

UNITED STATES BANKRUPTCY COURT  
For the Southern District of Iowa

In the Matter of  
JAMES L. JUNGNANN,

Case No. 87-3013-C  
Chapter 12

Debtor.

ORDER - OBJECTION TO PLAN

On February 16, 1988, the preliminary hearing on confirmation of Debtor's Chapter 12 Plan was held. Jerrold Wanek appeared on behalf of Debtor; David L. Davitt appeared on behalf of creditor Federal Land Bank of Omaha; the Chapter 12 Trustee, Anita L. Shodeen, appeared; and Kevin R. Query, Assistant U.S. Attorney, appeared on behalf of Farmers Home Administration (hereinafter "FmHA").

This is a core proceeding pursuant to 28 U.S.C. §157(b)(2)(L). The Court, having reviewed the file, briefs, and arguments of counsel, now enters its findings and conclusions pursuant to F.R. Bankr. P. 7052.

FINDINGS OF FACT

1. Debtor owns farm real estate in Dallas and Madison Counties, Iowa, and has been engaged in farming since 1967.

2. Debtor executed a real estate mortgage on August 5, 1981, in which Debtor mortgaged to the government his interest in real estate located in Madison County.

3. The granting clause of the mortgage gave FmHA an interest in described real estate together with all rights and interests of the Debtor to "rents, issues, and profits

thereof and revenues and income therefrom" and "all payments at any time owing to Borrower by virtue of any sale, lease, transfer, conveyance, or condemnation" of any part of the real estate.

4. Debtor executed a security agreement with FmHA in 1982, giving FmHA a security interest in crops, present and future, equipment, inventory, livestock, and farm products and supplies. Debtor also executed security agreements on October 27, 1983, April 12, 1984, and October 3, 1986. Commencing with the security agreement of October 27, 1983, Debtor also gave FmHA a security interest in all accounts, contract rights and general intangibles. FmHA perfected its security interest with a financing statement filed with the Iowa Secretary of State on April 1, 1982, an amendment filed on March 26, 1984, and a continuation filed on December 17, 1986.

5. On February 26, 1987, Debtor entered into a Conservation Reserve Program (hereinafter "CRP") contract with the Commodity Credit Corporation whereby Debtor agreed to place designated acreage into the CRP for a period of ten years. As a condition of this contract, Debtor agreed to implement the conservation plan by planting and growing grasses and legumes to reduce and ameliorate the effects of erosion and by controlling the growth of weeds.

6. On December 10, 1987, Debtor filed a Chapter 12 petition.

7. The Court takes judicial notice that FmHA filed its claim on February 16, 1988. The claim recited that Debtor is indebted to FmHA in the total sum of \$359,200.17. FmHA alleged its claim was secured as a result of real estate mortgages filed in the county recorder's office, financing statements filed with the Secretary of State of Iowa, and security agreements.

8. FmHA's claim asserts the amount secured on real estate is \$39,079.00. It lists the market value of the real estate as \$87,879.00 subject to prior liens of \$48,800.00 showing a balance of \$39,079.00.

9. The claim asserts the market value of chattels is \$13,132.00.

10. FmHA asserts its secured claim is in the amount of \$52,211.00 (\$39,079 + \$13,132), and its unsecured claim is in the amount of \$306,989.17.

11. Debtor filed his Plan of Reorganization (hereinafter "Plan") on January 8, 1988.

12. Article II of the Plan provided that Debtor would pay a cash sum to the Trustee on December 15 of each year. Debtor then provided that the Trustee was to collect a percentage fee pursuant to 11 U.S.C. §1202(d) (2) from all of said payments. All claims paid in full or in part through the Trustee would be credited in full, without deduction for a Trustee's fee, on the date the Trustee received a payment.

13. Debtor treated impaired secured claims in Article

IV, Class 3. In Appendix 2, FmHA was given an allowed secured claim in real estate for \$38,168.62 and the balance of the claim, \$331,751.52, was treated as an unsecured claim under Class 4. pursuant to Class 4, unsecured claims, the creditors holding allowed unsecured claims are to be paid to the extent of one cent on each dollar.

14. Article V of the Plan provided for lien avoidance. Debtor listed property as exempt tools of trade and household goods pursuant to Iowa Code §627.6 (1987). Debtor then provided that unless timely objection was filed, the judicial or non-possessory, non-purchase money liens encumbering said assets would be avoided and said property would vest in Debtor free and clear of any lien, claim or interest of any of the creditors, and the claims of said creditors would be allowed as unsecured claims.

15. Debtor treated Executory Contracts in Article VI. Appendix 5 listed a 10-year CRP contract with the Commodity Credit Corporation as current in status and that Debtor was assuming said contract. No value was given to the contract.

16. The FmHA filed an objection and asserted the value of its allowed secured claim should include a valuation for the CRP contract. Debtor argues the CRP contract should not be included in determining the value of FmHA's allowed secured claim because said contract was completely executory

on the date Debtor's petition was filed and this constitutes post-discharge income.

#### ISSUES

The Farmers Home Administration has raised the following objections to this Plan:

1. FmHA objects to Article V in that Section 522(f) lien avoidance is not permitted under §1225;

2. FmHA objects to the Debtor's proposed satisfaction of Trustee's fees out of funds due the creditors;

3. Debtor in proposing a payment of 1% of the unsecured claims does not propose a plan of reorganization in good faith; and

4. Debtor's CRP contract should be assigned a value as part of FmHA's allowed secured claim.

#### DISCUSSION

I. Lien Avoidance. FmHA's first objection to Debtor's Plan is that section 522(f) lien avoidance is not permitted under section 1225. This objection must fail because the Court has recently decided that lien avoidance is available in the Chapter 12 case. Matter of Simmons, \_\_\_\_ B.R. \_\_\_\_ (Bankr. S.D. Iowa 1988); Matter of Ferrari, No. 87-2841-C, unpub.op. (Bankr. S.D. Iowa May 6, 1988). However, the actual avoidance of the lien cannot occur until Debtor's discharge becomes effective pursuant to section 1228. Id.

II. Trustees Fees. FmHA's second objection to Debtor's Plan concerns Debtor's proposed satisfaction of Trustee's fees out of the funds due the creditors. The Court recently ruled on the identical issue in Matter of Sesker, No. 87-3014-C, unpub. op. (Bankr. S.D. Iowa June 10, 1988). In Sesker, the Court concluded that section 1225(a) (5) (B) (ii) requires the debtors' payment of trustee's fees to be a payment in addition to the required present value payments to secured creditors. Id. Thus, since the debtors were paying the trustee's fees out of the funds due creditors, the Court held the debtors' proposed plan violated section 1225(a) (5) (B) (ii).

In the case at bar, Debtor's Plan contains the identical Trustee's fees payment provision the Court rejected in Sesker. Therefore, FmHA's objection must be sustained because the Trustee's fees payment provision violates section 1225(a) (5) (B) (ii)

III. Good Faith. FmHA's third objection is that by proposing a payment of 1% of the unsecured claims, Debtor does not propose a plan of reorganization in good faith. Section 1225 provides in relevant part:

(a) Except as provided in subsection (b), the court shall confirm a plan if--

(3) the plan has been proposed in good faith and not by any means forbidden by law....

(b) (1) If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the court may not approve the plan unless, as of the effective date of the plan--

(B) the plan provides that all of the debtor's projected disposable income to be received in the three-year period, or such longer period as the court may approve under section 1222(c), beginning on the date that the first payment is due under the plan will be applied to make payments under the plan.

11 U.S.C. §1225. Since FmHA is partially secured and partially unsecured, its objection to Debtors Plan requires the Court to address the disposable income concern under §1225(b)(1)(B) and how it relates to the good-faith requirement of §1225(a) (3).

The Court in In re Kjerulf, 82 B.R. 123 (Bankr. D.Or. 1987), addressed the identical issue of whether a court can confirm a Chapter 12 plan which provides for zero or nominal repayment to unsecured creditors. The Court initially noted that two courts have stated, in dictum, that concerning "good faith", a Chapter 12 plan can provide that unsecured creditors will receive nominal or no payment. *Id.* at 12526, citing In re Big Hook Land & Cattle Co., 77 B.R. 793 (Bankr. D. Mont.1987); In re Citrowske, 72 B.R. 613 (Bankr. D.Minn. 1987). The Court went on to determine that a plan is not proposed in bad faith solely because it provides for zero or nominal repayment to unsecured creditors. Id. At 127.

In the case at bar, Debtor proposes to pay unsecured creditors 1% of their claims. There is no evidence indicating Debtor is not applying all his disposable income over the life of the plan in violation of section 1225(b)(1)(B). Therefore, the Court concludes Debtor's Plan is proposed in "good faith" pursuant to section 1225(a) (3).

IV. Conservation Reserve Program Contract. FmHA's final objection is that Debtor's CRP contract should be assigned a value as part of FmHA's allowed secured claim. This objection raises the issue of whether FmHA has a valid interest in Debtor's CRP payments under the terms of the mortgage. The granting clause of the mortgage gave FmHA an interest in Debtor's real estate together with an interest in all rights and interests in, among other things, the "rents, issues, and profits thereof and revenues and income therefrom...." Thus, the issue becomes whether Debtor's CRP payments are "rents and profits" under the mortgage.

In determining whether CRP payments are "rents and profits" under the mortgage, the Court must consider the statutory and regulatory provisions governing the CRP and the case law interpreting such. The goal of the CRP is to idle highly erodible crop land for a ten-year period and to plant it with protective cover in exchange for annual payments. Payments made under the CRP are specifically denominated as "rental payments" in the statutory and regulatory provisions governing the CRP. See 16 U.S.C.



§§3831-3834 (Cum.Supp. 1988); 7 C.F.R. §§704.2(a)(2), 704.13(a)(2), 704.16 (1988). In addition, numerous courts have determined that CRP payments are in the nature of rental payments. In re Harvie, 84 B.R. 197, 199-200 (Bankr. D. Cob. 1988); In re Waters, 83 B.R. 594, 613-14 (Bankr. N.D. Iowa 1988); In re Clark, 82 B.R. 131, 132-33 (Bankr. D. Cob. 1987); In re Ratliff, 79 B.R. 930, 931-32 (Bankr. D. Cob. 1987); contra Matter of Butz, 86 B.R. 595, 598 (Bankr. S.D. Iowa 1988). Given the plain language in the statute and regulations governing the CRP plus the weight of authority, the Court concludes CRP payments are in the nature of rental payments.

Characterization of CRP payments as rental payments does not automatically mean said payments are subject to a "rents and profits" mortgage clause. Rather, the Court must determine whether said payments can be construed as "rents and profits" under state law. The Iowa Supreme Court has construed the phrase "rents, issues, and profits" as follows:

The phrase "rents, issues and profits" as distinguished from the land itself refers to the products of the land, the annual rentals, the income derived therefrom, whether in money or in products. It has been said that "to cultivate and have the use of the lands is to receive the rents and profits." Where one by lease agrees to pay a certain sum for the right to cultivate and use the land, the sum so stipulated is rent, and represents the landlord's share in the issues and profits of the land, and where the lease provides for share of the crop, the share of the crops represents the landlord's portion of the

issues and profits derived from the use and cultivation of the land. Part of it may be paid in cash and part of it in crops and products. The word "profits" as used in the phrase "rents, issues and profits" is synonymous with "rents."

Equitable Life Ins. Co. of Iowa v. Brown, 220 Iowa 585, 590, 262 N.W. 124, 127 (1935) (authorities omitted). This Court agrees with Judge Melloy in Waters, 83 B.R. at 614, that under the above definition, the CRP annual rental payments are in the nature of rents, issues, and profits from the use and ownership of the land. As a result, Debtor's CRP payments are subject to FmHA's claim as mortgagee under the rents and profits clause of the mortgage.

V. Post Petition Security Interest. Debtor argues that pursuant to Bankruptcy Code section 552 (a), the CRP payments are post-discharge income not subject to FmHA's security interest because the CRP contract was completely executory on the date Debtor filed his petition. However, Debtor's argument is not persuasive. Section 552 provides:

(a) Except as provided in subsection (b) of this section, property acquired by the estate or by the debtor after the commencement of the case is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case.

(b) Except as provided..., if the debtor... entered into a security agreement before the commencement of the case and if the security interest created by such security agreement extends to property of the debtor acquired before the commencement of the case and to proceeds, product, offspring, rents, or profits of such property, then such security interest extends to such proceeds, product,

offspring, rents, or profits acquired by the estate after the commencement of the case to the extent provided by such security agreement and by applicable nonbankruptcy law, except to any extent that the court, after notice and a hearing and based on the equities of the case, orders otherwise.

11 U.S.C. §552. FmHA's mortgage granting clause, which conveyed an interest in Debtor's real estate rents and profits, was effective between FmHA and Debtor from the date of execution of the mortgage. Federal Land Bank of Iowa v. Lower, 421 N.W.2d 126, 129 (Iowa 1988). Said mortgage was executed over six years before Debtor commenced his bankruptcy case. As a result, under section 552(b), FmHA's interest in rents and profits (the CRP payments) continues in rents and profits acquired by the estate post-petition except to the extent the Court, after notice and hearing, and based upon the equities of the case, orders otherwise. Debtor has not convinced the Court that the equities of the case require the Court to modify FmHA's rights in the post-petition rents and profits. Thus, Debtor's argument that section 552 cuts off FmHA's post-petition security interest in CRP payments is without merit.

#### CONCLUSION AND ORDER

WHEREFORE, based on the foregoing analysis, the Court concludes the following:

- 1) Lien avoidance is available in Chapter 12;
- 2) Section 1225(a) (5) (B) (ii) requires Debtor's payment

of trustee's fees to be a payment in addition to the required present value payments to secured creditors;

3) Debtor's proposal of paying 1% of the unsecured claims does not result in a lack of "good faith" filing; and

4) CRP payments are "rents and profits" under FmHA's mortgage and must be assigned a value as part of its secured claim.

IT IS ACCORDINGLY ORDERED that FmHA's objections to Debtor's Plan are sustained in part and overruled in part.

Dated this 21<sup>st</sup> day of September, 1988.

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RUSSELL J. HILL  
UNITED STATES BANKRUPTCY JUDGE