In the United States Bankruptcy Court

for the Northern District of Iowa

CARL M. SIMON, DIANE L. SIMON Debtors.	Bankruptcy No. 94-21591KD Chapter 12

ORDER RE REQUEST FOR HEARING ON VALUATION

On November 30, 1995, the above-captioned matter came on for hearing on Debtors' Request for Hearing on Valuation of a dairy herd. Debtor Carl Simon appeared in person with Debtors' attorney Peter Riley. Ray Terpstra appeared on behalf of Creditors Morris Eckhart, Barry Hammarback and James Koby ("Creditors"). Dan Childers appeared on behalf of Dave's Feed Store, Inc. Evidence was presented after which the Court took the matter under advisement. This is a core proceeding pursuant to 28 U.S.C. 157(b)(2)(K).

STATEMENT OF THE CASE

Debtors filed their Chapter 12 Petition on October 4, 1994. They have filed a Plan which has not been confirmed. A significant issue in underlying proceedings was ownership of a dairy herd which forms the core of Debtors' attempts to reorganize their farming operation. The herd consists of approximately 250 head of cattle, most of which are Holstein milking cows. The majority of Debtors' cash flow is generated by the sale of milk from this herd to Wapsi Valley Sales. Based on a ruling by this Court in an adversary proceeding involving ownership of the cow herd and determination of a security interest in the cattle, Debtors acknowledge the necessity of amending their reorganization plan. To avoid additional amendments, Debtors have filed this Motion for Valuation requesting the Court to value the cow herd so that they can amend the plan consistent with the Court's ruling in the adversary proceeding using correct values.

Debtors presented the testimony of Mr. Martin Waterhouse who has been an auctioneer since 1973. Mr. Waterhouse has a sales operation in Manchester, Iowa. He testified that he is familiar with the Debtors' herd as Mr. Simon frequently buys and sells cattle through his sale barn. Mr. Waterhouse testified that he has not recently gone to debtors' farm. He testified, however, that he is familiar with the farming operation of Mr. Simon and is generally familiar with the cattle in question and the types of cattle which Mr. Simon buys and sells.

Mr. Waterhouse valued the cattle between $500 and $600 per head. He based his opinion upon his general knowledge of the types of cattle which Mr. Simon purchases. It is based, to some extent, on the milk production of these cattle which has averaged 51 lbs. per head. He testified that the sale of the herd in bulk would reduce the total sale price. He also considered the fact that Mr. Simon is known in the local community and that Mr. Simon purchases cattle that are outside the parameters of the type of cattle which most people would ordinarily purchase. He testified that Mr. Simon generally purchases cattle at these sales for not more than $100 to $200 over the sale price for a pound cow. A pound cow, being a non-producing cow, is sold by the pound for slaughter. The general price for a pound cow is approximately $30 per hundred weight. An average cow would weigh somewhere around 1,000 pounds and would, therefore, sell for approximately $300.

Mr. Waterhouse testified that he has personal knowledge only of the cattle bought and sold at his sale barn by Mr. Simon. He understands that Mr. Simon has purchased cattle from other sources but is not aware of the purchase price of these cattle. He has not been on Debtors' premises recently nor did he personally inspect the cattle prior to making his valuation. Mr. Waterhouse testified that his estimate of value is based upon the fact that a sale would include sales expenses of between 6% and 7%. He testified that a sale in bulk would reduce the total sale price though he also subsequently testified that sometimes a sale in bulk can increase the sale price. For example, a going out-of-business sale was held by a Mr. White in the local community in July of 1995 in which a dairy herd was sold in bulk and the average sale price was between $700 and $800 per head.

Debtor Carl Simon also testified as to the value of this herd. He testified that there were approximately 240 cows in the operation at the time of filing of the Petition and there are now approximately 275 cattle in the herd. There are three or four different categories of cattle, in terms of quality. He testified that he has approximately 100 cows of little value. He estimates that these are worth between $250 and $300. A second category consists of approximately 100 cows which are moderate producers and are valued between $350 and $435. A third group consists of approximately 70 cattle with a value between $400 and $475. Finally, he has a group of approximately five cows which he considers to be of high quality with a value in excess of $660 per head. Based on these conclusions, the average price for this herd would be approximately $400 per head.

Mr. Michael Behr testified on behalf of Creditors. A major consideration in his valuation was milk production. Mr. Behr testified that this is a dairy herd and the purpose of the herd is to provide cash flow through the production of milk. He testified that the milk production of Debtors' herd has been gradually increasing based upon milk sale records. Milk production, since the filing of Debtors' petition over 13 months ago, has generated $504,111.69 in total milk sales.

Mr. Behr testified that, in his opinion, the value of the herd is $750 per head. He testified that the average sale price for a Holstein dairy cow in Iowa is slightly in excess of $1,100. Mr. Behr testified that he reduced the value $350 per head based in part on the factors identified by Mr. Waterhouse. He based the value of this cow herd on milk production as a starting point and then factored in other matters to arrive at his conclusion.

In summary, Debtors state that the cows in their dairy herd were purchased for approximately $525 on average and sold for slaughter for an average of $394 per head. They assert, therefore, that the value lies somewhere between these two numbers. Debtors argue that the sale prices at market are the best indicators of present value. They admit that their plan envisions a going concern and that they do not intend to propose a liquidation plan.

Creditors claim that Debtors purchase cattle at low prices and attempt to rehabilitate them to become adequate milk producers. They keep those where the rehabilitation effort has been successful and sell those which do not produce. Those cattle are sold at pound prices. Creditors, therefore, assert that the sales prices do not accurately reflect the value of the herd on their dairy farm at any one time. They assert that the value of this herd is substantially more than the purchase prices. Creditors claim that the sale price of the cows reflects the lowest possible value because the worst cows are being sold at any one time. Additionally, they assert that this herd must be valued on the basis of milk production. This is another way of saying that the herd must be valued as a going concern and, so valued, it is substantially more valuable than in a "going out-of-business" context or as cull cattle.

CONCLUSIONS OF LAW

Debtors are seeking valuation pursuant to 506(a). The first sentence of that section states, in pertinent part, that an allowed claim is a secured claim "to the extent of the value of [the] creditor's interest in the estate's interest in [the] property." 11 U.S.C. 506(a). The second sentence states that "[s]uch value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property." Id. In making this valuation, the Court relies on existing 8th Circuit case authority which holds that the proper analysis is to value the property as a going concern and not under a liquidation analysis when the debtor anticipates retaining the property.

The 8th Circuit has stated as follows:

We adopt the reasoning of the Fifth Circuit in In re Rash, and other courts that have focused on the second sentence of Section 506(a) and we now conclude that the value of [the] lien interest is properly based on the retail value of the collateral without deduction for costs of sale. We agree with the Fifth Circuit that the retail valuation method is the only method that gives full effect to the entire language of Section 506(a). "If the first sentence of 506(a) were interpreted to mean that the value must be fixed at the amount which the creditor would receive on foreclosure, then the last sentence of the statute which provides that the value should be determined in light of the purpose of the valuation and of the proposed disposition or use of the property, would be surplusage." In re Rash, 31 F.3d at 329 (quoting In re Courtright, 57 B.R. 495, 497 (Bankr. D. Or. 1986)). Under the wholesale valuation method, the creditor's interest would always be valued at the amount the creditor would receive upon disposition of the collateral, regardless of the purpose of the valuation or of the proposed disposition or use of the property. The wholesale method would not be affected by whether the debtor intended to release the property or intended, instead, to retain and use the property. Rather, where a debtor intends to retain and use the collateral, the purpose of the valuation is to determine the amount an undersecured creditor will be paid for the debtor's continued possession and use of the collateral, not to determine the amount such creditor would receive if it hypothetically had to repossess and sell the collateral. Such an interpretation ignores the express dictates of Section 506(a).

In re Trimble, 50 F.3d 530, 531-32 (8th Cir. 1995).

This rationale was utilized in In re Sprecher, 65 B.R. 598, 601 (Bankr. C.D. Ill. 1986), to value farm machinery and livestock the debtor sought to redeem in a Chapter 7 case. The court stated that the debtor would retain and continue to use the property and, therefore, it refused to discount the value to reflect a decreased value which a hypothetical purchaser would be willing to pay. Id. In In re Bowling, 64 B.R. 710, 711 (Bankr. W.D. Mo. 1986), the court valued a dairy heard as dairy cows rather than at less than half that value as cows sold for slaughter. The debtor had elected to participate in a dairy termination program which required that the cows be slaughtered. Id. The court, however, stated that the secured creditor, which had no say in whether the debtor would participate in the termination program, must be compensated to the fair market value of the herd as a dairy herd. Id. at 713.

The Court concludes that Debtors' dairy herd should be valued as a going concern. Mr. Behr's valuation seems most appropriate. Debtors' sale price for the cows reflects only the sale price for pound cows which can no longer produce milk. Debtors' dairy herd, by definition, is a producing herd with milk production running close to the average for a dairy herd in Iowa. As such, its value is significantly higher as a going concern and Mr. Behr's valuation based in substantial part upon milk production is the most valid method of placing a value on this herd. The Court accepts the estimate of value of $750 per head. This number is fair and has already been reduced more than $300 from the sale price of an average dairy cow in Iowa based on the factors outlined by Debtor's expert, Mr. Waterhouse.

WHEREFORE, Debtors' Request for Hearing on Valuation is GRANTED IN PART and DENIED IN PART.

FURTHER, Debtors' dairy herd has a value of $750 per head.

SO ORDERED this 7th day of December, 1995.

Paul J. Kilburg
U.S. Bankruptcy Judge