UNITED STATES BANKRUPTCY COURT
For the Southern District of Iowa

In the Matter of

WALTER MARLIN BROWN,
BURDEAN RUTH BROWN,
Debtors.

Case No. 87-46-C

Chapter 12

MEMORANDUM OF DECISION AND ORDER

On February 13, 1987 a motion for relief from stay filed on behalf of Deutz-Allis Credit Corporation (Deutz-Allis) on January 16, 1987 and a resistance thereto filed on behalf of the debtors on January 30, 1987 came on for telephonic hearing before this court in Des Moines, Iowa. Marlyn S. Jensen appeared on behalf of the debtors. Arnold D. Kenyon III appeared on behalf of Deutz-Allis. At the close of the hearing the parties were given three weeks to submit letter briefs.

On February 25, 1987 the debtors' motion requesting that Deutz-Allis account for security deposits filed on January 30, 1987 and a resistance thereto filed on February 24, 1987 came on for hearing before this court in Des Moines, Iowa. Marlyn S. Jensen appeared on behalf of the debtors and Timothy R. Kenyon appeared on behalf of Deutz-Allis. At the close of the hearing the parties were given ten days to submit letter briefs. Both matters were considered fully submitted on March 6, 1987.

FINDINGS OF FACT

1. Deutz-Allis and the debtors entered into various leases of farm machinery and equipment during the later part of 1984. Security deposits totaling $32,000.00 were given on four pieces of machinery. Deutz-Allis claims a security interest in the leased machinery and estimates the total sum owing at $238,652.00.

2. In 1986, Deutz-Allis commenced a replevin action in the United States District Court for the Southern District of Iowa (Civil No. 86-227-A). By order entered April 22, 1986 Deutz-Allis was permitted the immediate possession of the machinery in question and was required to post a $200,000.00 bond.

3. A hearing on Deutz-Allis' motion for summary judgment in federal district court was scheduled for January 9, 1987.

4. The debtors filed their Chapter 12 petition on January 8, 1987.

5. Deutz-Allis filed its motion for relief from the automatic stay on January 16, 1987.

6. The debtors filed a resistance to said motion on January 30, 1987. The debtors assert the various defenses already raised in the district court action. The debtors do not now want the property returned to them. Rather they seek a rescission of the contracts and restitution of the security deposits.

The debtors further state that the only item of machinery now in their possession is a small tractor/mower worth approximately $2250.00. They offer adequate protection payments of 8 percent of this value until their Chapter 12 plan is confirmed. The debtors further assert that the $32,000.00 security deposits provide Deutz-Allis adequate protection of its interest.

7. On January 30, 1987 the debtors filed a motion pursuant to 11 U.S.C. section 542(a) requesting that Deutz-Allis account for security deposits. The debtors assert their belief that security deposits have been transferred to another entity and their need to know the present location in order to commence an action for turnover.

8. In its brief filed March 6, 1987 Deutz-Allis asserts that the balance of the debts due far exceed the value of the machinery secured and the security deposits held. Deutz-Allis values the machinery at $96,250.00. This figure plus the $32,000.00 security deposit equals $128,250.00. Deutz-Allis further asserts that the property is not necessary for an effective reorganization as the debtors seek to rescind the lease agreements and do not want the return of the property.

9. The debtors filed their Chapter 12 plan on April 12, 1987. The debt to Deutz-Allis is treated as a class 6 and 7 claim. The debtors plan to release all claim to equipment now in the creditor's possession in exchange for a turnover of the security deposit plus 9.7 percent interest from December 29,

1984. This sum comprises the majority of income to fund the plan in 1987.

ANALYSIS

The requirements for obtaining relief from the automatic stay are contained in 11 U.S.C. section 362(d) which provides:

> (d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay --
>
> > (1) for cause, including the lack of adequate protection of an interest in property of such party in interest; or
> >
> > (2) with respect to a stay of an act against property under subsection (a) of this section, if
> >
> > > (A) the debtor does not have any equity in such property; and
> > >
> > > (B) such property is not necessary to an effective reorganization.

The concept of adequate protection referred to in section 362(d)(1) is not specifically defined in the Code. Rather, what constitutes adequate protection is a factual question to be determined on a case by case basis. In re Briggs Transp. Co., 780 F.2d 1339, 1349 (8th Cir. 1985). Section 361 of the Bankruptcy Code lists three nonexclusive means by which adequate protection may be provided. Pursuant to 11 U.S.C. section 1205(a), the provisions of section 361 do not apply in Chapter 12 cases. Section 1205(b) provides separate tests for

adequate protection in Chapter 12 cases. Unlike section 361 which focuses on protecting "a decrease in the value of such entity's interest in such property" (sometimes called "lost opportunity cost"), section 1205(b) emphasizes "a decrease in the value of property securing a claim or of an entity's ownership interest in property".

The provisions of Chapter 12 do not appear to modify the application of section 362(d)(2) which provides an alternative means for relief from the automatic stay. Section 362(d)(2) does not address the concept of adequate protection. Rather, the stay may be lifted under section 362(d)(2) if two requirements are met: 1) the debtor lacks equity in the property, and 2) the property is not necessary to an effective reorganization.

The debtors and Deutz-Allis appear to agree that the value of the leased equipment is approximately $96,000.00 to $98,000.00. Adding the security deposit made brings the total value of the property to at least $128,000. Deutz-Allis claims a lien on the property for its total claim of approximately $238,632.00.[1] Even without resort to other encumbrances on the subject property it is apparent that the debtors have no equity in the property.[2] The court, therefore, must determine whether the property is necessary for an effective reorganization.

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[1] On April 30, 1987 Deutz-Allis filed proof of claim which apparently estimates the unsecured portion of its claim at $131,494.19.

[2] The debtors likewise have no equity in the small lawn and garden tractor. The tractor has been valued at approximately $2,250.00 and the balance due to Deutz-Allis is approximately $4,392.00.

Traditional notions of whether property is necessary for reorganization are inapplicable in the instant case. The debtors are in possession of one small lawn and garden tractor and wish to use that item as part of their plan of reorganization. The debtors do not seek the return or the use of the remainder of the property, now in the hands of Deutz-Allis. Instead the debtors seek the return of the security deposits made in connection with their lease agreements.[3] Having conceded that the return of the property is not sought, the debtors have not met their burden of establishing that the property is necessary for an effective reorganization. Accordingly, the court finds that the requirements of section 362(d)(2) have been established and relief from the stay is appropriate.

In resisting Deutz-Allis' motion for relief from stay the debtors have asserted the defenses originally raised in the creditor's replevin action in federal district court. The debtors contend that these defenses entitle them to the return of various security deposits. This court notes, however, that a hearing on relief from stay under section 362 is not the proper forum for deciding affirmative defenses or counterclaims by a debtor against a creditor. See In re Gellert, 55 B.R. 970, 974 (Bankr. N.H. 1985); In re Pappas,

[3] The debtors have not established that the security deposits in question are property of the estate so as to be subject to the stay provisions of the Code. The lessee's right to obtain the return of security deposits varies according to the language of the agreement. No agreement has been submitted in this case. Typically, however, such a deposit is designated as the equivalent of liquidated damages to be retained by the lessor. See Matter of Riviera, 280 F. Supp. 741, 750 (W.D. Mo.) aff'd. 390, 2d 556 (8th Cir. 1967) cert. denied, 391 U.S. 964 (1968).

55 B.R. 658, 660 (Bankr. Mass. 1985); In re Dennison, 50 B.R. 950, 953 (Bankr. E.D. Pa. 1985).

As one court stated:

> The debtor will frequently have, or be able to devise,....counterclaims against the secured creditor. Fraud, negligence, breach of contract, usury, interference with perspective business advantage, securities fraud, antitrust violations -- all are claims that a debtor might raise to challenge the debt. Allowing a debtor to raise these real or imagined claims, when a creditor files a complaint for relief from the automatic stay, could flood the bankruptcy courts with complex trials - including jury trials -- on every conceivable tort and contract counterclaim. Such a result does not accord with either the essential nature of a complaint for relief from stay, that of a hearing on a preliminary injunction, or with the intention of the drafters of the Bankruptcy rules, who gave calendar priority to these hearings.
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> The complaint to vacate the stay was not designed to initiate full adjudication on the merits of prior liens filed by a secured creditor, and it was error for the bankruptcy judge to consider affirmative defenses and counterclaims going to the merits and amount of Audubon's judgment.
>
> In conclusion, it is important to emphasize that the refusal to permit a bankruptcy court to adjudicate affirmative defenses and counterclaims going to the substance of a prior foreclosure proceeding in no way undermines the authority of that court to decide whether to continue the automatic stay. The bankruptcy judge must determine whether the Rolloffs have any equity in the foreclosed property. He must also decide whether the continuation of the stay will cause undue harm to Audubon. Finally, it is necessary that he evaluate

> whether there is a reasonable possibility of successful rehabilitation of the bankrupt and how such prospect will be affected should the encumbered property be withdrawn from the estate.
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> As for the Roloffs' assertion that they should be allowed to attack the prior judgment on the merits, it is enough to say that whatever right they may have to litigate that question must be exercised elsewhere and not in response to a complaint to vacate an automatic stay.

In re Roloff, 598 F.2d 783, 788 (3rd Cir. 1979). The legislative history of 11 U.S.C. section 362 is in accord. See S. Rep. No. 95-989, 95th Cong., 2d Sess. 55, reprinted in 1978 U.S. CODE, CONG. & ADMIN. NEWS 5787, at 5841.

The debtor's defenses include a claim that several of the items that were leased were contracted for as a result of false representation. The debtors seek rescission of such contracts, restitution of security deposits, and compensation for the time and money expended to repair several items. Rather than await an imminent decision on the merits of their claims in the creditor's replevin action, the debtors filed their petition in bankruptcy. Rather than object to the claim of this creditor or its assignor, the debtors raise these defenses in the context of a resistance to a motion for relief from stay. Review of the debtors' proposed Chapter 12 plan reveals that the debtors do not address the debt owing to Deutz-Allis. Instead they foresee a compromise wherein they will execute a release of all equipment in the possession of the creditor in

exchange for the turnover of the security deposits plus interest. Given the objection to the debtors' plan filed on behalf of Deutz-Allis on April 28, 1987 the debtors' proposed compromise is unrealistic. The debtors' entitlement to the return of security deposits could be quickly resolved in the original action in district court. Accordingly, relief from stay is warranted in order to permit Deutz-Allis to proceed on its action for replevin.

Given the court's finding that relief from the automatic stay is proper, it is unnecessary to rule upon the debtors' motion under section 542(a) that Deutz-Allis account for security deposits.

THEREFORE, IT IS ORDERED that, based on the foregoing analysis, the motion for relief from stay filed by Deutz-Allis is granted.

Signed and filed this 26th day of June, 1987.

LEE M. JACKWIG

U.S. BANKRUPTCY JUDGE