

IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF: )  
)  
ROBERT RICHARD PETERSEN and )  
BARBARA LEE PETERSEN, ) CASE NO. BK93-80038  
)  
DEBTOR(S). ) CH. 12

MEMORANDUM

Hearing was held on March 21, 2000, on a Motion to Modify Plan to Increase Payments to Unsecured Creditors. Appearances: Charles Meyer for the debtors, Howard Duncan for Stanco, Inc., and Richard Lydick Chapter 12 Trustee. This memorandum contains findings of fact and conclusions of law required by Fed. Bankr. R. 7052 and Fed. R. Civ. P. 52. This is a core proceeding as defined by 28 U.S.C. § 157(b)(2)(A) and (J).

Background

This matter is before the court on creditor Stanco Inc.'s ("Stanco") allegation that the debtors have failed to report all their disposable income during the pendency of their Chapter 12 case. The Chapter 12 Trustee has joined Stanco's position. Barbara Petersen, one of the the debtors, received an inheritance during the pendency of the Chapter 12 case which consisted of an undivided one-third interest in real property and \$61,000.00 in cash. Stanco and the Trustee allege that the debtors failed to report the inheritance, that the inheritance must be included in the calculation of disposable income and that, due to the receipt of the inheritance, the debtors have not paid all their disposable income into the plan. Finally, Stanco and the Trustee urge this court to include the value of the debtors' interest in real property received by inheritance in calculation of disposable income although there is no plan to liquidate the property.

In opposition, the debtors argue that, although they did indeed receive an inheritance, it has been reported. The debtors also argue that all of the inherited funds were reasonably required for the maintenance and continuation of the debtors' farming operation. Finally, the debtors argue that the real property received by the debtors is not available for distribution under state law, and that the value of the land is not required to be considered in the disposable

income calculation.

FACTS

1. The debtors, Robert and Barbara Petersen, filed for relief under Chapter 12 of The Bankruptcy Code in January, 1993. The Chapter 12 Plan was confirmed on December 14, 1993, and was completed, according to its terms, three years later, in 1996. However, a discharge was not entered in 1996 because the Trustee and Stanco requested an accounting from the debtors. The debtors were ordered by the court to provide the accounting and did so.

2. The debtors received a total \$61,000.00 in cash from Mrs. Petersen's father's estate, in several distributions.

3. On April 1, 1994, Barbara Petersen, who was the personal representative of her father's estate, received \$2,500.00 for her services to the estate and a partial distribution from the estate of \$43,500.00 for a total of \$46,000.00. From this \$46,000.00, \$29,500.00 was paid back into the estate; \$26,000.00 for a pivot irrigation system and \$3,500.00 for a 1987 Chevy Celebrity. The net cash received was \$16,500.00.

4. The \$26,000.00 was paid for the pivot irrigation system located on land owned by Mrs. Petersen's father which was inherited by Mrs. Petersen and her two sisters. The amount paid was required to be paid by the terms of the will. Prior to the opening of the will, the Petersens were under the assumption that the pivot would be inherited by Mrs. Petersen without payment. However, because Mrs. Petersen's father was upset by the bankruptcy filing, he changed his will to require repayment for the pivot system; \$20,000.00 in principal and \$6,000.00 in interest.

5. Mrs. Petersen received two additional payments of \$2,500.00 for her services as personal representative. This income was reported as wages on the Petersens' quarterly reports.

6. Mrs. Petersen also received a \$10,000.00 distribution in 1995. This distribution, however, did not pass through the Petersens' accounts. The \$10,000.00 was placed in an account kept by Mrs. Petersen and her two sisters to be utilized in their farming operation. Mr. Petersen did not report the income on his quarterly reports but did disclose the

disbursement on the accounting that was ordered by this court.

7. Mrs. Petersen also received an undivided one-third interest in farmland that was owned by her father. This land is owned with two of her sisters. Currently, the Petersens rent this land from the sisters and utilize it for farming purposes. Because Mrs. Petersen owns an interest in this land and she also rents it, she receives rental income from this property. This is reported on the quarterly reports under rents paid and received.

8. Mrs. Petersen and her sisters inherited some land from their mother several years prior to her father's death. The inheritance was subject to a life estate in her father. The land was part of the real estate farmed by Mr. Petersen during the case and rent was paid for its use.

9. According to the operating reports, in 1993, the farming operation accumulated receipts in the amount of \$180,931.00 while disbursing \$254,432.00. This leaves a negative balance of \$73,501.00. The 1994 receipts totaled \$158,878.00 while disbursing \$163,154.00. This leaves a negative balance of \$4,276.00. In 1995, the receipts totaled \$187,547.00 while the disbursements totaled \$169,500.00. Thus, the farm operated at a positive balance of \$18,047.00 for 1995. The 1996 farming year resulted in receipts of \$182,193.00 and disbursements of \$178,263.00. The final calculations of 1996 show the debtor operating from a positive balance of \$3,930.00. At the end of the plan, in 1996, the debtors had an operating deficit over the life of the plan of \$55,800.00.

10. Mrs. Petersen holds two non-farm jobs and all of her income from those jobs has been reported.

11. Mr. Petersen filed almost all of his quarterly reports late and seemed to complete and file a number of them all at the same time. The quarterly reports are a bit confusing and hard to decipher. However, when read in conjunction with the accounting, it appears that the Petersens did report all of their disposable income. According to the accounting and the undisputed testimony of Mr. Petersen, all of the money both earned by the debtors and inherited was spent either by the debtors for their care or for the furtherance of farming operations. The \$10,000.00 disbursement that Mrs. Petersen placed in an account to be

used for farm operations on her land was used for removal of timber and other land improvements.

12. At the time of trial, the Petersens owned a 1988 Lincoln Towncar, a 1984 Ford F150, had about \$1,500.00 cash assets in a checking account, and about \$3,000.00 in a savings account that represents proceeds from a government check that will be used to pay rent on lands that are to be farmed.

#### Decision

The inherited cash and land, while property of the estate, do not represent excess disposable income.

#### Analysis

According to the Bankruptcy Code, all "disposable income" is required to be paid into the plan and distributed to creditors. See 28 U.S.C. § 1225 (stating that disposable income is to be paid into a plan if the Trustee or an unsecured creditor objects unless the plan proposes payment in full of creditor claims). When challenging a debtor's contribution of disposable income, the initial burden of proof is on the Trustee to show that the debtors have failed to contribute all of their disposable income to the plan. Hammrich v. Lovald (In re Hammrich), 98 F.3d 388(8th Cir. 1996). However, the ultimate burden lies with the debtors to show that, indeed, they are satisfying the disposable income obligation. In re Hammrich, 98 F.3d at 389; In re Kuhlman, 118 B.R. 731, 738 (Bankr. D. S.D. 1990).

Further, 28 U.S.C. § 1225(b)(2) defines "disposable income" as "income which is received by the debtor and which is not *reasonably necessary* to be expended (A) for the maintenance or support of the debtor or a dependant of the debtor; or(B) for the payment of expenditures necessary for the continuation, preservation and operation of the debtor's business." (emphasis added) Although Section 1225 pertains to confirmation of a plan, the disposable income requirement may also come into play at the time a debtor requests discharge. Rowley v. Yarnell, 22 F.3d 190 (8<sup>th</sup> Cir. 1994); In re Meyer, 173 B.R. 419 (Bankr. D. Kan. 1994); In re Wood 122 B.R.107 ( Bankr. D. Idaho 1990).

The "reasonably necessary" terminology of Section 1225 requires the court to conduct a subjective analysis of a

debtor's expenditures while considering the totality of the circumstances. In re Wood, 122 B.R. at 115; In re Kuhlman, 118 B.R. at 739. The Eighth Circuit Court of Appeals has held that the determination of disposable income is a "fact intensive inquiry into whether the debtor has 'income which is in excess of that reasonably required for maintenance and continuation of [its] farming operation from one year to the next.'" Broken Bow Ranch, Inc., v. Farmers Home Administration, (In re Broken Bow Ranch, Inc.,) 33 F.3d 1005, 1008 (8th Cir. 1994) (emphasis in the original) (quoting In re Coffman, 90 B.R. 878, 885 (Bankr. W.D. Tenn.1988)). In essence, the calculation is done by computing the sum by which the debtor's income is in excess of the obligations at the end of the plan, after taking into consideration the amount of funds necessary to continue the farming operation. In re Broken Bow Ranch, 33 F. 3d at 1009.

While debtors should be allowed a reasonable year-to-year carryover, debtors should not be allowed to accumulate an unreasonably large amount of funds such as would constitute a windfall at the time of discharge. In re Coffman, 90 B.R. at 888 In the present case, the debtors have not accumulated a large amount of wealth nor have they spent a large amount of funds either personally or for their business. The funds and real estate which were inherited were reasonably necessary for and used for the care of the debtor or the debtors' dependents or for the continuation of the farming operation.

#### The Cash

Mrs. Petersen received \$7,500.00 as a fee for serving as personal representative of her father's estate. This amount was included by the debtors as wages in the quarterly reports and has been already included in the debtors' calculations of disposable income. This money was used for the living expenses of the debtors as well as for farming operations. It is, therefore, not disposable income.

The remaining amount of cash that Mrs. Petersen inherited was income for the purposes of the disposable income test. Mr. Petersen did attempt to report the net amount received both on his quarterly operating report for 1995 and the accounting that was filed with the court in 1996. Although Mr. Petersen's accounting methods are somewhat confusing, he did make a good faith attempt to report the net inheritance and did include it in his calculations.

Mr. Petersen testified, without contradiction, that all monies received were put back into the farming operation and used to maintain the farming business. Section 1225 specifically states the funds that are utilized either for the care of the debtor or the debtor's dependents or for the preservation, continuation and operation of the debtor's business are not disposable income. These funds were used for the farming operation and are, therefore, not disposable income.

#### The Real Estate

Mrs. Petersen also inherited an undivided one-third interest in real estate which was inherited by herself and two of her sisters. This property was rented and farmed by Mr. Petersen both prior to the death of Mrs. Petersen's father and since that time. Mrs. Petersen's one-third share of the land rent is reported as rental income received and the payout of rent is accounted for as a disbursement. The liquidation value of Mrs. Petersen's interest in the real property is estimated by the debtors at \$43,500.00. The question presented is whether the value of the real property itself is "disposable income."

The Eighth Circuit Court of Appeals has interpreted the disposable income requirement broadly to include many different types of income. In re Koch, 109 F.3d 1285, 1289 (8<sup>th</sup> Cir. 1997) (Worker's Compensation Benefits); In re Broken Bow Ranch, Inc., 33 F.3d 1005 (8<sup>th</sup> Cir 1994) (government program payments earned during the plan period but received after the end of the plan).

In Berger v. Pokela (In re Berger), 61 F.3d 624 (8th Cir. 1995), the Eighth Circuit Court of Appeals held that disposable income included the value of the equity in property which was created upon the gratuitous forgiveness of a debt formerly secured by real property. In Berger, the mother of one of the debtors held a mortgage upon the debtors' property. Upon the Chapter 12 filing, the mother's claim was listed as \$45,000.00. However, before completion of the plan, she forgave the indebtedness by filing a release of the \$45,000.00 secured debt. Due to this forgiveness, the debtors realized equity in the property. The Circuit Court held that the value of the equity in the land that was obtained during the plan period should be treated as property of the estate and that the value should be available to unsecured creditors. The

Court reasoned that 28 U.S.C. § 1207 states that a debtor's estate includes all property or income received after the Chapter 12 petition is filed but before the case is closed.

In the present case, the debtors testified that the land is being rented by them and all income received by Mrs. Petersen from the rental of this property has been reported. This land was farmed by the debtors and the revenue received by the debtors from the rental income and from the crops produced on the land apparently helped fund the plan. The "value of the equity" in the inherited land has been included in the disposable income calculation by the inclusion of the proceeds of crop production and the payment and receipt of rental income.

The land is "reasonably necessary for the continuation, preservation or operation of the debtor's business." Mr. Petersen is currently farming the land and will continue to do so. The value of the land is represented by the rents paid to the owners. The debtors report the rents paid and the rents received on the quarterly operating reports. If, in addition to the stream of rental payments from the land, the liquidation value must be made available to creditors, then the land would have to be sold to provide that cash for distribution to creditors. If the land is sold, the debtors would have no farming business to continue. Such a result is certainly not the purpose of Chapter 12, which was enacted to save the family farm.

#### Conclusion

The inheritance has been properly accounted for in the overall operation of the farm business and these debtors have no "disposable income" as that term is defined at 11 U.S.C. § 1225(b)(2). A discharge shall be granted upon submission of a proposed order. If the Trustee declines to sign off on such an order, counsel for the debtors may submit it without such signature, accompanied by a letter explaining the situation.

Separate journal entry to be filed.

DATED: April 10, 2000.

BY THE COURT:

/s/Timothy J. Mahoney  
Chief Judge

Copies faxed by the Court to:

4 LYDICK, RICHARD  
20 DUNCAN, HOWARD T.

Copies mailed by the Court to:

Charles Meyer, P.O. Box 289, Stanton, NE 68779-0289  
United States Trustee

Movant (\*) is responsible for giving notice of this journal entry to all other parties (that are not listed above) if required by rule or statute.

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DEBTOR(S) ) CH. 12  
) Filing No.  
)  
Plaintiff(s) )  
vs. ) JOURNAL ENTRY  
) DATE: April 10, 2000  
\_\_\_\_\_  
Defendant(s) ) HEARING DATE: March 21, 2000

Before a United States Bankruptcy Judge for the District of Nebraska regarding Motion to Modify Plan to Increase Payments to Unsecured Creditors.

APPEARANCES

Charles Meyer, Attorney for debtors  
Howard Duncan, Attorney for Stanco, Inc.  
Richard Lydick, Chapter 12 Trustee

IT IS ORDERED:

The inheritance has been properly accounted for in the overall operation of the farm business and these debtors have no "disposable income" as that term is defined at 11 U.S.C. § 1225(b)(2). A discharge shall be granted upon submission of a proposed order. If the Trustee declines to sign off on such an order, counsel for the debtors may submit it without such signature, accompanied by a letter explaining the situation.

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