would consent to the proposed sale of the 90 acres if it is not required to file a release of its mortgage on the remaining land, the critical issue before the court is whether debtors can force such a release. Debtors argue that Liberty Bank must release the mortgage because the land vested in the debtors on confirmation of their plan (11 U.S.C. § 1227(b)) free and clear of any claim or interest of Liberty Bank which was provided for by the plan (11 U.S.C. § 1227(c)).

I do not construe 11 U.S.C. § 1227(c) to require Liberty Bank to file a release of its mortgage. The confirmed plan clearly bifurcated Liberty Bank's claim into an allowed secured claim and an allowed unsecured claim. The bifurcation was accomplished as an effect of 11 U.S.C. § 506(a). The plan treated Liberty Bank's lien against the real estate as valueless and, therefore, the value of the real estate did not contribute to Liberty Bank's allowed secured claim. Because the mortgage secured a claim that was not an allowed secured claim, the mortgage was void under the plan as an effect of 11 U.S.C. § 506(d). To obtain confirmation, debtors' plan would have to have met one of the requirements of 11 U.S.C. § 1225(a) (5). There was no objection by Liberty Bank that it did not. Under the Code, confirmation of the plan had the effect of vesting the property of the estate in the debtors, as the plan did not provide otherwise. 11 U.S.C. § 1227(b). The property vested "free and clear of any claim or interest of any creditor provided for by the plan" except as to liens retained pursuant to the plan. 11 U.S.C. § 1227(c). Thus the real estate vested in the debtors free of the claims of unsecured creditors, including Liberty Bank, and free of voided liens. Even so, the estate continues to exist after confirmation. *Cf. Security Bank of Marshalltown, Iowa v. Neiman*, 1 F.3d 687, 690 (8th Cir. 1993) (estate continues to exist after confirmation of chapter 13 plan).

The Westerbergs will obtain a discharge when they have completed plan payments other than long-term debt. 11 U.S.C. § 1228(a). They have not yet made all such plan payments as they are delinquent in their payments to the trustee on behalf of unsecured creditors. They are also delinquent on their long-term payments to Liberty Bank. This case, therefore, is still subject to dismissal or conversion. If the case is dismissed, Bank's lien, which is now void, would be reinstated under 11 U.S.C. § 349(b). Requiring a formal release of the mortgage, which is not mandated by the plan, would be contrary to Liberty Bank's reinstated rights in the property if the case is dismissed. Such lien rights could not be reinstated as a matter of law if Liberty Bank is forced to file a release of the mortgage. Moreover, a release is not necessary. If the plan is performed, Liberty Bank's lien rights in the real estate will remain void as a result of confirmation and consummation. Accordingly, a formal release of the Bank's void interest will not be required. Liberty Bank consents to a partial formal release for the purposes of the sale.

As to the sale motion, debtors may sell and pay reasonable and necessary closing costs without advance court approval, but they may not pay any professional fees relating to the sale without such approval. Debtors shall hold in trust any proposed professional fees subject to court approval and may pay the balance of sales proceeds to John Hancock Mutual Life Insurance Co. Debtors shall file a report of sale.

ORDER

IT IS ORDERED that debtors' motion to sell 90 acres of real estate as described in the motion is GRANTED. The sale shall be free and clear of liens with liens to attach to the proceeds of sale.

IT IS FURTHER ORDERED that debtors may pay from the sales proceeds the reasonable and necessary costs of sale including costs of abstracting, transfer and taxes. Debtors may not pay professional fees without court approval, but they shall hold any such proposed fees pending court approval. The sales proceeds after payment or holding of such costs shall be paid to John Hancock Mutual Life Insurance Co. Debtors shall file a report of sale.

IT IS FURTHER ORDERED that debtors' motion to require the filing of a formal mortgage release by Liberty Bank & Trust Co. is DENIED.

So ORDERED THIS 19th DAY OF DECEMBER, 1994.

William L. Edmonds
Chief Bankruptcy Judge