Ag Lending in a Down Economy: Ag Liens, Secured Transactions and Best Practices

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Ag Lending in a Down Economy: Ag Liens, Secured Transactions and Best Practices

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Agenda
- Agricultural workouts (and unique issues)
- Statutory agricultural liens
- Agricultural bankruptcy

Agricultural workouts
- Understand the borrower and borrower’s operation
  - Critical borrower issues and objectives
  - Obtaining information from borrower (status and location of crops/livestock, expected sales, material contracts, short term operating needs, etc.)
  - Collateral review and inspection; documentation
- Review loan documents
- Review title encumbrances and UCC-1 filings
- Use of workout or forbearance agreement
  - Require additional sources of repayment or collateral
  - Correct attachment or perfection issues
  - Obtain lender release
  - Require partial liquidation of collateral (in re Hall, 617 F.3d 1161 (2012) issue)
  - Measurable objectives
  - Offer a “carrot” (discounted payoff, debt held in abeyance, lien release, etc)

Statutory Agricultural Liens
- Revised Article 9
  - A security interest is “an interest in personal property or fixtures which secures payment or performance of an obligation”. UCC §9-315(a). Serves as “blanket” security interest on identifiable proceeds. UCC §9-315(a).
- Interplay between Revised Article 9 and Statutory Agricultural Liens
  - Prior to the adoption of Revised Article 9 in 2001, statutory liens were not incorporated into Article 9. Statutory liens were stand alone liens. With the adoption of Revised Article 9 statutory agricultural liens were partially incorporated into Revised Article 9. UCC §§ 9-102(a)(5), 9-109(a)(2) and 9-302. Revised Article 9 controls the law that governs the agricultural liens, however, Revised Article 9 does not control the attachment, perfection and priority of agricultural liens. UCC §9-302. Comment 2.
Statutory Agricultural Liens

- **Agricultural Liens under Revised Article 9**
  - **Livestock**
  - **Crops**

- **Provisions Revised Article 9**
  - **State statute must provide that an agricultural lien arises in such proceeds and only then will the rules of Article 9 apply to the lien on such proceeds.**
  - **Proceeds**
    - Miss. 118-201(a)(1)
    - Utah Code Ann. 11-338.01(a)(1)
    - Ark. Code Ann. 18-41-101(a)
    - Miss. Code Ann. 85-7-11(a)

- **Priority**
  - **Refined Article 9** First to file: UCC § 9-322(a)(2).
  - **Statutory Agricultural Liens** A perfected agricultural lien has priority over a conflicting perfected security interest or agricultural lien. UCC § 9-322(a)(2).

Statutory Agricultural Liens

- **Scope and attachment**
  - **Great Western Bank v. William Poultry, 786 N.W.2d 437 (N.D. March 23, 2010)** (North Dakota “feed supplier” lien extends to unpaid young stock)
  - **In re Voss, 426 B.R. 326 (Bankr. March 24, 2010)** (North Dakota “feed supplier” lien extends to unpaid barn rent but does not extend to unpaid barn repairs and damage caused to a tractor). 

- **Perfection**
  - **Revised Article 9. Under Article 9, a security interest must be perfected in order to obtain any priority over competing security interests and other agricultural liens since conflicting security interests and agricultural liens are generally afforded priority on a first to file or perfect basis. UCC § 9-322(a).**
  - **Statutory Agricultural Liens. An agricultural lien is perfected if it has become effective and all of the applicable requirements for perfection under Article 9 have been satisfied.**

- **State of perfection**
  - **Revised Article 9. The state the debtor is located. UCC § 9-301.**
  - **Statutory Agricultural Liens. The state the farm product is located. UCC § 9-303.**

Statutory Agricultural Liens

- **Crops/Livestock that Move to Another State**
  - **UCC § 9-316 provides that an Article 9 security interest remains perfected if the collateral moves to another state. However, UCC § 9-316 does not apply to agricultural liens. See Comment 7.**
  - **Example 10. Supplier holds an agricultural lien on corn. The lien arises under an Iowa statute. Supplier perfects by filing a financing statement in Iowa, where the corn is located. UCC § 9-302. Debtor stores the corn in Missouri. Assume the Iowa agricultural lien survives or an agricultural lien arises under Missouri law (though this Article does not govern). Once the corn is located in Missouri, Missouri becomes the jurisdiction whose law governs perfection. UCC § 9-302. Thus, the agricultural lien will not be perfected unless Supplier files a financing statement in Missouri.**


- **Iowa**
  - **Great Plains National Bank v. William Poultry, 786 N.W.2d 437 (N.D. March 23, 2010)** (North Dakota “feed supplier” lien extends to unpaid young stock)

- **Ohio**
  - **Lisco State Bank v. McCombs Ranches, Inc, 752 F. Supp. 2d 1008 (N.D. Ohio 2010)** (failure to identify debtor’s social security number should be directed to notice)

- **Iowa**
  - **Great Plains National Bank v. William Poultry, 786 N.W.2d 437 (N.D. March 23, 2010)** (North Dakota “feed supplier” lien extends to unpaid young stock)

- **Pennsylvania**

Buyer of Farm Products (Federal Food Security Act)

- **Applicable to agricultural liens “as created by the seller” issues?**
  - **Direct notice states (Tennessee and Arkansas)**
    - **Strict Compliance**
      - Farm Credit MidSouth, PCA v. Farm Fresh Carnish Company, 371 F.3d 450 (8th Cir. 2004)
      - State Bank of Cherry v. CGB Enterprises, Inc., 924 N.E.2d 604 (Ill. Ct. App. 2012) (failure to identify county where crops were grown invalidates notice)
      - CNH Capital v. Taker Grain and Supply Co. (In re Pridi), 2012 BNA NEWS 4506
  - **Substantial Compliance**
    - First Nat’l Bank & Trust v. McIntyre County Cooperative Ass’n, 897 F.2d 144 (3rd Cir. 1990)
    - Farm Credit Services of America, PCA v. Raly, Inc., 663 N.E.2d 637 (Ohio Ct. App. 1996)

- **Iowa**

Ag Lending, 3
Statutory Agricultural Liens

- Representing the Bank (Article 9 secured lender)
  - Attachment.
    - Did the livestock actually consume or did the crops actually benefit from the goods/services provided by the lien claimant?
    - Is the lien claimant able to identify the proceeds from the sale of livestock or crops that actually consumed or benefited from the goods/services provided?
    - Does the state lien statute provide that the lien attaches to the proceeds from the sale of the livestock or crops? See UCC §9-315, cmt 9.
  - Perfection.
    - Did the lien claimant file the lien in the state that the livestock/crops were located? See UCC §9-302.
    - Did the livestock or crops go into another state, and if so, did the lien claimant properly perfect in the new state? See UCC §9-316, cmt 7.

Statutory Agricultural Liens

- Representing the Agricultural Lien Creditor
  - Agricultural lien properly perfected?
  - Multi-state issue. Were the livestock/crops moved outside of the state where the lien was perfected? Should the lien claimant also perfected in the state where the livestock/collateral were transferred to or sold?
  - Identifiable proceeds issue. Does the state agricultural lien statute provide that the lien extends to the proceeds of the livestock/crops? Should the lien claimant file (for central filing states) or give notice (for direct notice states) to farm product buyers to limit the commingling of livestock/crop proceeds?

Agricultural Bankruptcy

- Chapter 12
  - Access to cash collateral; cash collateral and adequate protection agreed order
  - Acknowledgment of claim; perfection
  - Cash collateral budget
  - Adequate protection payments
  - Timeliness to file and confirm Chapter 12 plan
  - Events of default
  - Rights/remedies in the event of default; “drop-dead” stay relief
  - Confirmation issues
    - Eligibility
    - Plan terms
    - Feasibility
  - Related issues
    - Non-dischargeability action
    - Related parties; co-debtor stay issues
    - Adverse actions against buyers of farm products

Conclusion

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Ag Lending, 4
### Differences Between Security Interest and Agricultural Lien

<table>
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<tr>
<th><strong>Article 9 Security Interest</strong></th>
<th><strong>Statutory Agricultural Liens</strong></th>
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<tbody>
<tr>
<td>A security interest is &quot;an interest in personal property or fixtures which secures payment or performance of an obligation.&quot;</td>
<td>An &quot;agricultural lien&quot; is: &quot;an interest, other than a security interest, in farm products: (A) which secures payment or performance of an obligation for: (i) goods or services furnished in connection with a debtor's farming operation; or (ii) rent on real property leased by a debtor in connection with its farming operation; (B) which is created by statute in favor of a person that: (i) in the ordinary course of its business furnished goods or services to a debtor in connection with a debtor’s farming operation; or (ii) leased real property to a debtor in connection with the debtor’s farming operation; and (C) whose effectiveness does not depend on the person’s possession of the personal property.&quot; 9-102(a)(5).</td>
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<tr>
<td>The law of the jurisdiction in which the debtor is located governs perfection, the effect of perfection or nonperfection, and the priority of an agricultural lien.</td>
<td>The law of the jurisdiction in which farm products are located governs perfection, the effect of perfection or nonperfection, and the priority of an agricultural lien. This choice of law provision will require secured parties who are relying upon an agricultural lien to perfect their agricultural lien by filing a financing statement in the state to which farm products are transported by the debtor if they are removed from the state in which they were produced.</td>
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<tr>
<td>Under Article 9, a security interest must be perfected in order to obtain any priority over competing security interests and other agricultural liens since conflicting security interests and agricultural liens are generally afforded priority on a first to file or perfect basis. 9-322(a).</td>
<td>Under Article 9, an agricultural lien must be perfected in order to obtain any priority over competing security interests and other agricultural liens since conflicting security interests and agricultural liens are generally afforded priority on a first to file or perfect basis. 9-322(a). An agricultural lien is perfected if it has become effective and all of the applicable requirements for perfection under Article 9 have been satisfied. 9-308(b). A financing statement must be filed in order to perfect an agricultural lien. 9-310(a). Possession is not available as a means of perfection for agricultural liens. 9-313(a).</td>
</tr>
<tr>
<td>9-315 (a) provides that a security interest or an agricultural lien continues in collateral notwithstanding its sale, lease, license, exchange or other disposition unless the secured party authorized the disposition free of the security interest or agricultural lien. However, 9-315(a)(2) provides that only a security interest attaches to identifiable proceeds of collateral.</td>
<td>9-315 (a) provides that a security interest or an agricultural lien continues in collateral notwithstanding its sale, lease, license, exchange or other disposition unless the secured party authorized the disposition free of the security interest or agricultural lien. If the enabling statute provides that an agricultural lien arises in such proceeds, then the rules of Article 9 applicable to agricultural liens will apply to the lien on such proceeds. Comment 9, 9-315.</td>
</tr>
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Security interests generally have priority according to priority in time of filing or perfection. 9-322(a)(1). A perfected security interest has priority over a conflicting unperfected security interest or agricultural lien. 9-322(a)(2). The first security interest or agricultural lien to attach or become effective has priority if a conflicting security interest or agricultural lien is unperfected. 9-322(a)(3).

As with security interests, agricultural liens generally have priority according to priority in time of filing or perfection. 9-322(a)(1). A perfected agricultural lien has priority over a conflicting unperfected security interest or agricultural lien. 9-322(a)(2). The first security interest or agricultural lien to attach or become effective has priority if a conflicting security interest or agricultural lien is unperfected. 9-322(a)(3). Significantly, however, 9-322(g) provides that if a statute under which an agricultural lien in collateral is created provides that the agricultural lien has priority over a conflicting security interest or agricultural lien in the same collateral, the statute governs priority if the agricultural lien is perfected. Thus, individual states may opt out of the first to file or perfect priority rule of Article 9 with respect to agricultural liens. Some state agricultural lien statutes take advantage of this provision by establishing specific priority rules for agricultural liens which may be different than the general “first to file or perfect” priority rule of Article 9. See, e.g., Minn. Stat. §§ 514.964, 514.966.
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Table of Contents

I. UCC Revised Article 9 / Agricultural Liens .............................. 2
   A. Agricultural Liens
   B. Buyer of Farm Products (Federal Food Security Act)

II. Bankruptcy .................................................................................. 11
    A. Case Administration
    B. Bankruptcy Estate
    C. Chapter 12
I. UCC REVISED ARTICLE 9 / AGRICULTURAL LIENS

A. Agricultural Liens

1. Feed supplier is required to file a UCC-1 every 31 days to maintain super-priority Iowa agricultural supply dealer lien; for livestock born at the producer’s facilities, the “acquisition price” for purposes of calculating the lien amount was zero. Crooked Creek Corporation (the “Debtor”) operated a farrow-to-finish hog farm. The Debtor was indebted to Primebank (the “Secured Creditor”) and the debt was secured by a security interest in the hogs of the Debtor. The Debtor contracted with Oyens Feed Supply, Inc. (the “Feed Supplier”) to supply feed. The Debtor was indebted to the Feed Supplier and the Feed Supplier filed an agricultural supply dealer lien under Iowa Code 570A. The Debtor filed a Chapter 12 bankruptcy. The Secured Creditor and Feed Supplier asserted priority liens in the escrowed proceeds from the sale of the hogs. In an earlier certified request to the Iowa Supreme Court, the Iowa Supreme Court held that the Feed Supplier was not required to give any notification to the Secured Creditor to have an enforceable super-priority agricultural supply dealer lien under Iowa Code 570A. Oyens Feed Supply, Inc. v. Primebank, 808 N.W.2d 186 (Iowa 2011). There remained unresolved legal issues as to whether: (a) the agricultural supply dealer was required to file a new UCC-1 financing statement every thirty-one (31) days in order to maintain perfection of its agricultural supply dealer's lien as to feed supplied within the preceding thirty-one (31) day period; and (b) the “acquisition price” for purposes of calculating the lien amount was zero for livestock born in the producer's facility. Another certified request was made to the Iowa Supreme Court and the Iowa Supreme Court held that: (a) an agricultural supply dealer is required to file a new financing statement every 31 days in order to maintain perfection of its lien, and (b) the “acquisition price” for purposes of calculating the lien amount was zero for livestock was born in the producer's facility. The producer’s overhead costs and costs of production should not be considered because the status provides for “acquisition price” not “acquisition costs”. The Feed Supplier is entitled to a super-priority lien for the full extent of the value of feed consumed by the hogs without any reduction for any “acquisition price” of the producer. Oyens Feed & Supply, Inc. v. Primebank, 879 N.W.2d 853 (Iowa 2016).

Comment. This case should be read in conjunction with Farmers Coop, Co. v. Ernst & Young Inc. (In re Big Sky Farms Inc.), 512 B.R. 212 (Bankr. N.D. Iowa 2014) and In re Shulista, 808 N.W.2d 186 (Iowa 2011) and 451 B.R. 867 (Bankr. N.D. Iowa 2011).

2. Iowa agricultural supply dealers’ lien notice must be issued every 31 days to have an uninterrupted lien. Farmer Cooperative Company (the “Feed Supplier”) supplied feed to Big Sky Farms, Inc. (the “Debtor”) on an open account. The Debtor became insolvent and filed bankruptcy in Canada. Under
operation of Chapter 15 of the U.S. Bankruptcy Code, the issues of priority were deferred to the Iowa Court. The Feed Supplier asserted a statutory Iowa agricultural supply dealers’ lien on the livestock under IA Stat. § 570A.5. The Canadian bankruptcy receiver, Ernst & Young, Inc. (the “Receiver”), did not dispute the lien but asserted that the Feed Supplier was only entitled to a lien for the feed supplied within 31 days prior to filing the lien notification. The Court agreed. Both the Receiver and the Feed Supplier moved to amend this ruling and the Court analyzed each motion. First, the Court determined that its ruling on the 31-day rule should stand, which means suppliers only have perfected agricultural liens for purchases made 31 days prior to each of its filed financing statements. Next, the Court amended its ruling on the amount of the Feed Supplier’s perfected agricultural lien to find a genuine issue of material fact existed as to the unpaid amount of the Feed Supplier’s claim as well as the secured status of its claim. As a result, these issues were left for determination at trial. Farmers Coop. Co. v. Ernst & Young Inc. (In re Big Sky Farms Inc.), 512 B.R. 212 (Bankr. N.D. Iowa 2014).

Comment. The Farmers Coop. Co. decision should be read in conjunction with the Oyens Feed & Supply Inc., 808 N.W.2d 186 (Iowa 2011) and In re Shulista, 808 N.W.2d 186 (Iowa 2011) and 451 B.R. 867 (Bankr. N.D. Iowa 2011).

3. Revised Article 9 entitles the agister to a priority lien under the Idaho agister lien statute. Green River Dairy, LLC (the “Debtor”) owned and operated a dairy farm and was indebted to Farmers National Bank (the “Secured Creditor”). The debt was secured by a security interest in certain personal property including the dairy cows of the Debtor. The Secured Creditor filed a UCC-1 finance statement. The Debtor and J & M Cattle Co., LLC (the “Agister”) contracted for the Agister to provide food, care and other services to the Debtor’s dairy cattle. The Debtor failed to pay the Agister and the Agister asserted a possessory Idaho agister lien under Idaho Code 45-805. The Agister commenced a legal action. The Secured Creditor argued that because the Idaho statute did not expressly address priority of the lien, but the statute did expressly state that the secured creditor should be paid before the lien creditor, that the Agister was limited to a junior lien. The Court disagreed. UCC § 9-333(b) provides a possessory lien has priority over a security interest unless the lien statute expressly provides otherwise. Because the Idaho lien statute was silent as to lien priority, the general rule under UCC § 9-333(b) controlled and the Agister was entitled to a priority lien. J & M Cattle Co. v. Farmers National Bank, 330 P.3d 1048 (Idaho 2014).

4. Iowa agricultural supply dealers’ lien extends to the proceeds of the livestock. The debtor Donald Molstad (“Debtor”) was indebted to Cooperative Credit Company (“Secured Creditor”) and the indebtedness was secured by a security interest in the farm products and livestock of the Debtor. Watonwan Farm Service (“Feed Supplier”) supplied feed to the Debtor on an open account.
The Debtor filed a Chapter 12 bankruptcy and the Secured Creditor and the Feed Supplier asserted liens in the livestock and the proceeds from the livestock. The Feed Supplier asserts a statutory Iowa agricultural supply dealers’ lien under IA Stat. §570A.5. The Secured Creditor did not challenge the lien on the livestock, but the Secured Creditor challenged whether the lien attached to the proceeds of the livestock on the basis that statutory liens must specifically state that the lien attaches to the proceeds of the livestock. The Secured Creditor argued that attachment provision of UCC §9-315 does not extend to statutory liens and, therefore, the lien statute must affirmatively state the lien attaches to the proceeds. The Court disagreed and held the agricultural lien extended to any resulting sales proceeds on equitable grounds. The Court stated, “[g]iving an agricultural supply dealer a lien that can only be enforced against the collateral (in this case, the pigs) but not the proceeds of that collateral could lead in many circumstances—like this one—to provide little protection for the agricultural supplier.” Schley v. Peoples Bank (In re Schley), No. 10-03252, Adversary No. 10-09255, 2014 Bankr. LEXIS 1724 (Bankr. N.D. Iowa Apr. 18, 2014).

Comment. The Court elected to expand the scope of the Iowa agricultural supply dealers’ lien on equitable grounds. Revised Article 9 and the attachment language of the Iowa agricultural supply dealers’ lien do not expand the scope of the lien to attach to the proceeds. See Stockman Bank of Montana v. Mon-Kota, Inc., 3432 Mont. 115 (Mont. 2008) (Montana lien does not attach to the proceeds because the statute must specifically provide the lien attaches to the proceeds).

5. Livestock not “agricultural products” under Idaho agricultural lien statute. The debtor Green River Dairy, LLC (“Debtor”) was indebted to Farmers National Bank (“Secured Creditor”) and the indebtedness was secured by a security interest in the dairy cows of the Debtor. The Debtor purchased feed on credit from various feed suppliers (“Feed Suppliers”). The Debtor went insolvent and the Feed Suppliers asserted priority statutory liens against the dairy cows under Idaho Stat. §45-1802 on the basis that the statutory lien in the feed consumed by the livestock extended to the livestock. The Secured Creditor argued that the dairy cows that consumed the feed were not “agricultural products” under Idaho law and, therefore, the Feed Supplier did not have a valid lien in the livestock. The Court agreed holding that “[l]ivestock, including dairy cows, are not an agricultural product that may be the subject of an agricultural lien” and the consumption of feed that is the subject to a statutory lien does not extend to the livestock that consume the feed. Farmers Nat’l Bank v. Green River Dairy, LLC, 318 P.3d 622 (Idaho 2014).

6. Supplier of feed and other related services is limited to a livestock production lien under Minnesota law, and is also not entitled to the higher priority feeder’s lien. The feed supplier Wilmont-Adrian Cooperative supplied feed and provided nutritional analysis and custom nutrition plans to the hog producer Profit Pork. New Vision Coop only supplied feed to the hog producer.
The hog producer went insolvent and the feed suppliers asserted various statutory liens against certain proceeds from the sale of hogs. Wilmont-Adrian Cooperative argued that it was entitled to a higher priority feeder’s lien under Minnesota law because the Minnesota feeder’s lien included any one that “stores, cares for, or contributed to the keeping, feeding… or other care of livestock.” The Court held implied that a lien claimant may only be entitled to one lien category and to be eligible for the feeder’s lien the supplier must directly care for or contribute to the feeding of the livestock. Because the livestock input lien was more applicable to the goods and services provided by Wilmont-Adrian Cooperative, the Court held that it was not also entitled to the high priority feeder’s lien. *First Nat’l Bank v. Profit Pork, LLC*, 820 N.W.2d 592, 2012 Minn. App. LEXIS 96 (Minn. Ct. App. 2012).

7. **Failure to properly identify the hogs in the UCC-1 filing under the Iowa agricultural supply dealer’s lien causes the lien to be unperfected.** The supply dealer filed a UCC-1 that stated “All livestock located at [certain barn location].” The Bankruptcy Court ruled that for any hogs not located at the barn locations listed in the UCC-1, the lien was unperfected. *First Nat’l Bank v. Farmers Coop Soc’y (In re Coastal Plains Pork, LLC)* 2012 WL 6571102 (E.D. N.C. Bankr. 2012)

*Comment Note.* The Court implied that had the UCC-1 just stated “[A]ll livestock” the UCC-1 would have properly identified all of the hogs. The assumption is that that the Court deferred to the general principles under Revised Article 9 (UCC § 9-504 and § 9-108(2)(a)-(f)) that a UCC-1 that describes a general category of collateral is sufficient to prefect a security interest. The take away is that the UCC-1 filer should either not attempt to identify the specific barn locations or, the UCC-1 should state “all livestock, including but not limited to, the livestock located at the following barn locations: [and then list the barn locations]”.

8. **Factual issues in the calculation of a priority lien under the Iowa agricultural supply dealer’s lien preclude granting summary judgment.** The Iowa agricultural supply dealer’s lien (Iowa Code § 570A.5(3)), provides that if properly perfected, the supply dealer is entitled to a priority lien for the difference between the acquisition price of the livestock and the fair market value of the livestock at the time the lien attaches or the sale of the livestock, whichever is greater. The Bankruptcy Court ruled that there remains factual issues as to: (1) the acquisition price of the hogs and whether feed, transportation, shelter and supervision expenses should be considered in the acquisition cost; (2) the value of the hogs considering some hogs did not consume any of the unpaid feed; and (3) whether the lien includes non-feed charges for interest and financing. *First Nat’l Bank v. Farmers Coop Soc’y (In re Coastal Plains Pork, LLC)* 2012 WL 6571102 (E.D. N.C. Bankr. 2012).
B. Buyer of Farm Products (Federal Food Security Act).

1. Secured creditor not limited by a grain buyer’s contractual right of setoff. David Walker (the “Debtor”) was a grain farmer and was indebted to Guaranty Bank & Trust Co. (the “Secured Creditor”). The debt was secured by a security interest in the crops and contract rights of the Debtor. The Secured Creditor filed a UCC-1 finance statement with the State of Mississippi. The Debtor had assumed several contracts to deliver grain to Agrex, Inc. (the “Buyer”) which contained the contractual right of the Buyer to offset future deliveries against any unpaid debts. The Debtor failed to deliver on a few contracts and was indebted to the Buyer. The Debtor subsequently sold $417,033 in grain to the Buyer and the Buyer contractually offset the $417,033 in grain sales against the $359,853 in earlier debts owed to the Buyer. The Secured Creditor commenced a legal action against the Buyer and the Buyer argued that it was entitled to the $359,853 because the rights of the Secured Creditor are limited to the rights of the Debtor in the grain contracts. Because the rights of the Debtor are contractually limited by the right of offset in the grain contracts, the rights of the Secured Creditor were also contractually limited by the right of offset in the grain contracts. The District Court disagreed and the Buyer appealed. The 5th Circuit held that the Secured Creditor is not limited to its security interest in the contract rights of the Debtor. Although the Secured Creditor had a security interest in the contract rights of the Debtor, the Secured Creditor also had a security interest in the crops of the Debtor and, therefore as the 8th Circuit held in Farm Credit Services of America, PCA v. Cargill, Inc., 750 F.3d 965 (8th Cir. 2014), the security interest takes priority over the contract rights of the Buyer. The court distinguished Consolidated Nutrition, L.C. v. IBP, Inc., 669 N.W.2d 126 (S.D. 2003) on the basis that in the South Dakota case the secured creditor failed to file an effective financing statement with the State of Dakota and, therefore, the buyer purchased the crop free and clear of any liens of the secured creditor under the Food Security Act. As a result of the extinguished security interest, the buyer in Consolidated Nutrition, L.C. was entitled to offset against unpaid debts owed to the buyer over the objection of the secured creditor. Guar. Bank & Trust Co. v. Agrex, Inc., 820 F.3d 790 (5th Cir. 2016).

2. Buyer of farm products not entitled to assert statutory right of offset under UCC §9-404. The debtors Bryan and Susan Stec and Stec Brothers, LLC ("Debtors") were indebted to Farm Credit Services ("Secured Creditor") and the debt was secured by a security interest in the crops of the Debtors. The Secured Creditor filed a CNS statement as to the crops. The Debtors sold corn to Cargill ("Buyer"). The Secured Creditor filed a lawsuit against Cargill seeking recovery of the Debtors’ delivered corn crops. The Secured Creditor argued that the Buyer purchased the farm product subject to the Debtors prior security interest and unless the Buyer obtains a waiver or makes the check jointly payable to the Secured Creditor under 7 U.S.C. § 1631(e), the Buyer buys subject to their Article 9 security interest. The Buyer did not make the check jointly payable to the
Secured Creditor. The Buyer argued that it had a right of offset under UCC §9-404 because the Debtor assigned its right of payment to the Secured Creditor and the statutory right of offset under Revised Article 9 pre-empted 7 U.S.C. § 1631(e). The Eighth Circuit disagreed and held that the sale of the farm product “does not switch [the Secured Creditor’s] lawsuit from one seeking corn to one seeking a right to payment on an account” and, therefore, the Court did not need to address whether UCC §9-404 pre-empts 7 U.S.C. § 1631(e). 


3. The Federal Food Security Act pre-empts Revised Article 9. The Illinois Court of Appeals affirmed a trial court decision that the Food Security Act preempts Revised Article 9. The Court adopted the reasoning in Farm Credit Midsouth, PCA v. Farm Fresh Catfish Co., 371 F.3d 450 (8th Cir. 2004), relying on the Supremacy Clause of the Constitution, the language of UCC § 9-109 (“This Article does not apply to the extent that: a statute . . . of the United States preempts this Article.”) and the language of the Food Security Act § 1631(d) (“notwithstanding any other provision of Federal, State, or local law[.]”) in support of its decision. State Bank of Cherry v. CGB Enterprises, Inc., 964 N.E.2d 604 (Ill. Ct. App. 2012); (affirmed by State Bank of Cherry v. CGB Enters., 984 N.E.2d (Ill. 2013)).

4. The State that the farm products were “produced in” controls where notice should be directed. When determining whether a buyer purchases farm products subject to the seller’s security interest and where the notice should be directed, the term “produced in” means “the location where farm products are furnished or made available for commerce.” The primary question on appeal was whether 206 head of cattle bought by the Colorado buyer were “produced in” Oklahoma (the state the buyer believed the cattle were located and where the seller resided) or in Missouri (the state that the cattle were actually located and for which the seller acquired the cattle from the cattle broker). Oklahoma has a central filing system. The FSA does not define “produced in,” nor does any case law, so the court implemented standard statutory interpretation canons. The Court rejected buyer’s argument that “produced in” should mean the geographic origin of the farm products—not the location from which the farm products were sold. The Court concluded that “purchased in” means “the location where farm products are furnished or made available for commerce.” The Court emphasized that this interpretation “allows lenders to discern where they must file notice . . . and ensures a practical means for buyers to discover otherwise unknown security interests in farm products.” Here, the seller delivered the cattle to the buyer in Oklahoma and the buyer had the cattle shipped to Colorado. Therefore, because the seller made the cattle available in Oklahoma, for the purposes of the FSA, the cattle were produced in Oklahoma. Because Oklahoma is a central filing state, the seller’s lender was required to register with the State of Oklahoma and the buyer was required to review the filing and make the payment jointly payable to

5. **The county were the crops are processed is not relevant for purposes of the Food Security Act.** The Secured Creditor filed two CNS farm product financing statements with Mississippi Secretary of State. Each CNS listed sweet potatoes as the farm product, included the county codes for two counties and listed the six parcels within those two counties. The debtor planted crops on the six parcels, but also in an unlisted county. However, the sweet potatoes grown in the unlisted county were processed in one of the listed counties. A produce company bought the sweet potatoes and did not make the check payable to the producer and the secured creditor. The Secured creditor argued that the CNS is not limited to the location the crop is grown but, instead, includes the location the crop is processed. The Court disagreed and held that the county were the crops are processed is not relevant because the CNS must identify the county were the crops are grown. *In re Moore,* 2013 Bankr. LEXIS 2060 (Bankr. N.D. Miss. May 17, 2013).

6. **Direct Notice States**

   a. **Failure to identify county where crops were grown invalidates notice.** The secured creditor failed to include the names of certain counties where the debtor grew crops. The secured creditor argued that it was not required to strict comply with the notice requirements and, that by identifying the other counties were crop were grown, the secured creditor was in substantial compliance. The Court disagreed and held that the Federal Food Security Act expressly requires the secured party to provide a description of the farm products subject to the security interest created by the debtor and the name of each county where the farm products are located. The Court recognized some conflicting and non-binding state case law as to “substantial compliance” with the notification statute. Accordingly, the buyer purchased debtor’s crop free of the secured creditor’s security interest despite knowing of the secured creditor’s security interest.¹ *State Bank of Cherry v. CGB Enterprises, Inc.*, 964

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¹ As noted in the case summary, there is conflicting case law as to whether the direct notice provisions of the FSA require strict or substantial compliance. The Illinois Court of Appeals in this case relied on the 8th Circuit decision in *Farm Credit Midsouth* for holding that the secured creditor must strictly comply with the statute. Alternatively, *First Nat’l Bank & Trust v. Miami County Cooperative Ass’n*, 897 P.2d 144 (Kan. 1995); *Farm Credit Services of MidAmerica, ACA v. Rudy, Inc.*, 680 NE2d 637 (Ohio Ct. App. 1996); and *Lisco State Bank v. McCombs Ranches, Inc.*, 752 F. Supp. 329, 13 UCC Rep. 2d 928 (D. Neb. 1990) have all held that the standard is substantial compliance. As for the 5th Circuit, even the majority and dissent in *State Bank of Cherry* disagreed whether the holding in *Peoples Bank v. Bryan Brothers Cattle Co.*, 504 F.3d 549, 64 UCC Rep. 2d 113 (5th Cir. 2007), required strict or substantial compliance.
b. Failure to identify debtor’s social security number and proper description of crops invalidates notice. The secured creditor failed to include the social security number of the debtor on the CNS statement and failed to properly identify the county where the crops were being grown. The secured creditor argued that it was not required to strictly comply with the notice requirements. The Court disagreed and held that the failure of the secured creditor to include the debtor’s social security number and a proper description of the crops in the Food Security Act notice invalidates the notice and allowed a grain elevator to purchase the crops free and clear of any claims of the secured creditor. *CNH Capital v. Trainor Grain and Supply Co. (In re Printz)*, 2012 LEXIS 4506 (Bankr. C.D. Ill. Sept. 27, 2012).

7. Central Filing States.

Priority limited to locations specified in the CNS statement. The secured creditor filed two CNS farm product financing statements with Mississippi Secretary of State. Each CNS listed sweet potatoes as the farm product, included the county codes for two counties and listed the six parcels within those two counties. The debtor planted crops on the six parcels, but also in an unlisted county. A produce company bought the sweet potatoes and did not make the check payable to the producer and the secured creditor. The Court found that for the two counties that the secured creditor properly listed, the produce company failed to comply with the Food Security Act and the secured creditor took priority. However, for the third unlisted county, the Court held that the produce company took priority because the secured creditor limited its CNS to the listed six parcels. *In re Moore*, 2013 Bankr. LEXIS 2060 (Bankr. N.D. Miss. May 17, 2013).

*Comment Note.* The creditor should not limit the scope of its CNS statement but, instead the creditor should identify all crops and all counties in the state in the CNS to avoid this outcome.

8. Set-off by Buyer.

*Buyer is not entitled to set-off.* A buyer of farm products is not entitled to set-off the obligation owed to the seller for the sale of grain against the prior indebtedness owed by the seller to the buyer. The Food Security Act allows a buyer of farm products to purchase the farm products free and clear of any security interests. However, the Food Security Act does not allow a buyer of farm products to acquire the proceeds of the farms
products (through a common law set-off) free and clear of any security interest in the sale proceeds. The FSA only defines a “security interest” as “an interest in farm products that secured payment or performance of an obligation.” The term does not reference or include within its definition the proceeds of the security interest. The Court reasoned that at the moment the grain buyer set-off against the debt owed to the seller, the grain buyer was no longer a buyer in the ordinary course of business but, instead, a creditor. To allow the common law setoff would circumvent Revised Article 9. *CNH Capital v. Trainor Grain and Supply Co. (In re Printz)*, 2012 LEXIS 4506 (Bankr. C.D. Ill. Sept. 27, 2012)

II. BANKRUPTCY.

A. Case Administration.

1. Preventing a dairy herd from going “dry” provided a quantifiable benefit to secured creditors and justified a surcharge to the lien claims of the secured creditors. The debtors Tollenaar Holsteins, Friendly Pastures and T Bar M Ranch (the “Debtors”) are related dairy producers who filed Chapter 11 bankruptcy petitions. The cases were administratively consolidated. The Debtors were indebted to Bank of the West and Hartford Accidental and Life Insurance Company (the “Secured Creditors”) and the debts were secured by the assets of the Debtors. The trustee requested a surcharge of the collateral of the Secured Creditors to pay the reasonable and necessary expenses incurred in preserving the estate under 11 U.S.C. § 506(c), specifically, for expenses incurred in keeping the debtors’ dairy herd “wet” before the herd was sold. The Secured Creditors objected on the basis that the surcharge would not provide a quantifiable benefit to the Secured Creditors, the applicable test under 11 U.S.C. § 506(c). The Court disagreed and held that the payment of these expenses would prevent the loss of valuable permits if the dairy cows went dry. *In re Tollenaar Holsteins*, 538 B.R. 830 (Bankr. E.D. Cal. 2015).

2. Automatic stay extends to post-confirmation property vested with a debtor under his Chapter 12 plan. The debtor filed and confirmed a Chapter 12 plan that vested the property of the bankruptcy estate with the debtor at plan confirmation. The Chapter 12 plan provided that the debtor would receive his discharge upon completion of the payments under the plan. Post-confirmation, but before discharge, a creditor commenced a legal action against the debtor without obtaining stay relief. The creditor argued that the property was no longer property of the estate and, therefore, no stay was in effect. The Court disagreed and held that even though the property vested with the debtor in his Chapter 12 plan, under Code § 362(c)(5), the creditor was still stayed from taking legal action against property of the debtor. *In re Blankenship*, 2013 Bankr. LEXIS 1767 (Bankr. S.D. Ohio April 29, 2013).
B. Creditors, Debtors and the Bankruptcy Estate.

1. Property of the Bankruptcy Estate.

Appreciated proceeds from the post-confirmation sale of land are not property of the bankruptcy estate subject to distribution to creditors. David and Patricia Smith (the “Debtors”) were crop farmers and confirmed a Chapter 12 plan. Post-confirmation the Debtors sold some crop land for $295,576 and sought to capture the difference between the sale price and the $100,000 value in the confirmed plan. Creditors and the Chapter 12 trustee objected on the basis that the proceeds from the post-confirmation sale should be characterized as “disposable income” and distributed to the creditors. The Court disagreed and held: (a) the property vested with the Debtors at plan confirmation and, therefore, the appreciated value is not property of the bankruptcy estate; and (b) appreciated assets are not disposable income. Appreciated proceeds cannot be considered regular income as it only occurs following the one-time sale of property and, therefore, falls outside of the disposable income definition which generally requires a steady stream of payments. In re Smith, 514 B.R. 464 (Bankr. N.D. Tex. 2014).

2. Administrative Claims.

Secured Creditor entitled to recover advances made to pay insurance as an administrative claim. Byron Jarriel (the “Debtor”) was indebted to Tippins Bank & Trust (the “Secured Creditor”). The debt was secured by a security interest in various collateral including two pieces of equipment. In order to protect its interest, the Secured Creditor required the Debtor to obtain insurance on the collateral. The Debtor filed a Chapter 12 bankruptcy. The Debtor failed to maintain insurance. The Secured Creditor made a post-petition protective advance to pay the insurance. The Debtor elected to sell the collateral post-petition and pay off the Secured Creditor in full. The Secured Creditor failed to include the costs it incurred for the insurance in its payoff and, subsequently argued that the Secured Creditor was entitled to reimbursement for these “administrative expenses.” The Debtor argued that the Secured Creditor failed to prove that the insurance was a reasonable and necessary expense of the bankruptcy estate. The Court disagreed and held that Code Section 503 governs administrative expenses and gives such post-petition expenses priority over pre-petition claims. The Court applied a two-prong test and determined the Secured Creditor’s claim qualified under § 503 as it (1) arose from a post-petition transaction between the Secured Creditor and the Debtor, and (2) was an actual and necessary expense to preserve the bankruptcy estate. Because the Secured Creditor acted in good faith and in the best interests of the estate, the Secured Creditor was entitled to an administrative claim for its post-petition advances to pay the insurance.

3. **Non-dischargeability actions.**

a. **Sale of collateral without consent of secured creditor does not constitute larceny or embezzlement; may constitute willful and malicious injury.** David and Kristen Pitz (the “Debtors”) owned and operated a crop farm. The Debtors were indebted to Peoples Savings Bank (the “Secured Creditor”). The debt was secured by a security interest in the crops of the Debtors. The Debtors sold the crops and did not apply the crop proceeds against the loan. The Debtors filed bankruptcy. The Secured Creditor filed an adversary action asserting that the sale of crops constituted larceny, embezzlement, or a willful and malicious injury and, therefore, the debt should be non-dischargeable under 11 U.S.C. § 523(a)(4) and (6). The court dismissed the larceny and embezzlement claims under § 523(a)(4) because a security interest is not the property of another. The court held there was sufficient legal basis to proceed to trial on the willful and malicious injury claim under § 523(a)(6) because there was a factual issue as to whether the Debtors intended to defraud the Secured Creditor. In re Pitz, 2016 WL 1530003 (Bankr. N.D. Iowa 2016).

b. **Sale of collateral without consent of secured creditor constitutes willful and malicious injury and is non-dischargeable.** Mark and Tammy Shelmidine (the “Debtors”) were married and owned and operated a dairy farm. The Debtors took out three loans from the Farm Service Agency (the “Secured Creditor”) which were each secured by farm equipment, machinery, crops, and cattle (the “Collateral”). The Secured Creditor perfected its security interests and each of the security agreements required the Debtors to receive FSA approval before selling or otherwise altering the Collateral. The Debtor sold cattle without the Secured Creditor’s authorization. The Debtors used the proceeds from these sales to pay off other creditors but never offered any of the proceeds to the Secured Creditor. The Debtor filed a Chapter 7 bankruptcy. The Secured Creditor filed an adversary action under 11 U.S.C.A. § 523(a)(6) asserting willful and malicious injury. The Secured Creditor argued that the Debtors’ use of the cash proceeds from the unauthorized sale was willful and malicious under § 523(a)(6). The Debtors maintained that the close, “supervised credit” relationship between the Debtors and the Secured Creditor meant the sales were impliedly authorized by the Secured Creditor. The Court disagreed and found in favor of the Secured Creditor following a two-part analysis under § 523(a)(6) that required (1) willful injury and (2) malice. First, the court found the Debtors subjectively intended to injure the Secured Creditor when it sold the cattle...
and failed to apply the proceeds to any of the debt held by the FSA. Second, the Court found the Debtors used the proceeds from the collateral sales to elevate certain creditors over the Secured Creditor, which implied malice. The Court ruled that the debt held by the Secured Creditor was non-dischargeable. United States v. Shelmidine (In re Shelmidine), 519 B.R. 385 (Bankr. N.D.N.Y. 2014).

C. Chapter 12.

1. Eligibility.


   i. Contracting with a third party for the planting and harvesting of a crop constitutes farming. Larry and Sandra Williams (the “Debtors”) rented farmland and contracted with their son to plant and harvest the crop on the rented farmland. The Debtors filed a Chapter 12 bankruptcy. The Chapter 12 Trustee moved to dismiss the bankruptcy arguing that the Debtors were not eligible to be debtors under Chapter 12 because they were not “engaged in a farming operation” for purposes of 11 U.S.C. § 101(18). The court disagreed and held that a Chapter 12 debtor does not have to own the land upon which the farming occurred nor does the debtor have to do all of the physical labor involved with farming. The Debtors entered into the lease contract with their son for their own benefit, owned the farm equipment, purchased the seed, fertilizer, and materials used in the operation, entered into insurance contracts in their own names, and made all of the decisions as to what crops would be planted and incurred all profits and losses. The court held that the Debtors were sufficiently involved with the farming operation to be engaged in a farming operation for purposes of Chapter 12 eligibility. In re Williams, 2016 WL 1644189 (Bankr. W.D. Ky. 2016).

   ii. Game farm constitutes a farming operation for purposes of Chapter 12 eligibility. Marone Acee (the “Individual Debtor”) operated a bird game farm on the property of a related entity Boulder Meadows (the “Corporate Debtor”). The Individual Debtor and the Corporate Debtor filed for Chapter 12 bankruptcy. Two creditors objected to the Chapter 12 plan on the basis that the Individual Debtor was not eligible for Chapter 12 bankruptcy because a bird game farm is not a “farming operation” for purposes of 11 U.S.C.A. § 109(e) and § 101(21). The Bankruptcy Court disagreed and held, that under the totality of the circumstances test, the Individual Debtor was engaged in a farming operation because
the Individual Debtor fed, maintained, protected and released the game birds and experienced the traditional risks associated with farming such to risk of disease and death. The Court held the Corporate Debtor was not eligible for Chapter 12 because the Corporate Debtor did not have this same involvement in the game farm.  United States Dist. Court N. Dist. of N.Y. Marone Acee v. Oneida Sav. Bank, 529 B.R. 494 (N.D.N.Y. 2015).

iii. **Cattle raised under a production contract constitutes a “farming operation” for the purposes of eligibility.** The debtors Randy and Geneva Perkins (“Debtors”) received social security benefits, raised 262 head of cattle under a production contract and raised and sold 37 head of cattle in their names. The Debtors filed a Chapter 12 bankruptcy. A creditor objected to the Chapter 12 plan on the basis that raising cattle under a production contract is not a “farming operation” for purposes of 11 U.S.C. §101(21). The Court disagreed and held that, under totality of the circumstances test, the Debtors were engaged in a farming operation because the Debtors performed the physical labor associated with raising cattle. In re Perkins, 2013 Bankr. LEXIS 4539 (Bankr. E.D. Tenn. Oct. 30, 2013).

Comment. In re Perkins evidences the trend of looking beyond just the traditional risks associated with farming to include individuals who raise livestock under production contracts.

b. **50% Farming Income Requirement.**

i. CRP payments and strawberry and game farm proceeds are farm income for the purposes of eligibility. The debtor Marone Acee (“Debtor”) owned and operated a bird game farm. The Debtor filed a Chapter 12 bankruptcy. Two creditors objected to the Chapter 12 plan on the basis that the Debtor was not eligible for Chapter 12 bankruptcy because the Debtor failed to have sufficient farm income for purposes of 11 U.S.C. §101(18). The Court disagreed and held that because over 50% of the Debtor’s gross income was as a result of CRP payments, a strawberry crop and product proceeds, and pheasant-related income the Debtor did qualify. See In re Acee, 2013 Bankr. LEXIS 4789 (Bankr. N.D.N.Y. Nov. 12, 2013).

ii. A settlement payment from a lawsuit that arose from farming activities can qualify as farming income. The debtor David McLawchlin (“Debtor”) was previously a rice farmer but, because of a permanent disability, had limited mobility. The only
source of farm income was $30,000 from the settlement of a lawsuit for crop losses in 2006, 2007 and 2008. The Debtor filed a Chapter 12 bankruptcy. A creditor objected to the Chapter 12 plan on the basis that the Debtor was not eligible for Chapter 12 bankruptcy because the Debtor failed to have sufficient farm income for purposes of 11 U.S.C. §101(18). The Court disagreed and held that the settlement proceeds arose out of a farming operation and were sufficient to meet the farm income requirements, even though the conduct that gave rise to the settlement occurred many years before. In re McLawchlin, 511 B.R. 422 (Bankr. S.D. Tex. Jun. 5, 2014).

c. 50% Farming Debt Requirement.

i. When the debtor secured by the principal residence does not arise from the farming operation, the amount of principal residence debt is excluded entirely from the Chapter 12 eligibility calculation. Marone Acee (the “Individual Debtor”) operated a bird game farm on the property of a related entity Boulder Meadows (the “Corporate Debtor”). The Individual Debtor and the Corporate Debtor filed for Chapter 12 bankruptcy. Two creditors objected to the Chapter 12 plan on the basis that the Individual Debtor was not eligible for Chapter 12 bankruptcy because less than 50% of the debtor’s aggregate, noncontingent, liquidated debts arose out of the farming operation, as required by 11 U.S.C.A. § 109(e) and § 101(18). The Bankruptcy Court agreed and held that the Individual Debtor failed to prove his personal residence should be included in the calculation (i.e. prove it arose out of the farming operation) and, as a result, he did not reach the 50% threshold. The Individual Debtor appealed. The District Court overruled and held, in reliance on In re Woods, 743 F.3d 689 (10th Cir. 2014), that because the principal residence debt was not farm related, it should be completely excluded from the debt calculation. United States Dist. Court N. Dist. of N.Y. Marone Acee v. Oneida Sav. Bank, 529 B.R. 494 (N.D.N.Y. 2015).

ii. For Chapter 12 eligibility purposes, all claims enforceable against either the debtor or its property are allowed. Carolyn Davis (the “Debtor”) owned a ranch and other properties in California. The Debtor filed for Chapter 7 in July 2010 and received a discharge that released her from personal liability for the unsecured claims associated with her properties. Then, in March 2011, the Debtor filed a Chapter 12 bankruptcy. At the time of her filing, her properties were valued at $1.6 million. The liens on those properties totaled $4.1 million, $2.5 million of
which was unsecured. The Bankruptcy Court dismissed her petition on the basis that the $4.1 million was over the $3,792,650 aggregate debt limit on eligibility for filing Chapter 12. The Debtor appealed, arguing that the unsecured portions of her secured creditor’s claims should not be included in her aggregate debt total for Chapter 12 eligibility purposes. The Bankruptcy Appellate Panel disagreed and affirmed the bankruptcy court’s decision dismissing the Chapter 12. It stated that the aggregate debt calculation, as required by 11 U.S.C.A. § 109(e) and § 101(18), includes all obligations enforceable against the Debtor’s property, even if such obligations were not enforceable against the Debtor personally or if there was sufficient value in the property. The Ninth Circuit affirmed this decision and explained that a creditor’s claim is still a “debt” if it is enforceable against either the debtor or the debtor’s property. Therefore, regardless of the Debtor’s Chapter 7 discharge, the “aggregate debt” still includes the full amount of all creditors’ claims against the property of the debtor for purposes of calculating Chapter 12 eligibility. In re Davis, 778 F.3d 809 (9th Cir. 2015).

iii. “Direct use” test is appropriate test for determination of farming debt in the 10th Circuit. The debtors Reson and Shuan Woods (“Debtors”) owned and operated a hay farming operation. The Debtors filed a Chapter 12 bankruptcy. A creditor objected to the Chapter 12 plan on the basis that the Debtor was not eligible for Chapter 12 bankruptcy because the Debtor failed to have sufficient farm debt for purposes of 11 U.S.C. §101(18). The Court agreed and held that a home construction loan that was used to pay off a loan for the purchase of their farmland was not excluded from the debt total because it arose from the farm operations. The bankruptcy court had applied the “some connection” test to the Debtors’ farming activities, and concluded that the presence of the farming operation’s office and records in the residence, and its proximity to the farm resulted in the construction loan being connected to the farming activities. The creditor appealed and the 10th Circuit held the bankruptcy court applied the wrong test, and remanded for a determination under the “direct use” test whether the Debtors’ loan “arises out of” their farming operation. The court explained that the “direct use” test is most proper because it is singularly focused on whether the loan proceeds were directly applied to or used in a farming operation, and best embodies the “direct-and-substantial” standard for connection between the loan and the farming operations. First Nat’l Bank v. Wood (In re Woods), 743 F.3d 689 (10th. Cir. 2014).
iv. Presumption that the home mortgage note secures non-farm debt. The debtor Acee (“Debtor”) owned and operated a bird game farm. The Debtor filed a Chapter 12 bankruptcy. Two creditors objected to the Chapter 12 plan on the basis that the Debtor was not eligible for Chapter 12 bankruptcy because the Debtor failed to have sufficient farm debt for purposes of 11 U.S.C. §101(18). The Court agreed and held that because the home mortgage debt did not secure farm debt the home mortgage debt was not farming debt for purposes of Chapter 12 eligibility See In re Acee, 2013 Bankr. LEXIS 4789 (Bankr. N.D.N.Y. Nov. 12, 2013). The Debtor appealed and the District Court affirmed on the basis that 11 U.S.C.A. §101(18)(A) creates a presumption that residential debt is not farm-related debt. Although the presumption can be overcome with evidence of a connection between the residential debt and the farming operation, there was no evidence present in this case. In re Acee, 2014 Bankr. LEXIS 89 (Bankr. N.D.N.Y. Jan. 10, 2014).

2. Dismissal/Conversion.

a. Stay relief motion must have been filed in first bankruptcy to disqualify debtor in second bankruptcy; stipulation granting stay relief is not sufficient to dismiss second bankruptcy. Craig and Lynda Herremans (the “Debtors”) were indebted to American Farm Mortgage Company (the “Secured Creditor”). The Debtors filed a Chapter 12 bankruptcy and confirmed a Chapter 12 plan (the “First Bankruptcy”). In conjunction with the confirmed Chapter 12 plan, the Debtors agreed that if the Debtors failed to make payment to the Secured Creditor that the Secured Creditor would be entitled to stay relief after filing an affidavit with the court. The Debtors failed to make a payment and the Secured Creditor filed the affidavit. The Debtors dismissed the First Bankruptcy and subsequently filed another bankruptcy (the “Second Bankruptcy”). The Secured Creditor moved to dismiss arguing that the combination of the right to stay relief in the First Bankruptcy and the filing of the Second Bankruptcy disqualified the Debtors from Chapter 12 under the serial filing restrictions under 11 U.S.C. §109(g)(2). The court disagreed and held that § 109(g)(2) is only effective if “a request for relief” or stay relief motion has been filed in the first bankruptcy. In this case, the Secured Creditor never filed a stay relief motion in the First Bankruptcy. Instead, the Debtors just consented to stay relief in the First Bankruptcy in the event of a payment default. The filing of the affidavit was not a “request for relief” for purposes of § 109(g)(2). In re Herremans, 532 B.R. 701 (Bankr. W.D. Mich. 2015).

b. Chapter 12 bankruptcy case dismissed after Debtor engaged in acts that negatively impacted the estate and destroyed value for his creditors. Charlie Dickenson (the “Debtor”) filed for Chapter 12 in August 2013. The
Chapter 12 Trustee filed a motion to dismiss under § 1208 and the Court granted on the basis that the Debtor (1) failed to fully disclose on his petition schedules, (2) failed to mention sales/exchanges he entered into immediately preceding (and even immediately following) his bankruptcy filing, (3) failed to identify his business partnerships, (4) made incorrect property valuations, (5) transferred encumbered assets, and (6) failed to develop a confirmable plan. *In re Dickenson*, 517 B.R. 622 (Bankr. W.D. Va. 2014).

c. **Debtor’s Chapter 12 case was dismissed because the Debtor failed to show a reasonable likelihood of success.** Keith’s Tree Farms, a general partnership (the “Debtor”) grew and sold trees. The Debtor filed for Chapter 12 bankruptcy. The Debtor proposed four Chapter 12 plans. Upon filing the fourth Chapter 12 plan, the Trustee moved to dismiss the bankruptcy under Code Section 1208(c)(5). The Court agreed and held the Debtor was unable to confirm a feasible plan based on the Debtor’s historical performance as well as the current condition of the Debtor’s business. The Court found testimony from the general partners regarding the partnership’s financials to be unreasonably optimistic and containing no reasonable data or projections to support confirmation of a Chapter 12 plan. *In re Keith’s Tree Farms*, 519 B.R. 628 (Bankr. W. Dist. Va. 2014).

d. **Filing proposed plan after 90 day deadline is not absolute right to dismiss.** The debtors Herman and Hendrina Vander Vegt (“Debtors”) were indebted to First Security Bank & Trust Company (“Secured Creditor”) and the indebtedness was secured by a security interest in its equipment and farm products. The Secured Creditor properly filed a UCC-1. The Debtor filed a Chapter 12 bankruptcy. The Debtors did not file a Chapter 12 plan within the 90 days required under 11 U.S.C. §1221. The Secured Creditor moved to dismiss. The Court held that §1221 was not an absolute deadline and the delays were caused by “the creditor’s resistances to the Debtor’s motions and the bankruptcy court’s issuance of orders”. *In re Vander Vegt*, 499 B.R. 631 (Bankr. N.D. Iowa. Oct. 16, 2013). The Secured Creditor appealed and the District Court affirmed holding that the Debtor may have additional time to file a plan if the delay was not the debtor’s fault. *First Sec. Bank & Trust Co. v. Vander Vegt*, 511 B.R. 567 (N.D. Iowa May 27, 2014).

3. **Plan.**

a. **Administration Claims.**

i. **Priority Stripping of Tax Claims.** The claims of the IRS and Iowa Department of Revenue were subject to the priority-stripping effect of Code § 1222(a)(2)(A). The debtor was a partner in a farming operation that dissolved in 2010. Although the debtor retained some farm assets, the debtor agreed to transfer substantially all of the farm assets to the other partner. The debtor filed a Chapter 12 bankruptcy and the IRS
argued that the debtor was not eligible for the benefits of Code § 1222(a)(2)(A) because the Supreme Court decision in *Hall* applied to the pre-petition transfer of farm assets by the debtor through the dissolution of the farming partnership. The Court disagreed and held that *Hall* was limited to the sale of post-petition assets and, therefore, the debtor was entitled to treat the resulting tax liability from the transfer of the partnership assets as an unsecured claim. *In re Hemann*, 2013 Bankr. LEXIS 1385 (Bankr. N.D. Iowa Apr. 3, 2013).

ii. **Debtor Can Not Use Estate Assets to Pay Post-Petition Capital Gains Taxes.** The debtor proposed to use the equity from the sale of 48 acres to pay post-petition capital gains incurred by the debtor from the earlier sale of equipment. The objecting creditors and Chapter 12 trustee argued that, under the U.S. Supreme Court decision in *Hall*, estate assets cannot be used to pay post-petition capital gains taxes. The debtor argued that *Hall* was not applicable; arguing that *Hall* only limited the debtor from categorizing capital gains as a general unsecured claim for purposes of plan confirmation. The Court disagreed and held that *Hall* was more expansive than just the treatment of capital gains taxes and prohibited the use of estate assets to pay post-petition capital gains taxes because the tax obligations were not tax obligations of the bankruptcy estate; and instead, are tax obligations of the individual. *Hall* held that post-petition taxes are outside Section 503(b) and, therefore, the taxes are not an allowed claim that may be treated within a Chapter 12 plan. *In re Ferguson*, 2013 Bankr. LEXIS 6 (Bankr. C.D. Ill. Jan. 2, 2013).

iii. **Proceeds of livestock and crops are not farm assets “used in a farming operation” and, therefore, the debtor was not eligible to treat the related tax liability as an unsecured claim.** The debtor raised crops and finished cattle. The debtor filed a Chapter 12 bankruptcy and argued that the sale of crops, cattle and the crop insurance proceeds received by the debtor were farm assets “used in the debtor’s farming operations” and, therefore, under Code § 1222(a)(2)(A) the debtor was entitled to treat the related tax liability as a general unsecured claim. The Court disagreed and held that, although the proceeds from the sale of farm products and crop insurance proceeds were farm assets, the proceeds were not “used in the debtor’s farming operation” and, therefore, the debtor was not eligible for beneficial treatment under Code § 1222(a)(2)(A). *In re Keith*, 2013 Bankr. LEXIS 2802 (Bankr. D. Kan. 2013).

iv. **The marginal method (as opposed to the proportional method) is the appropriate calculation of the Code § 1222(a)(2)(A) claims.** The debtor raised crops and finished cattle. The debtor filed a Chapter 12 bankruptcy and the IRS argued, for purposes of Code § 1222(a)(2)(A), the Court should apply the proportional method to calculate the resulting...
unsecured claim of the IRS. The Court disagreed and held that the marginal method adopted by Knudsen and Ficken (and not overturned by the Supreme Court in Hall) represent the proper calculation. In re Keith, 2013 Bankr. LEXIS 2802 (Bankr. D. Kan. 2013).

v. Treatment of Capital Gains. Income taxes recognized from the sale of a farm during Chapter 12 bankruptcy are not dischargeable and must be paid by the debtor. In a 5-4 decision authored by Justice Sotomayor (joined by C.J. Roberts, Scalia, Thomas, and Alito), the Supreme Court held that a federal income tax liability recognized from a farm sale during Chapter 12 bankruptcy proceedings is not incurred by the bankruptcy estate and therefore is not dischargeable. Under Code § 1222(a)(2)(A), certain governmental claims resulting from the disposition of farm assets are reduced to unsecured, general claims that may be discharged after incomplete satisfaction. That rule, however, only applies to claims in the debtor's plan that are “entitled to priority under section 507.” Section 507 lists ten categories of claims—two of which relate to taxes. The pertinent exception here is Code § 507(a)(2). That provision covers “administrative expenses allowed under section 502(b).” Code § 502(b) includes “any tax incurred by the estate.” Therefore, for post-petition taxes to be entitled to priority under section 507 and eligible for the section 1222(a)(2)(A) exception, the taxes must be “incurred by the estate.” Lynwood D. Hall, ET UX. v. United States, 132 S. Ct. 1882, 182 L. Ed. 2d 840 (2012).

b. Secured Claims.

i. Plan confirmation denied because treatment of secured claim was not commercially reasonable and inconsistent with customary lending practices and market rates. Richard and Mark Howe (the “Individual Debtors”) and Howe Farms, LLC (the “LLC Debtor”) filed Chapter 12 bankruptcies. NBT Bank (the “Secured Creditor”) was an secured creditor which held a first priority, perfected security interest in the Debtors’ personal property, including accounts, livestock, and farm equipment. The Debtors’ plan proposed a twelve-year amortization period at 6% interest with a balloon payment after seven years. Secured Creditor objected to this plan on the basis that the terms were not commercially reasonable and it would not receive the present value of its claims under 11 U.S.C.A. § 1225(a)(5)(B). The Court agreed and held for a loan secured only by livestock and farm equipment, the customary lending term ranged from five to seven years. Additionally, for high-risk borrowers like the Debtors here, the interest rate should range between 9% and 10%. As a result, the plan failed to meet the requirements of cram down and plan
confirmation was denied. *In re Howe Farms LLC*, 2014 Bankr. LEXIS 4385 (Bankr. N.D.N.Y. 2014).

ii. **Proposed interest of 2.5% does not adequately address the risk of loss.** The debtors Randy and Geneva Perkins (“Debtors”) were indebted to Farm Credit (“Secured Creditor”) and the indebtedness was secured by a security interest in the farm products of the Debtor. The Secured Creditor objected to the proposed Chapter 12 plan because the 2.5% fixed interest rate did not adequately address the risk of loss of the Secured Creditor under *Till v. SCS Credit Corp*, 541 U.S. 465 (2004). The Court agreed and held the appropriate interest rate on a secured claim was 2% over the prime rate of interest or 5.75%. *In re Perkins*, 2013 Bankr. LEXIS 4539 (Bankr. E.D. Tenn. Oct. 30, 2013).

iii. 15 year amortized term loan on cropland at prime plus 2.5% is customary and provides a sufficient risk factor to the secured creditor. The debtor proposed a 15 year amortization term loan on cropland at prime plus 2.5%. The secured creditor objected arguing that it is customary for loans secured by crop land to mature within five years and that the customary interest rate would be 6.25% to 8%. The Court disagreed and held in favor of the debtor on the basis that to preserve the farming operation a 15 year term is required. Prime plus 2.5% provides a sufficient risk factor under the U.S. Supreme Court decision in *Till*. *In re Wise*, 2013 Bankr. LEXIS 2299 (Bankr. D.S.C. June 3, 2013).

iv. 25 year amortized term loan on ranch property is not reasonable. The debtors owned a 900 acre ranch. The debtors filed a Chapter 12 bankruptcy and proposed to pay the secured creditor over 25 years. The secured creditor objected on the basis that the terms were not reasonable. The Court agreed and held that a 25 year term was not reasonable under current market conditions for purposes of Code § 1225(a)(5)(B). *In re Standley*, 2013 Bankr. LEXIS 1114 (Bankr. D. Mont. Mar. 22, 2013).

v. **Prime plus 1.25% is customary and provides a sufficient risk factor to the secured creditor.** The debtors owned a 900 acre ranch. The debtors filed a Chapter 12 bankruptcy and proposed to pay the secured creditor over 25 years at prime plus 1.25%. The secured creditor objected on the basis that the interest rate was not reasonable. The Court disagreed and held that prime plus 1.25% is reasonable for purposes of Code § 1225(a)(5)(B). *In re Standley*, 2013 Bankr. LEXIS 1114 (Bankr. D. Mont. Mar. 22, 2013).

c. **Feasibility.**
i. **Partial liquidation of farming operation did not result in feasible plan.** Bruce and Stacie Meinders (the “Debtors”) were dairy farmer and were indebted to State Savings Bank (the “Secured Creditor”). The indebtedness was secured by mortgages on farmland. The Debtors filed a Chapter 12 Plan (the “Plan”) that proposed to sell a robotic milking machine and use the proceeds to purchase fifty (50) additional dairy cows. The Secured Creditor objected and the court agreed that the proceeds from the robotic milker would not be enough to purchase the minimum number of the cows needed to support the Plan and, therefore, the Plan was not feasible. *In re Meinders*, 2016 WL 1599508 (Bankr. N.D. Iowa 2016).

ii. **Failure to propose a feasible Chapter 12 plan is cause to dismiss.** Keith’s Tree Farm (the “Debtor”) was a tree farm. The Debtor is indebted to Grayson National Bank (the “Secured Creditor”). The debt is secured by the real property of the Debtor. The Debtor filed a series of five Chapter 12 bankruptcy cases; with the Debtor unable to confirm a plan in the first four cases. In filing the fifth bankruptcy the Debtor changed its management and liquidated certain assets. The Secured Creditor filed a motion to dismiss arguing that even with the change in management and liquidation of assets the proposed Chapter 12 plan was not feasible, as required by 11 U.S.C. § 1225, and the case should be dismissed. The court agreed and held that the record establishes that the Debtor would not be able to make all payments under the plan or otherwise comply with the plan, that the Debtor had failed to show any reasonable likelihood of reorganization, and that the unreasonable delay in proposing a confirmable plan to the court the Debtor’s gross mismanagement in failing to provide accurate financial information constituted cause to dismiss under 11 U.S.C. § 1208. *In re Keith’s Tree Farm*, 2016 WL 1086758 (Bankr. W.D. Va. 2016).

*Comment.* It is not entirely clear why the Secured Creditor allowed five Chapter 12 bankruptcies to be filed and elected not to file a motion for stay relief in an earlier bankruptcy. Had stay relief order been entered in an earlier bankruptcy, 11 U.S.C. § 109(g)(2) restricts the debtor from filing a later Chapter 12.

iii. **Chapter 12 plan was feasible even though projected revenue and expenses were optimistic.** Bright Harvesting, Inc. (the “Debtor”) was a custom harvester company and farmed some cropland. The Debtor is indebted to Farm Credit of New Mexico (the “Secured Creditor”). The debt is secured by the real property of the Debtor. The Debtor filed a proposed Chapter 12 plan. The Secured Creditor objected and argued that that the proposed Chapter 12 plan was not feasible, as required by 11 U.S.C. § 1225. The court disagreed and held that although the projected revenue and expenses were generally optimistic there was enough
evidence in the record after modification of the plan terms by the court to find that the plan had a reasonable likelihood of success. *In re Bright Harvesting, Inc.*, 2015 WL 7972717 (Bankr. D.N.M. 2015).

iv. **Past financial history provides no reasonable probability that the plan terms will be satisfied.** The debtors Randy and Geneva Perkins (“Debtors”) were indebted to Farm Credit (“Secured Creditor”) and the indebtedness was secured by a security interest in the farm products of the Debtor. The proposed Chapter 12 plan proposed to make a significant balloon payment at the end of the plan term. The Secured Creditor objected to the proposed Chapter 12 plan because the plan was not feasible and there was no reasonable probability that the plan terms will be satisfied. The Court agreed and held the Debtor did not have the ability to sustain and fund the plan based on their financial history. *In re Perkins*, 2013 Bankr. LEXIS 4539 (Bankr. E.D. Tenn. Oct. 30, 2013).

d. **Post-Confirmation.**

i. **A change in law does not satisfy the substantial or unforeseeable change in circumstances requirement necessary to modify a confirmed Chapter 12 plan.** Victoria Gardner (the “Debtor”) owned various parcels of real estate including property jointly owned by her and her husband, as well as property that included a historic residence listed on the National Register of Historic Places. The Debtor filed a Chapter 12 bankruptcy and confirmed a Chapter 12 plan (the “Plan”). The Plan required, among other things, that the Debtor sell the historic property within twenty-seven (27) months after the Plan’s confirmation. If the sale did not take place within that time frame, one of the junior priority lien holders (the “Junior Creditor”) would be allowed to commence a legal action to foreclose its lien. Upon expiration of the allowed time, the Debtor moved to modify the Plan, claiming she was unable to sell the property within the allocated period due to the expiration of a state tax credit for historic sites that was critically important to a sale. The Junior Creditor objected and the Court agreed on the basis that a change in the law (1) was not a change in the Debtor’s financial circumstances, (2) was reasonably foreseeable, and (3) was not a substantial change. To modify a confirmed Chapter 12 plan under 11 U.S.C.A. § 1229, the modification statute, the Court required the Debtor to show the Debtor experienced a substantial and unanticipated change in financial condition post-confirmation. Based on this test, the Court found that the change in law did not impact the Debtor’s financial circumstances and, even if it had, it was not a substantial or unforeseeable impact and a modification was unjustified. *In re Gardner*, 522 B. R. 137 (Bankr. W.D.N.C. 2014).
ii. **Chapter 12 plan modification is only allowed upon satisfaction of 11 U.S.C.S. § 1229(b).** Colby Daniels (the “Debtor”) filed for Chapter 12 bankruptcy and confirmed a Chapter 12 plan (the “Plan”). Subsequently, the Debtor proposed plan modifications under § 1229(b) to sell certain farmland. The Chapter 12 Trustee objected and the Court held that the sale price should be settled via auction. The Court eventually found that the Debtor failed to meet his burden with regard to the feasibility of his modified plan and, therefore, failed to meet the burden to modify a confirmed Chapter 12 plan under 11 U.S.C.A. § 1229(b). *In re Daniels*, 2015 Bankr. LEXIS 1609 (Bankr. W.D. La. 2015).

iii. **Chapter 12 trustee is not entitled to compensation from the sale of farm property.** The debtors Kenneth and Melissa McLendons (“Debtors”) own and operate a sod farm. The Debtors filed a Chapter 12 bankruptcy and, in conjunction with the filing, sold certain property. The sale was not contemplated by the Chapter 12 plan. The Debtors sought to apply the proceeds of the sale to a secured claim. The Trustee objected and argued that he was entitled to a statutory 10% fee from the proceeds. The Court disagreed and held that the trustee was not entitled to the statutory 10% fee on the proceeds of the sale because additional compensation was not allowed under 11 U.S.C. §326. The Trustee is only entitled to fees only for payments made under a confirmed plan. Because the sale of the farm was not contemplated in the confirmed Chapter 12 plans the Trustee was not entitled to his compensation. *In re McLendon*, 506 B.R. 243 (Bankr. N.D. Miss. Oct. 18, 2013).