In the United States Bankruptcy Court

for the Northern District of Iowa

JOHN G. SPECHT, CAROL C. SPECHT	Bankruptcy No. 96-21022-D
Debtors.	Chapter 12

ORDER RE DEBTORS' AMENDED CHAPTER 12 PLAN

This matter came before the undersigned on March 13, 1997 for confirmation hearing on Debtors' Amended Chapter 12 Plan. The following appeared at the hearing: Brian W. Peters and Douglas C. Pearce for Debtors John and Carol Specht; Carol Dunbar, Chapter 12 Trustee; Martin McLaughlin for the United States on behalf of Farm Service Agency (FSA); and Joseph Peiffer for New Vienna Savings Bank. Evidence was presented after which the Court took the matter under advisement. The time for filing briefs has now passed and this matter is ready for resolution. This is a core proceeding pursuant to 28 U.S.C. 157(b)(2)(A), (L).

FINDINGS OF FACT

Debtors filed their Chapter 12 Petition on April 26, 1996. This is Debtors' third proposed plan. They propose to fund their plan with income from farming and from off-farm employment. Debtors propose to deed 80 acres to FSA to satisfy its secured claim. Debtors will turn over a tractor to New Vienna Savings Bank.

New Vienna Savings Bank, FSA and the Trustee have all objected to confirmation of the Amended Plan. They share the belief that the plan is not feasible. They argue that Debtors' projected income and expenses are not realistic in light of their past income and expenses. They also point out that Debtors' plan does not acknowledge potential liability for capital gains tax from the transfer of the 80 acres to FSA. The parties dispute the value of the 80 acres considering it is not accessible by road.

In addition, these three objectors have raised various other points. Among them, the Bank asserts that Debtor has incorrectly undervalued its secured claim. It claims a security interest in a pickup, certain calves, the 1996 crop, and proceeds from an IBP check. The Bank also claims a security interest in cattle. It argues Debtors cannot assert that this interest is avoidable as a lien on tools of their trade.

Trustee joins in the Bank's objections regarding feasibility. She also objects to payment of the Bank and the FSA directly by the Debtors, asserting that the payments should be paid through her to monitor timeliness for the protection of creditors. Farm Service Agency states the plan also fails to fully accommodate its secured claim. It concurs with the Bank regarding capital gains tax liability. It also asserts that cattle are not tools of the trade which would support lien avoidance.

The Bank filed a separate Motion to Dismiss and requested dismissal in its objection to confirmation. FSA has joined in that motion. Debtors filed a resistance.

The Court, in earlier confirmation hearings, placed values on certain estate property, as follows: farmstead located in Dubuque County, Iowa - $207,000; 1987 Ford F-150 Pickup -- $4,225; 1990 Chevrolet Lumina Eurosport -- $5,025. Debtors paid $54,000 for their farmstead in 1971.

Debtors' tax returns for 1990 through 1995 all reflect yearly farm losses. Future income projections under Debtors' plan do not incorporate self-employment and income taxes. Debtor John Specht testified that Debtors' living expenses have decreased based on their son moving out of the house. He anticipates monthly household expenses of $1,300 during the plan; average monthly household expenses for the past year were approximately $1,650. Debtors' monthly reports reflect that these expenses have not decreased since Debtors' son moved out in October.

Carol Specht testified that she now works part-time at a job which could become full-time next year. She also works at a supper club part-time and testified that she will increase her time working there. She anticipates monthly income of $400 during the plan; her average monthly income in the past year is approximately $150.

CONCLUSIONS OF LAW

Under 1225(a)(6), one of the requirements for confirmation is that Debtors "be able to make all payments under the plan and to comply with the plan." This "feasibility" standard requires the Court to determine whether the plan offers a reasonable prospect of success and is workable. In re Monnier Bros., 755 F.2d 1336, 1341 (8th Cir. 1985); In re Foertsch, 167 B.R. 555, 565 (Bankr. D.N.D. 1994). It "injects pragmatism into the confirmation process by prohibiting confirmation of overly optimistic reorganization plans clearly destined to fail and by not belaboring the inevitable demise of a hopelessly insolvent debtor." Foertsch, 127 B.R. at 565 (citation omitted). The test is whether the things which are to be done after confirmation can be done as a practical matter under the facts. In re Clarkson, 767 F.2d 417, 420 (8th Cir. 1985).

Debtors bear the burden of proof in meeting the feasibility requirement of 1225(a)(6). In re Rape, 104 B.R. 741, 748 (W.D.N.C. 1989). The Court considers the farm's earning power, capital structure, economic conditions, managerial efficiency and whether the same management will continue operations. Id. at 749. Debtors' income and expense projections may be considered in conjunction with their actual past performance to determine feasibility. In re Euerle Farms, Inc., 861 F.2d 1089, 1090 (8th Cir. 1988). "Because past behavior and productivity are excellent predictors of future production, courts have frequently rejected plans which are premised on highly optimistic projections of increased production." In re Crowley, 85 B.R. 76, 79 (W.D. Wis. 1988).

In In re Hirt, 97 B.R. 981, 983 (Bankr. E.D. Wis. 1989), the court found that the debtors' cash flow projections for their farming operations were flawed when tested against their actual circumstances. It found cause to dismiss the case as the case was over ten months old and further delays would be

unreasonable and prejudicial to creditors. Id. at 985. In In re Braxton, 124 B.R. 870, 874 (Bankr. N.D. Fla. 1991), the court found that the debtors' plan was not feasible. The court's valuation rulings increased debt service to secured creditors and actual market prices for finished hogs did not match those the debtors predicted in their plan. Id. A question of good faith also existed because of debtors' attempt to satisfy secured creditors by surrendering low, swampy, landlocked parcels of land of questionable value. Id. at 875.

Based on actual past performance, Debtors' projections are unrealistic. Monthly expenses and income reported in the past eleven months since Debtors filed their petition do not support those projected in Debtors' plan. Debtors' projected cash price for corn of $2.75 per bushel is not supported by historical averages. The plan does not provide for payment of self-employment and income taxes. Also, it does not totally provide for payment of the Bank's secured claim. Debtor's brief acknowledges that the Bank is secured by certain cattle and offspring and that the Court's valuation of a vehicle increases the Bank's secured claim.

Debtors assert that turning over the 80 acres to FSA will not have an effect on their tax liability. They argue that the return of the property results in discharge of indebtedness income, excludable from income by Internal Revenue Code 108. The Eighth Circuit held, in affirming a Tax Court decision, that such a transaction is not excludable under I.R.C 108. Gehl v. Commissioner, 102 T.C. 784, 790 (1994), aff'd, 50 F.3d 12, 1995 WL 115589 (8th Cir.), cert. denied, 116 S. Ct. 257 (1995). The Tax Court concluded that when a debtor transfers property to a creditor having a fair market value exceeding its basis but less than the recourse debt, the gain does not constitute income from discharge of indebtedness. Id. The Eighth Circuit affirmed, stating that this land transfer is outside the scope of 108 which excludes income from discharge of indebtedness in certain circumstances. Gehl, 50 F.3d 12, 1995 WL 115589, at *3 (unpublished decision).

As the record stands, Debtors' proposal to deed FSA 80 acres in satisfaction of its claim will produce income from a sale or exchange of property. This is not the type of income which is excludable under 108 as income from the discharge of indebtedness. Debtors' basis in the property is $54,000; the fair market value is $207,000. The difference of $153,000 is taxable income under Gehl. Debtors' failure to acknowledge this income and related taxes in the plan places an additional unincluded tax burden upon Debtors and further undermines the plan's feasibility.

The Court concludes that Debtors have failed to prove that their Amended Chapter 12 Plan filed February 18, 1997 meets the feasibility requirement of 1225(a)(6). Debtors filed their Chapter 12 Petition more than 11 months ago, utilizing the benefits of the automatic stay and delaying collection by their creditors. Despite this respite, Debtors have not been able to increase their income or decrease their expenses, according to their monthly reports, sufficient to support a workable Chapter 12 Plan. Debtors' projected income and expenses are overly optimistic and not supported by historical or market data. They have not accurately recognized income tax and self-employment tax liabilities. Further, Debtors have failed to correctly value secured claims.

The Bank and FSA requested dismissal of this case in their objections to confirmation. The Bank subsequently filed a formal Motion to Dismiss, joined by FSA. The Court concludes that it is appropriate to consider dismissal at this time. See In re Pretzer, 96 B.R. 790, 793 (Bankr. N.D. Ohio

1989) (concluding court has power to dismiss case on its own motion).

Filing for Chapter 12 protection without the ability to reorganize renders the petition subject to dismissal. Euerle Farms, 861 F.2d at 1192. The Eighth Circuit affirmed dismissal in Euerle Farms where the debtor had proposed a problematic and unconfirmable plan with payments to creditors being conjectural at best. Id. In In re Hirt, 97 B.R. 981, 985 (Bankr. E.D. Wis. 1989), the court found cause to dismiss in a Chapter 11 farm case where the case was over 10 months old and the record amply demonstrated the debtors' inability to effectuate a feasible plan.

Chapter 12 was structured to require debtors to speedily confirm a plan of reorganization. Pretzer, 96 B.R. at 793. Debtors may not request additional time for filing further plans or modifications as a way to prolong protection under Chapter 12 when there is no reasonable likelihood of reorganization. Id. Cause exists for dismissal where Chapter 12 debtors have had ample opportunity to propose a plan and have failed to do so. In re Luchenbill, 112 B.R. 204, 219 (Bankr. E.D. Mich. 1990).

The Court concludes that dismissal of this Chapter 12 case is appropriate. This is the third plan proposed by Debtors in the 11 months since they filed their petition. Monthly reports indicate Debtors have insufficient income to fund a workable plan. The failure to propose a confirmable plan is creating an unreasonable delay. 11 U.S.C. 1208(c)(1). Confirmation has been denied three times. Id. at (c)(5). Further delay will result in diminution of the estate in the absence of a reasonable likelihood of rehabilitation. Id. at (c)(9).

WHEREFORE, confirmation of Debtors' Amended Chapter 12 Plan is DENIED.

FURTHER, this case is DISMISSED.

SO ORDERED this 9th day of April, 1997.

Paul J. Kilburg
U.S. Bankruptcy Judge