UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF	)	
	)	
WILLOW GROVE PARTNERSHIP,	)	CASE NO. BK87-696
	)	
DEBTOR	)	Chapter 12

ORDER DENYING CONFIRMATION

Hearing on the second and third modifications and amended Chapter 12 plan was held in North Platte, Nebraska, on October 7, 1987. Appearing on behalf of the debtor was George Vinton of North Platte, Nebraska. Appearing on behalf of the Bank of Valentine, objecting creditor, was Geoffrey V. Pohl of Omaha, Nebraska.

In this unusual Chapter 12 case, the objecting creditor, Bank of Valentine, is, by agreement of the parties and in reality, an oversecured creditor. The allowed amount of its secured claim is $581,558.59 plus accruing interest, costs and appropriate attorney fees. The value of the collateral securing this obligation exceeds $900,000. The note representing the claim of the Bank is secured both by real estate and by personal property, including livestock.

The creditor is not inclined to continue as the operating lender for this ranching operation.

The debtor proposes to divide the claim of the creditor into two separate obligations, one secured by real estate, with the note representing an obligation of approximately 80% of the value of the real estate. The other note would be secured by the personal property.

The creditor objects to this treatment on several grounds. First, the creditor alleges that under Section 552 and Section 1225 the plan cannot be confirmed without the creditor retaining its lien and that its lien covers proceeds and offspring of the livestock and further that its lien is a property right which cannot be modified by a Chapter 12 plan. In other words, the creditor says that it has a cross-collateralized secured claim and the debtor cannot divide the claim into two parts and secure each part separately and with no cross collateralization.

The creditor further argues that to permit such a change in its status would change it from a highly oversecured creditor to one which could easily become undersecured depending upon the value of the real estate. The creditor suggests that the debtor would be able to obtain sufficient funds to pay off that portion of the claim which was secured by the livestock and leave the creditor only with real estate of questionable future value.

These provisions of the plan, suggests the creditor, violate its constitutional rights concerning due process of law and the taking of property as well as violate the specific provisions of the Bankruptcy Code.

The debtor argues that since this creditor is in an oversecured position and will not fund the operation, the creditor has the power to kill this Chapter 12 case which is certainly in violation of the intent of Congress when it passed Chapter 12. Debtor needs operating funds and without provisions such as it has suggested, it will not be able to grant a lien prior in right to that of the Bank to a future operating lender. Without such power to grant such a lien to a future operating lender, the debtor suggests that it will not be able to obtain funding. Debtor believes that under Section 1222 it should be permitted to modify the rights of the secured creditor and such modification can be so drastic as to change the terms of the note and to change the type of collateral securing the note.

Section 1325(a)(5)(B)(i) is the equivalent for Chapter 13 cases of Section 1225(a)(5)(B)(i). Section 1325 has been construed to mean that not only must the secured creditor be permitted to retain the lien in order for confirmation to occur, but also that the lien must be the lien that was bargained for. According to 5 Collier on Bankruptcy, 15th Ed., Section 1325.06 "A lien on substitute or replacement collateral for that securing the claim at the outset will not meet this confirmation test without the consent of the holder of the claim, so a plan proposing to transfer the lien securing the allowed secured claim to other collateral is not entitled to confirmation without the acceptance of the holder of the claim."

Collier does not cite any case authority for this position but, for the purposes of this opinion, this Court will accept the Collier position. Since the language is identical under Chapter 12, this Court determines that substitute collateral or a reduction in collateral shall not be permitted.

Therefore, this plan cannot be confirmed as it stands. However, this case has been through two confirmation hearings and, as suggested at the beginning of the opinion, it is an unusual Chapter 12 case. This creditor is substantially oversecured. It claims to have veto power over a Chapter 12 plan because of its

security position. This Court does not agree that an oversecured creditor should have such veto power and the following discussion may suggest some alternatives for the parties.

As Collier suggests at p. 1325-33, § 1325(a)(5)(B)(i) merely requires a provision in the plan for the retention of the lien. However, the lien that is retained is for the purpose of securing the deferred payments proposed under the plan to the extent of the amount of the allowed secured claim. See Collier, p. 1325-34 at note 91. See also 124 Cong. Rec. H 11107 (Daily Ed. Sept. 28, 1978). What this seems to mean is that the secured creditor has the right to its lien and has the right to have its allowed secured claim protected by such lien during the plan payout period.

However, as this Court suggested in the case of In re Wobig, 73 B.R. 292 at 294, 295 (Bkrtcy. D. Neb. 1987), "If a plan is feasible and meets other confirmation requirements, the creditor only has a right to receive the allowed amount of its secured claim and retain a lien on collateral to the extent of the balance due on the allowed secured claim." Therefore, there should be a mechanism available for a debtor in a situation such as this to free up some of the value in the collateral which secures the allowed secured claim of the Bank so that a confirmable reorganization plan can be proposed.

It also appears that the drafters of the Bankruptcy Code considered this very problem when the original 1978 Code was adopted. Section 552(b) provides, as the creditor suggests, that a security interest created prior to bankruptcy extends to proceeds, product, offspring, rents or profits of the property in which the interest was granted except to any extent that the Court, after notice and a hearing and based on the equities of the case, orders otherwise. (Emphasis added).

Whether or not the equities of this case would convince this Court to decide that such post-petition security interest should be cut off, or to what extent such post petition security interest should be cut off, is a factual issue and shall be set for hearing.

This Court, at the time this opinion is written, has over 500 Chapter 12 cases pending. This Court speculates that fewer than 1% of these cases involve fact situations such as this in which the major creditor is significantly oversecured and still strenuously objects to the attempted reorganization of the debtor. The creditor has the absolute right to object to reorganization on whatever grounds are legitimate. The proposed division of the allowed secured claim and the reduction of collateral are major changes in the rights of the creditor. However, Congress anticipated that debtors would need the opportunity to use collateral subject to a prepetition lien. Congress provided a method whereby the matter could be brought before the Court and

the Court, after weighing the equities, could decide whether the State law contract rights of the creditor should continue to prevail to such an extent that the debtor could not reorganize, or whether the debtor should be granted an opportunity to attempt to reorganize. Such opportunity would result by affecting some of the rights of the secured creditor, such as by cutting off its lien to some extent, as long as the debtor could protect the interest of the creditor in receiving payment over time of the allowed amount of its secured claim.

This plan cannot be confirmed and confirmation is denied. An evidentiary hearing on the issues concerning Section 552(b) shall be set on an expedited basis.

DATED: October 16, 1987.

BY THE COURT:

Timothy J. Mahoney
U.S. Bankruptcy Judge

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