An Agricultural Law Research Article

Farmer Reorganizations under the New Bankruptcy Code

by

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Originally published in LOYOLA LAW REVIEW
28 LOY. L. REV. 439 (1982)

FARMER REORGANIZATIONS UNDER THE NEW BANKRUPTCY CODE

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I. INTRODUCTION

The business of farming[1] has always been subject to un-

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1. The term "farming" is intended in its broadest sense to encompass any form of agricultural work. *But cf.* the definitions of "farmer" and "farming operations" found *infra*

predictable financial problems, especially since the farmer's crops may be endangered by weather, insects, and natural disasters. Additionally, farmers face the normal problems of all businessmen, which may be increased by unusual changes in the economy. All businesses have suffered recently from increases in interest rates, fuel shortages, declines in prices offered for goods, inflation, and other general economic problems, and the farmer is no exception. In fact, the farmer's prospects have become even more bleak over the past two years, and his present and future financial problems are becoming a topic of national concern. This article will explore the business of farming, the relief historically available for financially troubled farmers, and the present means of reorganizing farmers financially under the new Bankruptcy Code.[2]

II. PRESENT GENERAL FINANCIAL PROBLEMS OF FARMERS

Every business is vulnerable to inflationary spirals, increases in interest rates, competition for short-term, working-capital loans, depressed economic markets, and other general business conditions. Thus, the farmer-businessman must deal with these common problems, some of which may be controlled and some of which are unpredictable and cannot be controlled. To worsen his plight, the farmer is also especially jeopardized by special problems[3] such as the vicissitudes of the weather and natural catastrophes, which

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note 2.

2. The Bankruptcy Code is the result of action by the Commission on Bankruptcy Laws of the United States and was signed into law on November 6, 1978, as the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified at 11 U.S.C. §§ 101-151326 (Supp. IV 1980) and in scattered sections of 2, 7, 12, 15, 17, 18, 19, 20, 22, 28, 29, 31, 33, 40, 42, 43, 45, 46, 48, 49 U.S.C.). Title I of the Bankruptcy Reform Act of 1978, 11 U.S.C. §§ 101-151325 (Supp. IV 1980), shall hereafter be referred to as the Bankruptcy Code or simply as the Code.

A "farmer" is defined under the new Code as a "person" who received more than 80% of gross income in the tax year before filing from a "farming operation" owned or operated by such "person." 11 U.S.C. § 101(17) (Supp. IV 1980). A "person" is defined as an individual, partnership, or corporation. *Id.* § 101(30). A "farming operation" is defined to include farming, tillage of the soil, ranching, crop production, dairy farming, livestock or poultry production, and similar activities. *Id.* § 101(18). *See generally* Looney, *The Bankruptcy Reform Act of 1978 and the Farmer: A Survey of Applicable Provisions*, 25 S.D.L. Rev. 509 (1980). The new Code appears to broaden the scope of persons and entities who will be defined as "farmers" under the new Code. *See* Looney, *supra*, at 515.

3. For a discussion of the present problems abounding in northeast Louisiana, *see* Pope, *Broke—Poor Weather, High Interest Rates and Low Prices Put Farmers in Bind*, The Times Picayune/The States Item, Feb. 28, 1982, § 1, at 1, col. 1.

could cause either partial or total crop failure. Such natural disasters may also have long-range effects on production and earnings due to factors such as erosion and alterations in soil makeup.[4] Consequently, a farmer must make hard decisions which effect the outcome of crop yield and income.

Until recently most farmers were able to conduct operations on the internal financing that was provided from profits earned in prior years. However, the ability of farmers to generate internally their own working capital and financing has been diminished by several factors.

First, over recent years wide variations in weather have produced low crop yields.[5] This has caused decreased profits and precluded the normal practice of generating working capital internally through prior earnings and profits. Consequently, the erosion in profits and working capital has caused many farmers to obtain short-term, working-capital loans from commercial lenders to finance their operations. Naturally, such loans are made at the highest interest rates, thus compounding the profit erosion problem.[6]

Second, although the federal government has instituted programs over recent years to provide working-capital loans for farmers at low interest rates, these superficially attractive programs have had their own disadvantages. This borrowing has supplemented or provided needed working capital, but it has caused many farmers to become over-leveraged, top-heavy with debt. Federal agencies normally require security interests in virtually all of a farmer's land and equipment to secure the working-capital loans, leaving the farmer with little flexibility for other borrowing. Many Louisiana farmers have utilized these programs and become heavily burdened with debts. Thus, many local farmers are entering 1982 heavily in debt to federal agencies and commercial lenders.[7]

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4. *Id.*

5. In the Northeast Louisiana area, for example, droughts have occurred in three of the last four years. *See* Pope, *supra* note 3.

6. "Crushed between plummeting commodity prices and record interest rates, the United States farm economy is staggering toward one of its worst performances since the Depression." *The Ripples of a Farm Recession*, Business Week, Sept. 28, 1981, at 27.

7. There is a congressional movement to amend the Farmers' Home Administration (FmHA) regulations in order to prevent "massive numbers of farm foreclosures." [Jan.-June] Wash. Fin. Rep. (BNA) No. 8, at A-3 (Feb. 22, 1982); *see also* Pope, *supra* note 3.

As one writer has noted, farm debt has increased drastically over the last decade, and the "increasing debt-to-asset ratio reflects the increasing use of credit by farmers for operat-

Third, as mentioned before, the farmer is subject to peculiar problems, among them inclement weather. Even though changes in weather can be predicted to some degree, this provides the farmer no safeguard against extremely wet conditions, and only the farmer who has irrigation systems can be protected during droughts. Both droughts and rainy seasons can prevent the germination of crops, inhibit their growth and destroy some or all of the crop. In addition, excessive moisture may prevent harvesting and cause the loss of an entire crop. Naturally, extreme heat or cold can also damage or destroy crops. In Louisiana the 1981 drought had a devastating effect on the finances of farmers, causing them especially heavy losses. This will create grave problems for many farmers in 1982, especially for those over-leveraged.[8]

Fourth, over recent years farmers have increasingly been affected by our federal government's domestic and foreign policies.[9] Federal agencies have for a number of years purchased commodities for storage at specific support prices, have paid farmers not to plant, and have extended emergency loans for losses caused by natural disasters such as the drought recently experienced in northeast Louisiana.[10] Thus, our federal government has played a significant role in determining the productivity of American farmers as well as the prices received by those farmers.[11] Presently, partially due to these federal policies, the prices for commodities are not high, which further increases the problems that will be encountered by highly-leveraged farmers as they enter into the 1982 crop season.[12]

Fifth, and finally, the untimely demise of several grain elevators and storage facilities in Louisiana has created more unexpected financial problems for farmers. Several of these grain facilities have filed recently for reorganizations.[13] These proceed-

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ing expenses and capital expenditures." Looney, *supra* note 2, at 510.

8. *See* Pope, *supra* note 3.

9. Louisiana State Agriculture Commissioner Bob Odom has stated that the United States has "a national policy of cheap food." Pope, *supra* note 3, at 8. Net farm income is the lowest since the mid-1930's. *The Ripples of a Farm Recession*, Business Week, Sept. 28, 1981, at 27.

10. Many of the FmHA's programs oriented to making favorable loans to farmers, and especially "Economic Emergency loans," are slated to end this year. *See* Taylor, *1982: Another Tough Year?* 105 Farm J. 26 (1981); *Plummeting Prices Deepen Farmers' Woes*, Business Week, Dec. 21, 1981, at 37.

11. *See* Pope, *supra* note 3; *see also* the authorities cited *supra* notes 6, 9 & 10.

12. See the authorities cited *supra* notes 3, 6, 9 & 10.

13. At least four grain elevators in Louisiana have recently filed for reorganizations

ings will cause farmers to lose some or all of their stored produce and will suspend their cash flow until their commodities (or cash derived therefrom) are released from the jurisdiction of the bankruptcy courts. Obviously, this may create or enhance a cash-flow shortage for various farmers. As a result, the problems of farmers caused by the losses sustained from farming activities in 1981 will be further exacerbated by these unpredicted calamities in the storage of their crops.

All of the above factors lead one to two general conclusions. First, the yield of crops may never be predicted with a high degree of certainty until those crops are actually harvested. Second, the price that a farmer receives for his crops and the income that he might earn can never be predicted until his crops are sold and he actually receives the funds.

These factors compel these writers to one specific conclusion, *viz:* the position of the farming community in Louisiana, and possibly nationwide, is precarious. The cumulative losses over the last few years, when coupled with heavy borrowing during the same period, may cause a mass of farmers to be unable to meet their obligations as they become due. In turn, a collective default in farm-related obligations may trigger an unprecedented number of foreclosures in our faltering economy, which may further result in a partial or total collapse of the farming community and farm-related businesses. Ultimately, the forced liquidations of farms overburdened with debt may cause a tremendous loss of equity or value in farms.

All of these facts and factors subject agricultural finances to jeopardy and ruination and forebode dangerous consequences in 1982. Our economy is greatly dependent upon adequate farming commodities being produced by the farming community, and for this reason the welfare of American farmers has always been of great concern to Congress. When the Depression created tremendous financial despair for businesses in general in the 1930's, Congress moved to the aid of the farmers by passing section 75 of the old Act.[14] These writers believe that a better understanding of farm relief can be achieved by a review of the relief made available to farmers during and after the Depression under section 75, its amendments, and other legislation.

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under chapter 11 of the Bankruptcy Code.

14. Act of March 3, 1933, ch. 204, § 75, 47 Stat. 1467, 1470-73.

III. RELIEF AVAILABLE BEFORE AND AFTER THE DEPRESSION—A HISTORICAL OVERVIEW

Reorganization proceedings are for the purpose of rehabilitating businesses and businessmen, and these proceedings normally envision the readjustment of the debt/capital structure of an enterprise and its continuation in business, as opposed to the liquidation and dismantling of the enterprise.[15] Forced liquidations may cause unnecessary losses in property values.

The first three federal bankruptcy acts[16] were designed entirely for liquidation and contained no provisions for the rehabilitation of the debtor and preservation of his business.[17] An amendment to the third bankruptcy act providing rehabilitative relief was short-lived.[18] The fourth act, passed in 1898 (*old Act*),[19] was also inadequate in this regard, since the composition device offered under section 12 of the old Act[20] provided only limited relief for small debtors.[21] Section 12 was insufficient for rehabilitating either large corporate entities or farmers.[22]

Hence, there were no adequate rehabilitation statutes available for either businesses or farmers until 1933, when Congress enacted certain statutory rehabilitation provisions.[23] Remington[24] has

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15. *See generally* Blum, *The Law and Language of Corporate Reorganization*, 17 U. Chi. L. Rev. 565 (1950).

16. Act of April 4, 1800, ch. 19, 2 Stat. 19 (repealed 1803); Act of August 19, 1841, ch. 9, 5 Stat. 440 (repealed 1843); Act of March 2, 1867, ch. 176, 14 Stat. 517 (repealed 1878).

17. V. Countryman, Equity Receivership and Bankruptcy Reorganization 1. This work is not officially published, but is found in the teaching materials of Professor Countryman in his reorganization course at Harvard Law School.

For a historical discussion and perspective of the evolution of reorganization from equity receiverships through the Chandler Act, see 6 W. Collier, Collier on Bankruptcy ¶¶ 0.01-.10 (14th ed. 1979). The reader should note that the citation of this treatise is a reference to the fourteenth edition, which discusses bankruptcy law under the old Act; a discussion of the new Bankruptcy Code is contained in the fifteenth edition, first published in 1980, cited *infra* note 165.

18. *See, e.g., In re* Reiman, 20 F. Cas. 500 (C.C.S.D.N.Y. 1875) (No. 11, 675).

19. Act of July 1, 1898, ch. 541, 30 Stat. 544, 11 U.S.C. §§ 1-1255 (1976 & Supp. II 1978) (repealed 1979). The old Bankruptcy Act as amended will hereafter be referred to as the old Act or the Act, and all references to the old Act will be to the original sections of that Act.

20. *Id.* § 12, 30 Stat. at 549-50.

21. See the authorities cited *supra* note 17. Specifically, among other problems, secured creditors could not be bound under a plan confirmed under § 12. See also the discussion and authorities contained *infra* note 40. For the meaning of "composition," see *infra* text accompanying note 122.

22. See the authorities cited *supra* note 17.

23. Act of March 3, 1933, ch. 204, 47 Stat. 1467.

explained this historical event as follows:

> Section 75 was added to the Bankruptcy Act March 3, 1933 in the midst of the Great Depression. It formed a part of a new Chapter numbered VIII and entitled *Provisions for the Relief of Debtors*. Three forms of relief were established. Section 74, now Chapters XI and XII, dealt with *Arrangements*. Section 75 provided *Relief for Farmers*. Section 77 established *Railroad Reorganization*. On June 7, 1934, § 77B has become Chapter X. All of these Relief Sections or Chapters had a common purpose—to facilitate recovery from the depression.[25]

The initial reorganization statutes, which were contained in sections 74, 75, 77,[26] and 77B,[27] were passed during the Depression for the purpose of correcting the defective receivership procedure and replacing it with a comprehensive, statutory method of effecting rehabilitations.[28]

There was some argument that these sections were strictly emergency legislation, were passed to provide immediate statutory relief, and were poorly drafted because of the haste in their preparation and enactment.[29] Whether this argument is accurate is beyond the scope of this article; however, the reader should note that the legislative movement to enact a more appropriate statutory system for rehabilitation of financially troubled entities continued until 1938, when the Chandler Act was passed.[30] This Act repealed sections 74 and 77B.

However, the Chandler Act did not repeal section 75, which was the primary statutory vehicle for the rehabilitation of farmers both before and after enactment of the Chandler Act.[31] Rather, this section was maintained in force until March of 1949 and was not made a permanent part of the Bankruptcy Act of 1898 for various reasons.[32] In other words, section 75 was maintained as a sepa-

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24. 10 H. Remington, A Treatise on the Bankruptcy Law (1947). Harold Remington authored a comprehensive treatise on bankruptcy until his death, and The Lawyers Co-Operative Publishing Company continued this publication until the old Bankruptcy Act was repealed in 1979. Volume 10 of this treatise contains a comprehensive analysis of § 75 of the old Act.
25. *Id.* at 5.
26. Act of March 3, 1933, ch. 204, 47 Stat. 1467.
27. Act of June 7, 1934, ch. 424, 48 Stat. 911, 912-22.
28. See the authorities cited *supra* note 17.
29. *Id.*
30. The Chandler Act, ch. 575, 52 Stat. 840 (1938).
31. *See* 10 H. Remington, *supra* note 24, § 4002.
32. *Id.* § 4004. Remington points to the report of the House Committee on the Judici-

rate rehabilitative device which was extended through March 1, 1949, when it expired because it was not renewed by Congress.[33]

Section 75 will be explained in greater detail later, but the reader should note that no relief was expressly provided by Congress for farmers until their problems became particularly acute during the Depression. The elixir for the farmers' dilemma was initially the creation of section 75 and subsequently its amendments.

Rehabilitations for farmers were also available, and, especially after the expiration of section 75, through Chapter XII[34] of the Bankruptcy Act. However, Chapter XII was rarely used by farmers or other debtors to gain relief and rehabilitation;[35] and only one reported case can be found where Chapter XII was used as the vehicle for rehabilitation of a farmer's finances.[36] Hence, after the Depression and World War II the primary statute for rehabilitation of farmers was terminated, and Congress has not yet created a statutory vehicle expressly to alleviate agriculture's peculiar hardships.

In particular, there are no statutory provisions in the new Bankruptcy Code for rehabilitation of farmers. It thus appears that the relief available for farmers is the same as accorded businesses and businessmen in general under Chapter 11 of the new Bankruptcy Code.[37] This is unfortunate because farmers are presently experiencing especially great financial problems because of weather, inflation, and a general downturn in the economy. These problems are particularly acute in the southern part of the United States, and farmers in northeast Louisiana are facing extremely

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ary No. 1127, February 15, 1944, for a historical discussion and commentary on the subject of the temporary nature of § 75. Specifically, it appears that farmers were granted broader discharges than in ordinary bankruptcy proceedings. These broader discharge provisions appeared to make § 75 inconsistent with the permanent provisions of the old Bankruptcy Act, which contained more restrictions of the discharge of debts. *But cf.* the complete discharge of *all* debts for wage-earners under Chapter 13 of the New Bankruptcy Code. 11 U.S.C. §§ 1328(b) (Supp. IV 1980).

33. 10 H. Remington, *supra* note 24, § 4002.

34. The Chandler Act, ch. 575, §§ 401-526, 52 Stat. 840, 916-30 (1938).

35. For a discussion of Chapter XII generally, see Anderson & Ziegler, *Real Property Arrangements Under the Old and New Bankruptcy Acts*, 25 Loy. L. Rev. 713 (1979).

36. *In re* Benson, 9 Bankr. 854 (N.D. Ill. 1981).

37. *See generally* King, *Chapter 11 of the 1978 Bankruptcy Code*, 53 Am. Bankr. L.J. 107 (1979); Moller, *Chapter 11 of the 1978 Bankruptcy Code, or Whatever Happened to Good Old Chapter XI?* 11 St. Mary's L.J. 437 (1979). Any meaningful relief that might be provided farmers under Chapter 13 (which is primarily oriented to "wage-earners") is eroded because of the debt limitations and other restrictions imposed. *See generally* Looney, *supra* note 2.

critical problems. Because the old statutory means for farmer rehabilitation under section 75 are no longer available and because new relief for farmers has, to some degree, been reenacted under the new Bankruptcy Code, it would appear appropriate to contrast the old rehabilitative provisions with existing, available means for financial relief for farmers. This analysis will also suggest certain observations on the alternatives now available to farmers for rehabilitation of their financial affairs.

IV. FARMER RELIEF UNDER SECTION 75 OF THE OLD BANKRUPTCY ACT

A. Legislative Movement

On March 3, 1933, section 75 was added to the Bankruptcy Act for the purpose of permitting compositions and extensions for the benefit of farmers, similar to those provided for in section 74 for the benefit of individuals and partnerships.[38] Upon the filing of the farmer's petition under section 75, he and his property were brought under the exclusive jurisdiction of the Bankruptcy Court, regardless of the property's location, and all proceedings against him or his property were automatically stayed.[39]

The chief purpose of the provision was to make relief available for farmers whose affairs did not warrant or require liquidation.[40] Section 75 provided initially for composition or extension agreements that could be requested by the debtor and agreed to by a sufficient number of creditors.[41]

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38. *See generally* 10 H. Remington, *supra* note 24, §§ 4001-4131; Hanna, *Agriculture and the Bankruptcy Act*, 19 Minn. L. Rev. 1 (1934); Roberts, *Property, Mortgaged Land, and the Frazier-Lemke Act*, 13 N.C.L. Rev. 291 (1934); Comment, *A Survey of Sections 74 and 75 of the Bankruptcy Act in Actual Operation*, 43 Yale L.J. 1285 (1934). Prior to enactment of § 75, any meaningful rehabilitory relief for farmers was virtually unavailable under the Bankruptcy Act or any other statutes. *Id.*

39. 10 H. Remington, *supra* note 24, §§ 4001-4027.

40. "Forced liquidation of debtors' estates as in ordinary bankruptcy generally causes unnecessary losses." *Id.* § 4004, at 10.

41. *See generally id.*; Hanna, *supra* note 38 at 5. As Remington notes, under § 12 of the old Act, power was conferred upon bankruptcy courts to confirm compositions, if agreed to by a majority in number and amount of unsecured claims. Confirmation could be ordered without the necessity of adjudicating the debtor a bankrupt. The debtor took back his estate free from old claims and subject only to the new claims which he had agreed to pay. The consideration paid under the debtor's plan was distributed on account of old claims. 10 H. Remington, *supra* note 24, § 4005.

In comparison, § 75 enabled bankruptcy courts to confirm compositions or extensions of a farmer's secured *and* unsecured debts, "if agreed to by a majority in number and amount

Much of the commentary regarding the legislative history of section 75 indicates that this legislation was passed over the strenuous objection of various lenders.[42] Creditor-oriented interest groups argued that the legislation was a menace to the national credit structure, that it would afford no relief to debtors for whose benefit it was intended, that the provisions were ambiguous, that the legislation was unworkable, and that statutory relief was destructive of creditors' rights.[43] Notwithstanding these arguments, other commentary during this era suggested (a) that relief was necessary due to a steady decline in farm prices before the Depression (which was accelerated thereafter), due to a deflation in land values, and due to the constantly increasing burden of taxes; and (b) that the fears of the credit industry proved to be unfounded, because the implementation of section 75, as initially enacted, proved to be so cumbersome that any alleged harmful effects were negated by the inability of farmers to use the statute.[44] As initially drafted, section 75 was largely ineffectual as a vehicle to rehabilitate farmers; therefore, Congress moved to amend it one year after its enactment.

Criticism and irritation over the passage of section 75 in 1933 was heightened when Congress subsequently added subsection (s) to section 75 on June 28, 1934, to create what is commonly referred to as the first "Frazier-Lemke Act."[45] This amendment to section 75 significantly enhanced the relief available to farmers by impairing the rights of secured creditors to foreclose upon farm land.[46] Prior to the Frazier-Lemke Act, the farmer could only propose compositions and extensions; if these were not approved by the creditors and the court, he was forced to dismiss his proceeding or be adjudicated into straight bankruptcy.[47] The Frazier-Lemke pro-

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of secured *and* unsecured creditors." This new feature differed from § 12 by extending the bankruptcy court's power to bind secured debts. Section 75 thus appeared to be constitutional as initially drafted in 1933 and without the initial Frazier-Lemke Act (which will be discussed in detail later herein). *Id.*

42. See 10 H. REMINGTON, *supra* note 24; Hanna, *supra* note 38; and Comment, *supra* note 38.

43. *Id.*

44. *Id. See infra* note 47 and accompanying text.

45. Ch. 869, 48 Stat. 1289 (1934).

46. One commentator argued that, even if the Frazier-Lemke Act was held to be constitutional, it was "unfair, both in its harshness to creditors and in the implicit discrimination between the protection offered to farmers and other individual creditors." Hanna, *supra* note 38, at 32.

47. One commentator observed that, prior to enactment of the Frazier-Lemke Act, "[s]ection 75 was a hastily concocted statute dragooned into the [Bankruptcy] Act," and

visions gave the farmer increased rights in the event that the creditors and court did not approve any proposed composition or extension. Specifically, if the composition/extension was not approved, the farmer was adjudged a bankrupt, but was given a moratorium of five to six years within which to buy back his property from the court and his creditors.

Upon adjudication the farmer could request that all of his property, whether pledged, encumbered or unencumbered, be appraised and that his exemptions be set aside, subject to liens thereon.[48] The farmer then had two options by which he could redeem all or part of his property. Under one option, with the consent of those holding liens on the property redeemed, the farmer would pay the appraised value in an installment plan over a period of six years while retaining possession of his property. This repayment over six years was conditioned upon acceptance of such redemption or buy-back by the secured creditor affected;[49] and if the secured creditor objected to this partial-payment plan of purchase by the farmer, a second course of action was available.

Under the second option the court would stay all proceedings for a period of five years, allowing the farmer to retain possession of his property upon payment of only a reasonable rental and allowing the farmer to buy his property at the end of the five-year period by paying its appraised or reappraised value.[50] Therefore,

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that the "section as drafted proved almost wholly worthless." Hanna, *supra* note 38, at 5. Thus, without the marked relief afforded under the Frazier-Lemke Act, § 75 was not very useful or beneficial for farmers. *Id.*

48. *See generally supra* note 38.

49. The first option was described by the Supreme Court in Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555, 592 n.21 (1935), as follows:

> The prescribed payment (interest) for the first year is 1 per cent. on the appraised value. The prescribed payment for the second year is 3 ½ per cent. thereof (1 per cent. for interest, 2 ½ per cent. on account of principal). The prescribed payment for the third year is 2 ½ per cent. of the principal and as interest 1 per cent. on 97 ½ per cent. of the principal. The prescribed payment for the fourth year is 5 per cent. on account of the principal and as interest, 1 per cent. on 95 per cent. of the principal. The prescribed payment for the fifth year is 5 per cent. on account of principal, and as interest, 1 per cent. on 90 per cent. of the principal. The prescribed payment at the end of the sixth year is 85 per cent. of the principal, and as interest 1 per cent. of 85 per cent. of the principal. The present value calculated on a 6 per cent. basis, of all deferred payments (principal and interest) would be only 76.6 per cent. of the appraised value. In other words, the agreement to sell if assented to by the mortgagee would require him to relinquish his security not for its appraised value in cash, but for deferred payments which, if met, would yield (on a 6 per cent. basis) only 76.6 per cent. of the appraised value.

50. *Id.* at 592-93.

under either option, the Frazier-Lemke Act had the "controlling purpose of . . . [preserving] to the mortgagor the ownership and enjoyment of the farm property . . . and the avowed object . . . to take from the mortgagee rights in the specific property held as security; and . . . 'scale down the indebtedness' to the present value of the property."[51]

Secured creditors could retain their liens up to, but not exceeding, the appraised value until paid. Unsecured creditors were given a general lien subordinate to prior liens, but in no case could creditors thereafter assert, either against the farmer or his property, claims for an amount in excess of the appraised value of the property at the time of the filing of the petition. Therefore, the usual avenues available to secured creditors for realizing on their collateral were closed upon the filing of the farmer's petition.[52]

Prior to the enactment of section 75 in 1933 and the Frazier-Lemke Act in 1934, bankruptcy proceedings did not generally affect secured creditors at all, and the bankruptcy trustee took only such interest as the bankrupt might have transferred.[53] However, the Frazier-Lemke Act had the *express* purpose of impinging upon the rights of secured creditors since its main premise was to provide a moratorium for farmers to relieve them from overburdening mortgage indebtedness and the harshness resulting from a loss of their farms through foreclosure in a period of unprecedented depression.[54]

As Remington has pointed out, forced liquidations of a debtor's estate, as in ordinary bankruptcy, have generally caused unnecessary losses,[55] and where these losses have prevented farmers from cultivating their land and producing crops, the entire national economy has been affected.[56] Moreover, after the Depression had abated, the strain placed upon our economy by subsequent world-wide hostilities[57] caused section 75 to be continued and ex-

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51. *Id.* at 594.

52. *See* Roberts, *supra* note 38, at 291-92; Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555 (1935).

53. *See* Roberts, *supra* note 38, at 292; Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555, 586-91 (1935).

54. Roberts, *supra* note 38, at 292.

55. 10 H. Remington, *supra* note 24, § 4004, at 10.

56. *Id.*; *In re* Kalb, 54 F. Supp. 535 (D.C. Wis. 1944).

57. As stated in *In re* Kalb, 54 F. Supp. 535, 537 (D.C. Wis. 1944):

> When this section of the act was extended to March 4, 1944, our country was awakening to the need of a great defense effort. Many of the great nations of the world were

tended as emergency legislation until 1949.[58]

Therefore, in setting the enactment and amendment of section 75 in historical context, the reader must bear in mind that (a) the difficulties of farmers in the midst of the Depression were extraordinarily severe, (b) the Populist sentiment was "anti-big business," (c) lenders were viewed with suspicion,[59] and (d) the world-wide problems of war caused the statute to remain in force until after World War II.

B. Supreme Court Cases

The farm relief provided by Congress, especially under the Frazier-Lemke Act, created some of the most significant decisions regarding the authority of Congress under the bankruptcy power of the Constitution to impinge upon the rights of secured creditors. The history surrounding the invalidation of the initial Frazier-Lemke Act in 1935, and its subsequent reenactment and validation, can be traced through a trilogy[60] of significant and unprecedented Supreme Court decisions, beginning with *Louisville Joint Stock Land Bank v. Radford.*[61]

> then engaged in war. As was said by our Supreme Court in Falbe v. United States, 320 U.S. 549, decided January 3, 1944, "The danger of attack by our present enemies, if not imminent, was real, as subsequent events have grimly demonstrated. Congress realized that if war came our economy would be under great strain and there would of necessity be many dislocations, difficulties, and restrictions. We knew that agriculture would be called upon to expand greatly, for increased production would be essential to victory. Congress likewise bore in mind that upon the cessation of hostilities in World War I it was agriculture which first felt the chill breath of the great depression which all agree was an aftermath of that disrupting struggle. It must be assumed that Congress had sufficient justification to enact the original legislation."

58. 10 H. Remington, *supra* note 24, § 4004.

59. As a sign of the times, the following statement of Congressman Charles U. Truax in support of the Frazier-Lemke Act may be found at Hanna, *supra* note 37, at 8 n.8:

> On June 18, 1934, the Congress of the United States passed H.R. 9865, a new declaration of independence for the American farmer. When this law becomes effective I can but wonder what will become of the ruthless money lender when the breath of Gold leaves his feculent body and a financial death stops the rattling of his grasping brain, for he is unfit for the higher realm of life and too foul for the one below. He cannot be buried in the earth, lest he provoke a pestilence; nor in the sea, lest he poison the fish; nor swing in space like Mahomet's coffin, lest the circling worlds in trying to avoid contamination, crash together, wreck the universe, and bring again the noisome reign of chaos and Satan.

60. The trilogy of cases is Wright v. Union Cent. Life Ins. Co., 311 U.S. 273 (1940); Wright v. Vinton Branch of the Mountain Trust Bank, 300 U.S. 440 (1937); Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555 (1935).

61. 295 U.S. 555 (1935).

In *Radford* the debtor (Mr. Radford) filed for relief under section 75 in 1933 after defaulting on his loans to the Louisville Joint Stock Land Bank. Under the original foreclosure by the bank preceding the bankruptcy filing, a receiver had taken control of the mortgaged property. The debtor's petition was approved and a meeting of creditors was held, but the debtor failed to obtain the acceptance of the requisite majority in number and amount to the proposed composition. The bank offered to accept the deed of the mortgaged property in satisfaction of its debt and to assume the unpaid taxes, but the debtor refused to execute the deed.

Meanwhile, section 75 was amended by the Frazier-Lemke Act, and Mr. Radford filed amended petitions for relief under the new Act. This relief was attacked by the bank, but was upheld by both the Federal District Court for the western District of Kentucky[62] and the Circuit Court of Appeals for the Sixth Circuit.[63] Finally, the United States Supreme Court invalidated the amendment to section 75 known as the Frazier-Lemke Act and the relief that it made available to farmers.[64]

In essence, in the *Radford* case the bank refused the composition and extension proposal offered by the debtor, and after the debtor elected under the Frazier-Lemke Act to be adjudged a bankrupt, the bank declined to consent to the proposed sale to the debtor at the appraised value under option one of the Act (which provided deferred payments over six years), thereby forcing the debtor into option two, which provided for an appraisal of property, a five-year moratorium, and the right of the debtor to buy the property at the appraised (or reappraised) value during the five-year period.

In striking down section 75, the Supreme Court noted seven critical points. First, the debtor was allowed to redeem the property during the five-year moratorium for an amount *less* than the full mortgage debt, which was contrary to the general rule that a debtor could redeem his property free and clear of a mortgage debt only by paying the entire mortgage debt.[65]

Second, the sale to the debtor during the five-year period did not provide or allow the mortgagee to bid his claim in against the

62. *In re* Radford, 8 F. Supp. 489 (W.D. Ky. 1934).
63. Louisville Joint Stock Land Bank v. Radford, 74 F.2d 576 (6th Cir. 1935).
64. Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555 (1935).
65. *Id.* at 579 n.7.

property. Therefore, the act effected an *exclusive* sale to the farmer free of liens when the amount of the encumbrance exceeded the property. This ran contrary to the normal bankruptcy rule that a court should not authorize a sale at a price less than that which the lien creditor offered to pay for the property.[66]

Third, the Frazier-Lemke Act effected a fundamental change in the scope of the normal bankruptcy powers and impinged directly on the rights of secured creditors. In fact, the Supreme Court stated that the Act was the first step in a congressional attempt through the bankruptcy powers to abridge the substantive rights of a mortgagee in property held as collateral solely for the benefit of a mortgagor.[67]

Fourth, the Court affirmed that the bankruptcy powers granted to Congress in the Constitution were subject to the prohibitions of the fifth amendment, forbidding the taking of property without due process of law;[68] noting that the powers to regulate war, taxes, commerce, and aliens, were also subject to the fifth amendment, the Supreme Court reasoned that secured creditors were given too little protection for their property rights under the Frazier-Lemke Act.[69]

Fifth, the Court determined that the Act had the express and avowed purpose to take from the mortgagee various rights in specific property and that the cumulative effect of the Frazier-Lemke Act was the abridgement of sufficient rights to constitute a taking of property in violation of the fifth amendment.[70] The Court found that, under Kentucky law, the following property rights were taken from the bank:

> 1. The right to retain the lien until the indebtedness thereby secured is paid.
> 2. The right to realize upon the security by a judicial public sale.
> 3. The right to determine when such sale shall be held, subject only to the discretion of the court.
> 4. The right to protect its interest in the property by bidding at such sale whenever held, and thus to assure having the mortgaged property devoted primarily to the satisfaction of the debt, either through receipt of the proceeds of a fair competitive sale or by tak-

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66. *Id.* at 581-86.
67. *Id.* at 586-89.
68. *Id.* at 589-93.
69. *Id.* at 589-90.
70. *Id.* at 594-95.

ing the property itself.
5. The right to control meanwhile the property during the period of default, subject only to the discretion of the court, and to have the rents and profits collected by a receiver for the satisfaction of the debt.[71]

The court found that the "taking" of these rights under the Frazier-Lemke Act contravened the fifth amendment.[72]

Sixth, the Court noted that the *only* apparent right under the mortgage left to the bank was to retain its lien until sometime within the five-year period the mortgagor chose to release the lien by payment of the appraised value of the property.[73] Rejecting the argument that the dispossession of property during the five-year period was not injurious to the bank and that there was protection for the rights of the lender, the Court stated that there were fundamental differences in the delays and procedures under the Frazier-Lemke Act and the delays and procedures under prior bankruptcy legislation.[74]

Finally, the Court declined to determine whether the substantial changes created by the Frazier-Lemke Act were arbitrary or unreasonable, as being part of permissible public policy, reasoning that the central issue was whether the Act, as applied, took from the bank without just compensation (and gave to Radford) rights in specific property that were of substantial value.[75]

Based upon all of the above, the Court held that the Frazier-Lemke Act was unconstitutional. Significantly, the *Radford* case did *not* hold that the deprivation of a mortgagee by bankruptcy provisions of any *one* of the five property rights enumerated in that case would necessarily render the legislation unconstitutional.[76] Also, the entirety of section 75 was not nullified, but only the provisions added by the Frazier-Lemke Act that were subsections.[77]

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71. *Id.* at 594-95.
72. Actually, the decision is unclear as to (a) whether the "taking" of the rights in question was improper per se; or (b) whether the "taking" was proper, but not achieved with sufficient "due process" of law; or (c) whether both the "taking" and "due process" prohibitions of the fifth amendment were contravened.
73. 295 U.S. at 596.
74. *Id.* at 596-97.
75. *Id.* at 598-602.
76. 10 H. Remington, *supra* note 24, § 4005.
77. *Id.*

Thus, promptly after the Supreme Court's decision in *Radford,* Congress passed the second Frazier-Lemke Act in 1935 to correct the faults in the first Act.[78] Remington briefly summarizes the changes effected in the second Frazier-Lemke Act as follows:

> The Second Frazier-Lemke Act gives bankruptcy courts the power after the adjudication of the farmer to grant possession of all property and a three-year stay on payment of rental to be fixed by the court plus payments on principal if within the farmer's ability with the privilege of redeeming the property at the end of the three years of prior thereto at appraised or reappraised value. Secured creditors subject to the farmer's right of redemption were given the right to a sale at public auction. If the farmer defaulted during the stay or failed to redeem at the end thereof the court was authorized to appoint a trustee and proceed in ordinary bankruptcy.[79]

The new legislation prompted a new round of Supreme Court cases concerning challenges to the constitutionality of the new Frazier-Lemke Act. In *Wright v. Vinton Branch of the Mountain Trust Bank*[80] (*Wright I*) and *Wright v. Union Central Life Insurance Co.*[81] (*Wright II*), the Supreme Court upheld the new amendments.

Both *Wright I* and *Wright II* involved the same farmer-debtor and the same 200 acre tract of land located in Virginia. These cases reflect the changing attitude of the Supreme Court regarding the policies underlying the legislation (and especially the seriousness of the farmer's plight), the statutory relief necessary to rehabilitate farmers, and the breadth of the constitutional powers granted to Congress under the bankruptcy power to provide the needed relief.

In *Wright I* the Virginia farmer had given a deed of trust (mortgage) to secure a debt held by the Vinton Branch of the Mountain Trust Bank. The debt secured by the deed of trust was in default and the property had been advertised for sale pursuant to the deed of trust and the provisions of Virginia law. To prevent the pending foreclosure of the farm land, Mr. Wright filed a petition under section 75 of the Bankruptcy Act. The foreclosure was

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78. Ch. 792, 49 Stat. 942 (1935).

79. 10 H. Remington, *supra* note 24, § 4005, at 12; for a comparison of the changes in the second Act, see Wright v. Vinton Branch of the Mountain Trust Bank, 300 U.S. 440, 464-66 n.9 (1937).

80. 300 U.S. 440 (1937).

81. 311 U.S. 273 (1940).

stayed, and the debtor made a proposal for a composition that was unacceptable to the bank. Subsequently, Mr. Wright filed an amended petition under the new Frazier-Lemke Act, and asked that he be adjudicated a bankrupt and receive the benefits of the recently amended Act. Thereafter, on appeal the district court held the new Act to be unconstitutional. This ruling was affirmed by the appellate court of appeals, and the Supreme Court overruled both lower appellate courts.

The tenor of the Court's rationale in *Wright I* was strikingly different from that in *Radford*. It is submitted that the opinion rendered in *Wright I* reflected a clear shift in the Supreme Court's view of public policy, indicating a more liberal balancing of the need for farmer relief against the need for protection of the rights of secured creditors, with the balance clearly turned in favor of farmer relief. The Court began its decision with the proposition that *Radford* did *not* question the *power* of Congress to offer aid to distressed farmers by the means of a rehabilitation under the Bankruptcy Act; rather, the Court reasoned that the first Frazier-Lemke Act was declared unconstitutional "solely on the ground that the bankruptcy power of Congress, like its other great powers, is subject to the fifth amendment; and that, as applied to mortgages given before its enactment, the statute violated that Amendment, since it effected a substantial impairment of the mortgagee's security."[82] Thus, the decision centered more on the *degree* to which Congress exercised its power under the initial Act, rather than on its *authority* to exercise this power *vel non*.

The Court went on to state that its prior decision in *Radford* did *not* hold that the deprivation of any *one* of the enumerated (five) important substantive property rights would render the bankruptcy provisions invalid; rather, the *effect* of the prior statute was to deprive the mortgagor of the *entirety* of the five rights enumerated in the decision. The decision then discussed the changes that Congress had made in the Frazier-Lemke Act to preserve the mortgagee's rights.

First, there was congressional movement to leave the lien wholly unimpaired.[83] Creditors were allowed to retain their lien up to the actual value of the property, as fixed by appraisals, and the

82. 300 U.S. at 456-57.
83. *Id.* at 458 n.2. See *Wright I*, 300 U.S. at 464-66 n.9, for a comparison of the first and second Frazier-Lemke Acts.

new statute provided for a public sale in the discretion of the Court upon request of the secured creditor under appropriate circumstances.[84]

Second, the legislative intent was clear that the mortgagee was allowed the right to protect its interest in the property by bidding its lien claim at such sale, if held.[85]

Third, the Court rejected the proposition that the mortgagee should have the *absolute* right to determine when a sale should be made within the new three-year moratorium.[86] The Court reasoned that the three-year period of rehabilitation provided under the statute was not unreasonable, nor absolute, since a court might terminate the stay and order a sale at an earlier date. Further, the debtor's right to retain the property was conditioned upon his compliance with the orders of the court, which would include the right of the court to require reasonable rental payments from the debtor semiannually and to apply the payments to claims held by secured or unsecured creditors. Also, the possession of the debtor, rather than the mortgagee, was conditioned upon the existence of an emergency in each locality within which the Act would be implemented, and upon the cessation of any emergency, the court could shorten the stay of proceedings provided and immediately proceed to liquidate the estate.[87]

Fourth, the right of the mortgagee to control the property during default and have the rents and profits collected by a receiver for the satisfaction of its debt was rejected.[88] The Court reasoned that possession by the debtor, rather than a receiver, was reasonable and that the provisions for the payment of rental by the debtor were also reasonable.

Fifth, and finally, the Court rejected the contention that the delay in enforcement of the mortgage for an approximate three-year period was unreasonable, and the Court held that the other modifications of creditors' rights were reasonable.[89] Essentially, the Court held that the new Act did not modify secured creditors' rights, whether remedial or substantive, to such a degree as to

84. *Id.* But see *Wright II*, 311 U.S. 273 for an interpretation of when a public auction was appropriate.
85. 300 U.S. at 458-61.
86. *Id.* at 460-64.
87. *Id.*
88. *Id.* at 465-68.
89. *Id.* at 468-70.

deny the due process of law guaranteed by the fifth amendment. Hence, it held the new Act to be valid and constitutional.[90]

Approximately three years later, Mr. Wright again appeared before the Supreme Court in the *Wright II* decision.[91] In the second case Mr. Wright had experienced problems in gaining the relief necessary for his rehabilitation. Apparently, Mr. Wright had been granted the three-year moratorium under the second Frazier-Lemke Act, which embodied the rights to have his property appraised and to redeem it from the Court during the three-year moratorium. However, the facts of the decision indicate that shortly after being adjudged a bankrupt and being given the three-year period of redemption, a creditor, Union Central Life Insurance Co., had challenged the right of redemption by filing a petition praying that the proceeding be dismissed or, alternatively, that an immediate public sale be held. The debtor opposed the petition and filed a cross petition in which he sought to have the land appraised, to be allowed to redeem it at the appraised value, and to be discharged of any liability created through a deficiency in the sales price.

The narrow issue presented to the Supreme Court was whether Mr. Wright should be accorded the *exclusive* opportunity, on his request, to redeem the property at either a reappraised value or value fixed by the Court *prior* to the lower court ordering a public sale at which creditors and third parties could bid for the debtor's farm. The lower courts had denied him this right, holding that Mr. Wright had no hope of rehabilitation, had disobeyed orders of the court, and was not entitled to a reappraisal and redemption of the property.

The argument focused upon whether the debtor should have the right (to be exercised solely by him) to redeem the property at the value fixed by the court under the first proviso of section 75(s)(3), *before* denying him this exclusive right and offering the property via public sale to any other party under the second proviso of section 75(s)(3). In other words, if the court had granted the debtor's cross-petition, he would have been entitled to the sole right to have a reasonable time, fixed by the court, within which to redeem the property at its value and have it turned over to him free and clear of encumbrances, with his discharge being granted

90. *Id.*
91. 311 U.S. 273 (1940).

as part of the rehabilitation program. Only in the event the debtor failed to redeem within the fixed period of time (or disobeyed court orders) would the court authorize the public auction at which the secured creditor could bid its claim in as part of the auction price.[92]

The Court rejected the argument that there was a conflict between the provisions, holding that the Act must be liberally construed to give full relief to farmer-debtors. Thus, the rights of the debtor under the first proviso were held to override the rights of the creditor under the second proviso.[93]

The Court rejected the argument that giving the debtor the *exclusive* right to purchase the property at the appraised value, rather than allowing the mortgage holder to purchase the property at the full value of its secured claim, was unconstitutional. The only constitutional right given to the mortgagee the court held was to realize the full amount of the fair market value of his collateral and that he had no constitutional right to bid on his collateral or receive more than its appraised value.[94]

Moreover, the Court reasoned that Congress had not empowered it to deprive the farmer-debtor of his express and fundamental statutory right to redeem his property at the reappraised value, and if a court held otherwise, this "would be to imply a power of forfeiture wholly incompatible with the broad design of the Act to aid and protect farmer-debtors who were victims of the general economic depression."[95] Therefore, the Court ultimately reasoned

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92. *Id.*

93. As the Court stated:

> This Act provided a procedure to effectuate a broad program of rehabilitation of distressed farmers faced with the disaster of forced sales and an oppressive burden of debt. Safeguards were provided to protect the rights of secured creditors, throughout the proceedings, to the extent of the value of the property. There is no constitutional claim of the creditor to more than that. And so long as that right is protected the creditor certainly is in no position to insist that doubts or ambiguities in the Act be resolved in its favor and against the debtor. Rather, the Act must be liberally construed to give the debtor the full measure of the relief afforded by Congress . . . lest its benefits be frittered away by narrow formalistic interpretations which disregard the spirit and the letter of the Act.

Id. at 278-79 (citations omitted).

94. *Id.* at 278-82; *see infra* note 96 and accompanying text.

95. *Id.* at 280-81; as the Court stated:

> To hold that they empowered the court to deprive the debtor of his express and fundamental statutory right to redeem at the reappraised value or at the value fixed by the court would be to imply a power of forfeiture wholly incompatible with the broad design of the Act to aid and protect farmer-debtors who were victims of the

that Congress had the right, under the bankruptcy power, to take away certain property interests of creditors within constitutional limits in order to provide a comprehensive rehabilitation program for farmers during widespread conditions of economic depression. Such remedial and rehabilitative rights were held to be proper and not be denied due to suggestion of a contrary legislative intent.

The majority opinion clearly stated that there was no impropriety in denying the creditor the right to utilize all of his indebtedness in bidding for its collateral at a public sale, while granting the debtor the prior exclusive right to redeem the property from the Court at only its appraised value, which could be significantly less than the debtors owed to the objecting mortgage holder.[96]

C. Analysis

It is submitted that there are several propositions that might be extracted from this trilogy of decisions. First, and most obviously, the bankruptcy powers of Congress are, in fact, limited by the prohibitions of the fifth amendment; any legislation completely abrogating the fundamental rights of secured creditors might pass the bounds of reason and constitutionality.

Secondly, and within these initial broad generalizations, it is equally clear that Congress has been given the constitutional power to enact comprehensive legislation, if it so desires, expressly designed to (a) enable the farmer to keep his farm land and (b) allow him to rehabilitate himself through his labor and efforts in the face of depressed economic conditions. Specifically, the ultimate thrust of the second Frazier-Lemke Act was to permit seemingly bankrupt farmers to retain their land over a *minimum* period of three years, to be granted a moratorium in paying creditors, to be required to pay only a reasonable rental set by the court, to be allowed to work their land in an attempt to gain refinancing or other financial help, and to be required to pay only the appraised value of their property to redeem it, rather than the full amount of any burdensome mortgage debt. This last factor is especially important, since the Depression appeared to create a deflation in the

general economic depression.

96. The facts of *Wright II* indicate that the complaining creditor was owed approximately $16,000 and that the appraised value of the farm was only approximately $6,000. *Id.* at 276. Thus, under the redemptive powers granted to the farmer, Mr. Wright could buy back his farm for less than one-half of the mortgage debt encumbering the property. *Id.*

fair market value of farm land. The deflation in farm values, when coupled with the overburdening farm debt existing prior to and during the Depression, created an impossible situation for the farmer, to wit: he was simply not able to produce enough from the sale or refinancing of his farm, especially in a forced liquidation, to pay off the entire mortgage indebtedness, especially as it increased as interest accrued. This basic economic principle is one that these writers believe may be necessary for farmers in today's economy to rehabilitate fully their finances.

V. RELIEF FOR FARMERS AVAILABLE UNDER CHAPTER XII OF THE BANKRUPTCY ACT

Section 75 of the old Bankruptcy Act, as has been noted, was not made a permanent portion of the Act, and it expired on its own terms after 1949.[97] By 1950 and thereafter, the emergency situation created by the Depression and World War II had ended. Thus, the rehabilitation of individual farmers and farms owned by partnerships was provided under Chapter XII of the old Act,[98] and individual farmers and corporate farmers might find some rehabilitative relief under Chapter XI under the old Act.[99] However, since secured debts could not be altered under a Chapter XI arrangement plan,[100] the obvious vehicle for restructuring the farmer's finances was Chapter XII of the Act, which allowed an arrangement plan to alter both secured and unsecured debts.[101]

Fortunately, since World War II America's economy has substantially prospered, and there have been very few petitions filed under Chapter XII of the old Act.[102] In fact, Chapter XII was sel-

97. *See supra* notes 31-33 and accompanying text.

98. The Chandler Act, ch. 575, §§ 401-526, 52 Stat. 840, 916-30 (1938).

99. *Id.* §§ 301-399, 52 Stat. at 905-16.

100. *See generally* Anderson, *Partially Secured Creditors: Their Rights and Remedies under Chapter XI of the Bankruptcy Act*, 37 LA. L. REV. 1003 (1977); Anderson, *Secured Creditors: Their Rights and Remedies under Chapter XI of the Bankruptcy Act*, 36 LA. L. REV. 1 (1975).

101. *See generally* the authorities cited *infra* note 102.

102. *See generally* Anderson & Ziegler, *supra* note 35. Commentary on Chapter XII had been virtually nonexistent from the time of its enactment in 1938 as part of the Chandler Act until 1975. However, since 1975, several articles have been written analyzing Chapter XII, and at least one book has been written on the subject. *See, e.g.*, W. NORTON, REAL PROPERTY ARRANGEMENTS: CHAPTER XII, FEDERAL BANKRUPTCY ACT (1977); Anderson & Ziegler, *supra* note 35; Dole, *The Chapter XII Cram-down Provisions*, 82 COM. L.J. 197 (1977); Fine, *Unjamming the "Cram-down,"* 52 AM. BANKR. L.J. 321 (1978); Gilbert & Massari, *Chapter XII "Cram-down"—Bad Medicine or Just Desserts?* 52 AM. BANKR. L.J. 99 (1978);

dom used as a vehicle for rehabilitation by any entities until the real estate recession of 1974-1975.[103] During the early 1970's there was a "boom" in real estate and its financing. However, inflation and spiralling interest rates caused a severe recession in the years of 1974-1975, which precipitated an unprecedented increase in filings of real property arrangements.[104]

Macey & Macey, *The Chapter XII Chrysalis*, 52 AM. BANKR. L.J. 121 (1978); Merrick & Bufithis, *Chapter XII—Why Is It?*, 52 AM. BANKR. L.J. 213 (1978); Weintraub & Crames, *Chapter XII Comes of Age: Recent Developments*, 51 AM. BANKR. L.J. 291 (1977); Comment, *Constitutional Limitations on the Bankruptcy Power: Chapter XII Real Property Arrangements*, 52 N.Y.U. L. REV. 362 (1977).

103. *See generally* authorities cited *supra* note 102.

104. Prior to the real estate recession in 1974-1975, there were only seven reported cases concerning confirmation of Chapter XII plans. Sumida v. Yumen, 409 F.2d 654 (9th Cir. 1969); Rader v. Boyd, 267 F.2d 911 (10th Cir. 1959); Meyer v. Rowen, 195 F.2d 263 (10th Cir. 1952); *In re* Herweg, 119 F.2d 941 (7th Cir. 1941); Kyser v. MacAdam, 117 F.2d 232 (2d Cir. 1941); *In re* Hamburger, 117 F.2d 932 (6th Cir. 1941); Kunze v. Prudential Ins. Co. of America, 106 F.2d 917 (5th Cir. 1939).

After 1974 there was a tremendous increase in reported Chapter XII cases analyzing confirmation of plans and many other aspects of Chapter XII proceedings. Bizzell Pharmacy, Inc. v. Hemingway, 12 COLLIER BANKR. CAS. 2d 270 (4th Cir. 1977); *In re* Pembroke Manor Apts., 547 F.2d 805 (4th Cir. 1977); *In re* Castle Village Co., 4 BANKR. CT. DEC. (CRR) 730 (S.D.N.Y. 1978); *In re* Walker, 4 BANKR. CT. DEC. (CRR) 697 (M.D. Fla. 1978); *In re* Bell Tower Plaza, 4 BANKR. CT. DEC. (CRR) 678 (C.D. Cal. 1978); *In re* KRO Assocs., 4 BANKR. CT. DEC. (CRR) 462 (S.D.N.Y. 1978); *In re* LaMarche and Cerino, 4 BANKR. CT. DEC. (CRR) 443 (M.D. Fla. 1978); *In re* Stillbar Constr. Co., 4 BANKR. CT. DEC. (CRR) 452 (N.D. Ga. 1978); *In re* Bergman, 3 BANKR. CT. DEC. (CRR) 1313 (S.D.N.Y. 1978); *In re* Pickett, Gardner, Landers & Assocs., 3 BANKR. CT. DEC. (CRR) 727 (N.D. Ga. 1977); *In re* Hobson Pike Assocs., 15 COLLIER BANKR. CAS. 2d 346 (N.D. Ga. 1977); *In re* Fierman & Fierman, 3 BANKR. CT. DEC. 1006 (CRR) (E.D. Pa. 1977); *In re* Bergman, 14 COLLIER BANKR. CAS. 2d 222 (S.D.N.Y. 1977); *In re* Bekare Realty Assocs., 14 COLLIER BANKR. CAS. 2d 202 (E.D. Pa. 1977); *In re* Brookhollow Assocs., 14 COLLIER BANKR. CAS. 2d 251 (D. Mass. 1977); *In re* Nevada Towers Assocs., 14 COLLIER BANKR. CAS. 2d 146 (S.D.N.Y. 1977); *In re* Romano & Romano, 12 COLLIER BANKR. CAS. 2d 513 (N.D. Ill. 1977); *In re* Tucker, 13 COLLIER BANKR. CAS. 2d 148 (D. Conn. 1977); *In re* Marietta Cobb Apts., Co., 3 BANKR. CT. DEC. (CRR) 720 (S.D.N.Y. 1977); *In re* Country Green Ltd. Partnership, 3 BANKR. CT. DEC. (CRR) 427 (W.D. Va. 1977); *In re* Pine Gate Assocs., 3 BANKR. CT. DEC. (CRR) 301 (N.D. Ga. 1977); *In re* Triangle Inn Assocs., 3 BANKR. CT. DEC. (CRR) 716 (E.D. Va. 1977); *In re* Hartsdale Assocs., 3 BANKR. CT. DEC. (CRR) 460 (S.D.N.Y. 1977); *In re* Hartsdale Assocs., 13 COLLIER BANKR. CAS. 2d 692 (S.D.N.Y. 1977); *In re* St. Simon's Properties, 2 BANKR. CT. DEC. (CRR) 1400 (N.D. Ga. 1976); *In re* Nob Hill Apts., 2 BANKR. CT. DEC. (CRR) 1463 (N.D. Ga. 1976); *In re* Pine Gate Assocs., 2 BANKR. CT. DEC. (CRR) 1478 (N.D. Ga. 1976); *In re* Pine Gate Assocs., 3 BANKR. CT. DEC. (CRR) 141 (N.D. Ga. 1976); *In re* Pine Gate Assocs., 3 BANKR. CT. DEC. (CRR) 137 (N.D. Ga. 1976); *In re* Hartsdale Assocs., 13 COLLIER BANKR. CAS. 2d 1275 (S.D.N.Y. 1976); *In re* Huntley Square Assocs., 2 BANKR. CT. DEC. (CRR) 1417 (D. Md. 1976); *In re* Sixth Ave. Inv. & Dev. Co., 2 BANKR. CT. DEC. (CRR) 1222 (S.D. Cal. 1976); Darvilla Housing Corp. v. Accousti, 2 BANKR. CT. DEC. (CRR) 1093 (D. Conn. 1976); *In re* Hall Assocs., 2 BANKR. CT. DEC. (CRR) 432 (E.D. Pa. 1976); *In re* Helmwood Apts., 2 BANKR. CT. DEC. (CRR) 1151 (N.D. Ga. 1976); *In re* Bearden, 2 BANKR. CT. DEC. (CRR) 1180 (N.D. Ga. 1975); *In re* Consol. Motor Inns, 1 BANKR. CT. DEC. (CRR) 1526 (N.D. Ga. 1975).

It is submitted that the increase in filings of real property arrangements during 1975-1978 was caused more by the building boom in apartment projects, hotels, and similar real estate projects, as opposed to economic problems peculiar to the farming industry. After the 1974-1975 recession, however, there was a short upswing in the nation's economy in approximately 1978, and then a downturn. Our nation is now faced with a severe recession that these writers believe will result in depressing effects in segments of the economy. One of these is the farming community, which is presently experiencing unprecedented financial calamities for reasons stated previously herein.

The relief that was available to farmers prior to the enactment of the new Bankruptcy Code in 1978 can be appreciated by comparing the relief available under section 75 in "emergency" conditions (created by the Depression and World War II) existing between 1933-1949 to the relief available under Chapter XII in "nonemergency" situations existing between 1950-1979.

A recapitulation of the relief available under section 75 is as follows:

(1) The farmer-debtor could petition for relief, propose a composition or extension, and attempt to gain acceptance and approval of it by his creditors and the court.

(2) If the court and creditors refused the composition or extension offered, the farmer-debtor could be adjudged a bankrupt and have one of two options to repurchase his farm.

(3) Under *either* option, the farmer-debtor would have his property appraised and his exemptions set aside to him.

(4) Under the first option, the farmer-debtor would be required to pay interest of one per cent of the appraised value of the property that he desired to retain during the first year; he would then have a graduated repayment schedule by which he could purchase the property that he retained at the full appraised value, but with little interest, over a total period of six years. This option required the consent of those holding liens on the property retained by the farmer.

(5) If the lienholders failed to consent to the first option, or if the farmer desired the second option, he was allowed a three-year moratorium, during which time he would retain possession of his property, farm his land, pay a reasonable value to be set by the

court (the rental would be allocated in payment among his creditors), and have the exclusive right to buy his property from the court at its appraised value, so long as he complied with the orders of the court. The appraised value was the amount fixed by the court upon adjudication, unless there was a subsequent reappraisal at or before the redemption of the property.[105]

(6) Under section 75, as amended by the Frazier-Lemke Act, there was an express legislative attempt to provide the farmer-debtor with the *exclusive* right to buy his property (presumably comprising principally his farm land) at a price equalling only its appraised value and without regard to the total encumbrances on the property. This had the ultimate net effect of "scaling down" the amount to which the secured creditors were entitled to the actual value of the farm, rather than the liens that were held against the property, and to reduce the "scaled down" liens to an *in rem* status.[106]

In contrast with the above, Chapter XII of the Bankruptcy Act afforded a multiplicity of solutions for restructuring debts secured by real estate to allow its retention by the debtor.[107] Obviously, by restructuring the obligations secured by a debtor's real estate, the debtor gained more "breathing room" within which these obligations might be satisfied. Under Chapter XII certain principles emerged regarding the permissible metes and bounds within which the debts encumbering real estate projects might be restructured and reorganized:

(1) The terms of the mortgage debt could be extended.[108]

(2) The interest rate of a mortgage debt could be adjusted to current market rates.[109]

(3) Payments required for the mortgaged debt of either princi-

105. See the authorities cited *supra* notes 38-96 and accompanying text. The farmer-debtor was discharged of any personal liabilities, which had the ultimate effect of reducing the "scaled down" lien(s) on the farm to an *in rem* status. *See supra* note 52 and accompanying text.

106. See the authorities cited *supra* notes 38-96 and accompanying text.

107. See the authorities cited *supra* notes 102 & 104 and accompanying text.

108. Wachovia Bank & Trust Co. v. Harris, 455 F.2d 841 (4th Cir.), *cert. denied*, 409 U.S. 844 (1972) (a Chapter X case); *In re* Benson, 9 Bankr. 854 (N.D. Ill. 1981); *In re* Castle Village Co., 4 Bankr. Ct. Dec. (CRR) 730 (S.D.N.Y. 1978); *In re* KRO Assocs., 4 Bankr. Ct. Dec. (CRR) 462 (S.D.N.Y. 1978); *In re* Triangle Inn Assocs., 3 Bankr. Ct. Dec. (CRR) 716 (E.D. Va. 1977).

109. *See* cases cited *supra* note 108.

pal or interest could be deferred and postponed.[110]

(4) Deferred or reduced payment of principle or interest could be added to the mortgage balance.[111]

(5) However, if there was equity in the property above the mortgage debt, there could be no reduction in the principal of the mortgage.[112]

(6) Also, the secured creditor was entitled to adequate protection of his collateral, but only to the extent and value of (or equity in) his collateral.[113]

(7) Also, if a creditor was partially (inadequately) secured, he was only entitled to protection for the value of (or equity in) his security and could have the deficiency in his secured claim satisfied in a manner similar to that provided for unsecured creditors.[114]

(8) Further, if a creditor was inadequately secured and if his mortgage was *in rem* against the debtor's property, the deficiency of his claim, as against his collateral, could be extinguished under the plan.[115]

(9) More importantly, if there was no equity in the real estate securing the claim of a mortgage holder, his claim could be relegated to the status of an unsecured creditor, dealt with as such, and erased as an inscription in the mortgage records.[116]

(10) As to unsecured creditors in Chapter XII proceedings, they were only entitled to receive what would be available in the event of a bankruptcy liquidation proceeding and to receive adequate protection for this liquidation value.[117]

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110. *See* cases cited *supra* note 108.

111. *See* cases cited *supra* note 108.

112. Rader v. Boyd, 267 F.2d 911, 913 (10th Cir. 1959); Kyser v. MacAdam, 117 F.2d 232, 238 (2d Cir. 1941); *In re* Pine Gate Assocs., 2 Bankr. Ct. Dec. (CRR) 1478 (N.D. Ga. 1976); W. Norton, *supra* note 102, pts. 24 & 25, at 80-118.

113. *In re* KRO Assocs., 4 Bankr. Ct. Dec. (CRR) 462 (S.D.N.Y. 1978); *In re* Hartsdale Assocs., 3 Bankr. Ct. Dec. (CRR) 46 (S.D.N.Y. 1977); *In re* Pine Gate Assocs., 2 Bankr. Ct. Dec. (CRR) 1478, 1491 (N.D. Ga. 1976); *In re* Accousti, 2 Bankr. Ct. Dec. (CRR) 1093 (D. Conn. 1976); W. Norton, *supra* note 102, pts. 24 & 25, at 80-118; *see also In re* 620 Church St. Bldg. Corp., 299 U.S. 24 (1936); Anderson, *Partially Secured Creditors: Their Rights and Remedies Under Chapter XI of the Bankruptcy Act*, 37 La. L. Rev. 1003 (1977).

114. *See* authorities cited *supra* note 113.

115. *See* authorities cited *supra* note 113.

116. *See* authorities cited *supra* note 113.

117. *See* comment, *supra* note 102.

(11) In regard to disposition of assets in the Chapter XII proceeding, a purchaser or the debtor was only required to pay the appraised value of the assets to those holding mortgages on it, in the event the asset was sold or retained by the debtor.[118]

(12) Further, if an item of collateral was abandoned, the debt that it secured was imputed to the appraised value of the abandoned collateral and thereby satisfied in an amount equal to the value of the abandoned collateral.[119]

As explained above, in Chapter XII proceedings restructurings of mortgaged debts aided in the rehabilitation of debtors and their real estate projects, so that they could realize the greatest possible value from their assets, and especially their real property. The means for achieving this benefit, in addition to the restructuring of the debts secured by real estate, were usually derived from, or enhanced by, a number of financial decisions or transactions concerning the retention or disposition of the property, including:

(1) The debtor could sell his assets as a "going concern" or in an "orderly liquidation" so as to achieve the greatest price.[120]

(2) The debtor might be able to "syndicate" his assets, which envisioned the procuring of funds and capital from a syndicate of investors who might receive economic or tax benefits from the assets that were the subject of the "syndication."[121]

(3) The debtor could merge his assets or business with more successful related entities to enhance the resuscitation of his finances.[122]

(4) The debtor could choose to retain his assets and use the assets to produce future earnings. And through the Chapter XII plan, he could then attempt to achieve either a settlement of his debts in an amount less than their face value (commonly known as a "composition"), extend the period of time for the repayment of his debts from future earnings (commonly known as an "extension"), or request both a composition of his debts and an extension

118. *In re* Pine Gate Assocs., 2 Bankr. Ct. Dec. (CRR) 1478, 1482 (N.D. Ga. 1976); W. Norton, *supra* note 102, pts. 24 & 25, at 80-118; *see generally* the authorities cited *supra* note 113.

119. Act of July 1, 1898, ch. 541, 30 Stat. 544, 560. For a general discussion of this proposition, *see* Anderson, *supra* note 113.

120. *See generally* Anderson & Ziegler, *supra* note 35.

121. *Id.*

122. *Id.*

of the time within which to repay them from future earnings.

(5) The debtor could offer that his creditors exchange their claims for stock, property, or partnership interests in his assets in satisfaction of the claims against the assets, which had the result of allowing the creditors to exchange their debt position for an equity, investment, or partnership position.[123]

(6) In addition, the debtor could choose to abandon unprofitable or unproductive assets (which carried with it an extinguishment of that portion of liabilities amply secured by any encumbrances on the abandoned assets), and the debtor could retain his more productive and profitable assets, so as to produce future earnings to pay creditors and reform his finances.[124]

VI. RELIEF AVAILABLE TO FARMERS UNDER THE NEW BANKRUPTCY CODE

A. Legislative Analysis

The means for achieving rehabilitation under Chapter XII was both the ability to restructure mortgage debts encumbering a debtor's assets and the subsequent leeway to make appropriate decisions concerning their retention or disposition. These dual decisions were the principal *modus operandi* for achieving rehabilitation. This vehicle has been carried forward and reenacted in the new Bankruptcy Code. The new Code has consolidated reorganizations formerly existing under Chapters X, XI, and XII of the old Act into one new chapter, which is Chapter 11 of the new Code.[125] The substantive law of these chapters under the old Act has been, to a large extent, integrated into Chapter 11 of the new Code.[126] It is submitted that the principal limitations in the rehabilitation, reorganization and restructuring process under the new Code, as compared to Chapter XII of the old Act, are as follows:

(1) A secured creditor may elect under section 1111(b)[127] of the new Code to have his claim treated specially, which would have

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123. *Id.*

124. *Id.*

125. *Id.* Note, U. ILL. L.F. 251 (1980); Klee, *All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code*, 53 AM. BANKR. L.J. 133 (1979); Comment, *From Debtor's Shield to Creditor's Sword: Cram Down Under the Chandler Act and the Bankruptcy Reform Act*, 55 CHI[-]KENT L. REV. 713 (1979).

126. *See generally* authorities cited *supra* note 125.

127. 11 U.S.C. § 1111(b) (Supp. IV 1980).

the specific purpose of allowing the creditor to preclude the debtor's scaling down (reducing) the mortgage debt to the value of the security and having the deficiency in the claim against the collateral treated as an unsecured debt.[128]

(2) Similarly, under section 1111(b) of the new Code, if a secured creditor holds an *in rem* mortgage, he cannot be forced against his will to receive shortly after confirmation only the value of his collateral; rather, he may elect to have his claim treated as though he had recourse against the debtor for the entirety of his claim (and thereby not be relegated entirely to his collateral and the value thereof).[129]

(3) Likewise, under section 1111(b) of the new Code, the secured creditor may elect to retain his lien against the collateral for the face amount of his debt and *not* have his lien fully or partially eradicated, even if there is marginal equity in his collateral.[130]

(4) But even if the secured creditor elects under section 1111(b) to retain his full lien, the debtor is only required to make future payments equal to the value of the *collateral*, rather than the face amount of the mortgage debt.[131] It is submitted that section 1111(b) inhibits farmer relief only where the farmer-debtor desires to sell or refinance his mortgaged farm land shortly after confirmation, since the election under section 1111(b) primarily precludes the secured creditor's having his lien "scaled down" to the appraised value of his collateral at confirmation and then being "cashed out" shortly thereafter through a sale or refinancing by the debtor.[132] Conversely, if the farmer desires to keep his land, not refinance it, pay the lienor(s) from an income stream provided by future earnings, and have the payments geared to the appraised value of the farm (rather than the mortgage debts encumbering it), the authors suggest that this result is expressly permitted under section 1129(b)(2)(A) of the Code. Thus, the new Code has the practical result, if not the intent, of "scaling down" secured debts (but not the liens securing them) because the income stream

128. *Id. See generally* Klee, *supra* note 125, at 150-56.

129. *Id. But cf. infra* notes 131-33 and accompanying text.

130. *Id.* However, if the creditor's lien is worthless or of little value, he is not eligible to make an election under § 1111(b) of the new Code. *See* Klee, *supra* note 125, at 153.

131. 11 U.S.C. § 1129(b)(2)(A) (Supp. IV 1980); *see* Klee, *supra* note 125, at 153.

132. As one commentator has opined, §§ 1111(b)(2), 1129(a)(7)(B), and 1129(b)(2) appear to preclude proponents of a plan from "appraising a creditor's collateral and buying him out." Klee, *The New Bankruptcy Act of 1978*, 64 A.B.A. J. 1865, 1866 (1978).

needed to satisfy the secured debt(s) must only have a "current value equal to the value of the collateral"[133] and not the amount or value of the debt(s).

In conclusion, and in comparison to section 75 and Chapter XII of the old Act, the main limitation imposed by the new Code on the restructuring of debts secured by real estate is to preclude (a) the "scaling down" of the face amount of mortgage debts to the value of the underlying collateral, and (b) the "cashing out" of the "scaled down" debt by the debtor shortly after confirmation, if the creditor opts for special treatment.[134] Under section 75 the express purpose of the statute was to "scale down" the mortgaged debt(s) on farms to the fair market value of the farm, as fixed by appraisal, and allow the farmer to have a three-year period of time within which to redeem his property from the bankruptcy court and "cash out" his mortgage creditors for the appraised value.[135] This right of redemption for less than the amount of the mortgaged debt was (and still is) an important right where the value of farm land is decreasing due to economic forces beyond the farmer's control; but the new Code appears to permit this result only by allowing the debtor's future payments to be made over an extended period and to be geared to the value of the farm.

Similarly, under Chapter XII of the old Act, it was clearly established that the debtor had the right to retain and buy back his property from the court and creditors for its appraised value, with the unsecured (undersecured) portion of the debt secured by the property to be treated as unsecured debt or extinguished (in the event the obligation was *in rem* to the property).[136] Therefore, the farmer-debtor had the clear right to relieve himself of oppressive and cumbersome mortgage debts under the format of redeeming his property at its fair market value. Further, it was equally clear that under Chapter XII the farmer-debtor could restructure immediate pressing obligations over a twenty-year period, thereby gaining a significant extension of time within which to pay the debts against his farm.[137] Under the old Act bankruptcy courts had the authority to require mortgage holders to accept the payment of this reduced debt from the farmer over a reasonable period of

133. 11 U.S.C. § 1129(b)(2)(a)(i) (Supp. IV 1980).
134. *See* authorities cited *supra* note 125.
135. *See* authorities cited *supra* notes 38-96 and accompanying text.
136. *See* authorities cited *supra* note 125.
137. *In re* Benson, 9 Bankr. 854 (N.D. Ill. 1981).

time.[138] Under section 75 the farmer was given three years within which to redeem his property, and although there are few specific cases so holding, it is submitted that under the "cram-down" powers of Chapter XII bankruptcy courts could have required an even longer period of time for the debtor to redeem his farm at the reduced appraised amount under appropriate factual circumstances.[139] Subject to only the limitations created under section 1111(b) inhibiting the right of the debtor to "scale down" and reduce mortgage debts under the new Code, there have been several cases according farmers broad flexibility to restructure their mortgage debts under Chapter 11 of the new Bankruptcy Code and thereby retain their farm land and pay their creditors from the future earnings derived from the crop production of their farm.

B. Cases Under the New Code

Remembering that many of the principles for rehabilitation existing under Chapter XII of the old Act were carried over and reenacted in Chapter 11 of the new Code, one might conclude that the most significant rehabilitation case under the old Act was *In re Benson*[140] and that it is still good precedent for reorganization cases under the new Code. In *Benson* the debtor owned a farm which was valued in excess of the one mortgage debt against it, which was approximately $179,093.28. In comparison, the debtor owed approximately $529,299.39 in debts secured by other (personal) property and approximately $168,047.05 in unsecured debts. The debtor's plan was not clear as to the treatment of chattel mortgage holders and unsecured creditors, and since the opinion stated that these classes of creditors accepted the plan, the treatment of these claims is not important for purposes of this analysis. What is important was the restructuring of the debt owed to the sole creditor secured by the debtor's farm.

At filing, the mortgage loan was fully due and payable in its entire amount. The debtor's plan provided that this creditor's

138. *In re* KRO Assocs., 4 Bankr. Ct. Dec. (CRR) 462 (S.D.N.Y. 1978). In the *KRO* case the court held that a first mortgage debt could be reduced to the value of the real property and that the debtor could pay the "scaled down" mortgage debt over a reasonable number of years, if there was provided a reasonable interest rate for the deferred payments, and if the debtor would provide evidence of (or a guaranty proving) a willingness to fulfill the repayment schedule proposed under the plan. *Id.* at 465.

139. *Id.*

140. 9 Bankr. 854 (N.D. Ill. 1981).

claim, to the extent fixed and allowed, would be paid in full over twenty years, with interest thereon at prevailing rates. The initial payment would be made at confirmation of the plan, and the balance was deferred and paid in nineteen consecutive, equal annual installments. The debtor owned both a retail store and engaged in farming operations, and the plan provided that this deferred mortgage debt would be funded by income from both operations.

The secured creditor in question strenuously objected to the restructuring of its mortgage debt, but the court exercised its "cram-down" power because it determined that the creditor, although not consenting to the plan, was (1) receiving adequate protection for the realization of the value of its debt as called for under section 461(11) of Chapter XII,[141] (2) receiving completely compensatory treatment as envisioned by *In re Mural Holding Corporation,*[142] and (3) receiving "fair and equitable" treatment of its claim under generally accepted principles of reorganization law.[143] The court rejected the creditor's argument that adequate protection was not being provided under the plan, since the protection was not "immediately and completely compensatory."[144] The fact that the loan had an original short term of two years and was fully due and payable at filing was held to have no bearing on the debtor's right to restructure it into a long-term loan over twenty years and thereby gain a reasonable time for repayment. As the court noted, "Since the debtor's farm land is undisputedly worth far more than the Bank's claim and the value is not depreciating, adequate protection exists if the debtor's plan pays the Bank's claim over 20 years with interest at rates to make the Bank whole."[145] In essence, the court pointed out that if the debtor defaulted under the plan, the objecting creditor would be fully protected by its right to foreclose on valuable farm land, which was being retained as security by the creditor under the plan.

This case clearly established the proposition that farmers should have the right to retain their land, restructure their mortgage debts over a reasonable time, and pay the mortgage debts out of future earnings. This philosophy has been reenacted in section

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141. The Chandler Act, ch. 575, § 461(11), 52 Stat. 840, 922 (1938).

142. 75 F.2d 941 (2d Cir. 1935).

143. *See, e.g.*, Wachovia Bank & Trust Co. v. Harris, 455 F.2d 841 (4th Cir.), *cert. denied*, 409 U.S. 844 (1972) (real estate reorganization case under Chapter X of the old Act).

144. *In re* Benson, 9 Bankr. 854, 858 (N.D. Ill. 1981).

145. *Id.*

1129(b)(2)(A) of the new Bankruptcy Code, which gives the court the right to confirm a plan of reorganization over an objecting secured creditor's dissent, where the objecting creditor will be paid in full, together with an appropriate interest rate, under the reorganization plan.[146] This proposition is expressly supported by the case of *In re Hollanger*,[147] where a bankrutcy court exercised its "cram-down" powers under the new Bankruptcy Code to allow two farmer-debtors to restructure various mortgage debts secured by farm land over the dissents of various mortgage creditors.

In the *Hollanger* case, a farmer and his wholly-owned farming corporation, engaged in consolidated farm operations, filed for reorganizations. The court found that the value of the farms in question greatly exceeded the amount of the debts which were secured by the land. Further, the court found that the debtors' plans were feasible, since there was presented a seven-year analysis, including a budget and income projection, for the debtors' farming operations, all of which illustrated the debtors' ability to cultivate their farm land and satisfy their obligations. Therefore, the court confirmed the corresponding, compatible plans, both of which provided that the debtors would retain farm land and repay their debts from future earnings.

The most significant restructuring of the mortgage debt through the plans was to provide that all mortgage payments due and owing at both filing and confirmation would be deferred and extended for seven years, at which time they would "balloon" and become fully due and payable. Further, the plan provided that normal annual installments owed on mortgage debts secured by the farms, with the exception of arrearages, would be slightly reduced by approximately 15%, with the new payments to be made in the mid-spring of each subsequent year. This allowed the long-term mortgage debts on the farm land to be paid at a slightly reduced amortization, except for arrearages. Since a plan was confirmed in the middle of a crop season, the debtors were allowed to continue to cultivate and harvest their crops in order to produce sufficient monies to meet their new installments. Thus, the debtors gained an eighteen-month moratorium after filing. In addition, the

146. *See* authorities cited *supra* note 125.

147. 15 Bankr. 35, 8 BANKR. CT. DEC. (CRR) 365, 5 COLLIER BANKR. CAS. 2d 386 (W.D. La. 1981). The reader should be aware that these writers were counsel to the debtors in the *Hollanger* case; however, it is hoped that the objectivity of this analysis is not thereby impaired.

plans provided that any debts bearing installment repayment schedules of *less than* seven years would be restructured to be paid in equal annual installments over seven years. Therefore, the essence of the plans was (a) to allow the debtors a seven-year period of rehabilitation, (b) to relieve them from immediately pressing arrearages, and (c) to defer the due dates of various obligations which they owed as part of the rehabilitation program.

Following the logic of *In re Benson,*[148] the court held that the *Hollanger* plan provided creditors the indubitable equivalent of their claims within the meaning of *In re Mural Holding Corporation.*[149] Hence, the court found that the plans provided completely compensatory treatment for all creditors, coupled with adequate protection for their claims, which allowed the confirmation of the debtors' plans over the objections of various secured claimants.

An unreported case furnishes another illustration of the possible rehabilitative results under the new Bankruptcy Code. The case of *In re Upshaw*[150] established that if a farmer is unable to retain his land and use the earnings derived from it to pay creditors in the future, the court can allow the debtor to restructure the obligations secured by the farm in the manner most likely to produce the greatest sale price. The debtor's plan in *Upshaw* provided a format similar to that in *Hollanger*. The major asset was a farm embracing approximately 217 acres, valued at approximately $450,000, which secured a first mortgage debt to a life insurance company in the approximate amount of $225,000 and a second mortgage debt in favor of the Farmer's Home Administration (FmHA) in the approximate of $155,000, which totaled approximately $380,000. The court found that the value of the farm exceeded the amount of these debts and furnished an "equity cushion" for the satisfaction of these claims.

The plan provided that the present annual payments and arrearages on these two secured claims would be deferred and "balloon" approximately three years after confirmation. The deferring of arrearages was similar to the restructuring provided under the *Hollanger* case.[151] The plan was one of orderly liquidation and provided that the two secured claims would be reduced to *in rem* basis

148. 9 Bankr. 854 (N.D. Ill. 1981).

149. 75 F.2d 941 (2d Cir. 1935).

150. *In re* Upshaw, No. 580-01026-M (Bankr. W.D. La. Aug. 11, 1981). The reader should be aware that the authors were counsel to the debtors in the *Upshaw* case.

151. *See supra* notes 147-49.

and the property would be sold subject to these two secured claims, as restructured.[152] Under this liquidation plan a new purchaser could buy the property subject to the *in rem* indebtedness and have approximately one year before being required to make mortgage payments. Therefore, the restructuring of the debt would allow the purchaser to have some "breathing room" within which to make annual payments after purchase, and the purchaser would not have to assume and become personally liable for the underlying mortgage debts. These two favorable factors were found to enhance the debtor's ability to receive the highest possible price for his farm land thereby receiving the greatest possible recovery of equity in the land for himself and his creditors.

Another unreported case furnishes an illustration of the restructuring on the farm land to enhance the farmer's ability to continue farming operations, refinance this land, or sell his farm. In the case of *In re Adcock*,[153] a father and two sons owned approximately 718 acres of farm land valued at approximately $1,250,000. The debtors had engaged in farming operations for several years. Because of continued losses and borrowings to meet working capital needs, the debtors had placed the following liens upon their property and farming equipment:

1. First Mortgage — insurance company	$ 419,000
2. Second Mortgage — FmHA	480,000
3. Third Mortgage — local bank	140,000
4. Fourth Mortgage — FmHA	280,000
	$ 1,319,000

The total debt encumbering the land was approximately $1,319,000. The debts of the local bank and the FmHA were also secured in various ranks and priorities against farm equipment. Finally, the bank held mortgages on personal collateral belonging to the debtors.

The farmer-debtors' particular problem in this case was that they had more than enough collateral to secure their creditors, but

152. The reduction of the mortgages debts to an *in rem* basis is consistent with the personal discharge from indebtedness granted to the Chapter 11 debtor upon confirmation. *See* 11 U.S.C. § 1141 (Supp. IV 1980).

153. *In re* Adcock, No. 581-00577-M (Bankr. W.D. La. Dec. 28, 1981). The authors were counsel to the debtors in the *Adcock* case.

the collateral was intermingled and interwoven between junior and senior liens in favor of the bank and the FmHA to such a degree that it was impossible to determine what collateral position was enjoyed by each secured lender. The FmHA was reluctant to agree or consent to any restructuring of their obligations.

The plan of reorganization proposed a substitution and exchange of the collateral held by the FmHA secured by equipment (of approximately $50,000) for the collateral of the bank which was secured by its third lien position (and in front of the FmHA's fourth lien position) on the farm of approximately $140,000. The debtor's plan essentially proposed to erase the FmHA's lien on its movable collateral and to erase the bank's lien on the farm land. Thus, the plan proposed to relegate the farm to the FmHA for satisfaction of its entire lien, since its enhanced collateral position of approximately $140,000 against the farm exceeded the collateral position of approximately $50,000 given up against the farm equipment. Conversely, the plan sought to move the lien of the bank from the farm so that it would only be secured by farm equipment and other personal property of the debtors. The bank finally consented to the plan but the FmHA voiced objection.

The court confirmed the plan based on the following logic. First, sections 361 and 1129(b)(2)(A)[154] envision that a secured creditor should have its collateral position protected throughout the proceeding for the value of the collateral; so long as this protection was provided, together with completely compensatory satisfaction of the secured creditor's claim, the creditor was being statutorily protected. It had no constitutional right to more than it was receiving. Under the *Adcock* plan, the FmHA was being adequately protected in the exchange of collateral position with the bank.

Second, the quality of the collateral given to the FmHA under the plan was superior to that which it was forced to release. Its lien position against the farm was increased by the deletion of the third mortgage in favor of the bank, which was superior to the FmHA's fourth mortgage position, and the FmHA was releasing its lien on equipment. The court found that the equipment was subject to deterioration and depreciation, whereas the farm would probably appreciate in value. Thus, both the quality of the new lien position on the farm given to the FmHA under the plan as well as the

154. 11 U.S.C. §§ 362, 1129(b)(2)(A) (Supp. IV 1980).

quantity (i.e., the value of collateral given up versus value of collateral received) were enhanced.

Third, the plan achieved a reasonable compromise which would prevent expensive and time-consuming litigation between the bank and the FmHA regarding their respective ranks and lien positions on the various items of chattels. This compromise fostered confirmation of a plan providing rehabilitation for the debtor and more complete recovery for all creditors.

Fourth and finally, the compromise allowed the debtors to have certain collateral released to them to be liquidated. The proceeds from the liquidation furnished them with working capital needed for future farming operations.

C. Practical Suggestions To Aid Farmer Relief

There are two practical suggestions that may aid in a farmer's rehabilitation. First, the continued use of the proceeds from a farmer's crop may form the nucleus to finance future farming operations. Parenthetically, if farmers are going to plant and cultivate their crops in the spring and summer of a year, they will first obtain a loan from an agricultural lender secured by the crop to be grown and its proceeds. The proceeds of this loan (commonly known as a "crop loan") will provide the monies with which to plant, cultivate, and harvest a crop. After the harvesting of a crop, the crop loan may be repayed from the proceeds derived from its sale.

In many instances, farmers will file for reorganizations in the middle of a crop year (i.e., prior to the harvest and sale of their crops). If this occurs, there will usually be no prospect for financing to plant, cultivate, and harvest crops in the future. The reorganization will have a "chilling effect" on any new lender advancing monies to produce crops. Therefore, the only available "financing" for a crop loan may be for the farmer to retain the proceeds derived from his present crops after they are sold and to use these to finance future farming operations, which will have the necessary result of not paying all of the proceeds to the existing crop lender. Thus, the crop lender will be forced to retain a "revolving" lien on any crops produced in future years until paid in full.

Adequate provision can be made to protect the crop lender by placing the proceeds derived from the crop in some form of supervised account and ensuring that the use of the proceeds from the account will be directly applied to the production of crops in future years. Therefore, the "adequate protection" mandated by section 361 for the existing crop lender will be the continued tracing of a crop lien to the proceeds, product, offspring, profits, etc., of the present collateral (crop).[155] The proceeds derived from the crop will be, in effect, old collateral in a new form. The plan can provide that the secured crop lender will be able to follow his collateral proceeds indefinitely from liquid funds to a tangible crop, to the harvested crop, to the proceeds derived from the crop and so on.[156]

One key to farmer rehabilitations may be the requirement that present crop lenders be required to allow the farmer to use these proceeds to produce crops in future years and be allowed to continue to trace the collateral through its various forms of crop production and proceeds until this creditor is fully paid. If additional or replacement security can be given such a creditor under section 361, this would further be advisable.[157]

A second practical suggestion for farmer rehabilitations is derived from the premise that, if encumbrances on a farm exceed the farm's fair market value, the farmer should be allowed to redeem and buy back his farm over a reasonable period for the fair market value of the farm, as appraised, if at all possible. Under the old Act, the cases allowed farmer-debtors to repay their creditors over a protracted period of time for the full amount of the debt.[158] Furthermore, if the full amount of the debts secured by the farm exceeded its fair market value, debtors were allowed to appraise their property and "cash out" their secured creditors under both Chapter XII of the old Act[159] and under section 75.[160] For example, in the case of *In re KRO Associates*,[161] a Chapter XII debtor was al-

155. *See generally* Coogan, *The New Bankruptcy Code: The Death of Security Interest?* 14 GA. L. REV. 153 (1980); Orr & Klee, *Secured Creditors Under the New Bankruptcy Code*, 11 U.C.C. L.J. 312 (1979).

156. *See* the authorities cited *supra* note 155. Essentially, the debtor may propose that the crop proceeds and new crop(s) grown subsequently will constitute collateral upon which the secured crop lender may be given a "replacement lien." *See* 11 U.S.C. § 361(a) (Supp. IV 1980).

157. 11 U.S.C. § 361(a) (Supp. IV 1980).

158. *See supra* notes 38-96, 137-39 and accompanying text.

159. *See supra* notes 108-19 and accompanying text.

160. *See supra* notes 38-96 and accompanying text.

161. 4 BANKR. CT. DEC. (CRR) 462 (S.D.N.Y. 1978). The holding of *KRO* was conditioned upon the debtor's amending its plan to provide some covenant or guaranty evincing a willingness to fulfill the repayment proposal contained in the debtor's plan. *See supra* note

lowed to "scale down" the first mortgage indebtedness on an office building to the value of the underlying building, retain the building, and pay off the reduced first mortgage debt over an extended period of years.[162]

In applying these concepts to the new Code, it does appear that debtors are inhibited in appraising their farm land and "cashing out" the underlying mortgage holders through sales or refinancing very shortly after confirmation.[163] The policy of the Code appears to restrict this practice, since it might result in a windfall in favor of the farmer-debtor in the event the property values appreciate rapidly after confirmation.[164]

Conversely, if the farmer-debtor desires to retain his land and repay it over a protracted period of time, he need only pay the fair market value of the property as defined under section 506(a) of the Code.[165] The basic premise here is that, regardless of whether a creditor makes an election to be fully secured for the entire amount of his debt pursuant to section 1111(b), he is only entitled to receive future payments having a present value equal to the un-

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138 and accompanying text.

162. See also the authorities cited at *supra* notes 38-96 regarding cases under § 75 of the old Act. The result should have been the same if a farm was involved rather than an office building.

163. *See* Klee, *supra* notes 125 & 132 and accompanying text.

164. *See* the authorities cited *supra* note 125.

165. 11 U.S.C. §§ 361(3), 506(a) (Supp. IV 1980). When read together, §§ 506 and 361 operate to reinforce the existing long-standing "rule to the effect that valueless junior secured positions or unsecured deficiency claims will not be entitled to adequate protection." 2 W. Collier, Collier on Bankruptcy ¶¶ 361-01 to -13 (15th ed. 1981); the reader should note that this treatise is the fifteenth edition and discusses bankruptcy law under the new Code; a discussion of the old Act is contained in the fourteenth edition, which is cited *supra* note 17. *See also* the authorities cited *supra* note 155.

> The evidence before the District Court is not presented by the record. And as the Court of Appeals, if the appeal had been allowed, could have revised the ruling of the court below only in matter of law, it necessarily follows—and was conceded at the bar—that petitioners are bound by the findings of fact. Petitioners insist that their consent to the plan of reorganization was necessary or that their claims should have been accorded "adequate protection." But the adequate protection to which the statute refers is "for the realization of the value of the interests, claims or liens" affected. Here the controlling finding is not only that there was no equity in the property above the first mortgage but that petitioners' claims were appraised by the court as having "no value." There was no value to be protected. This finding embraces whatever interests petitioners may have as junior lienors under the Illinois law and, in the same aspect, the constitutional argument is unavailing as petitioners have not shown injury.

In re 620 Church St. Bldg. Corp., 299 U.S. 24, 27 (1936).

derlying collateral, rather than the amount of the mortgage debt.[166] In other words, the debtor should not be required to pay more than the fair market value of his collateral (presumably his farm) in order to retain it and give mortgage holders secured by it fair and equitable treatment.

The normal problem with this approach is that the undersecured creditors on the farm will have an unsecured status for the undersecured portion of their claims, and they may object to a plan allowing a farmer's retention of his farm. For purposes of illustration, the following hypothetical example will suffice.[167] Assume the debtor owns a farm worth $1,200,000 which is subject to the following encumbrances:

1.	First Mortgage	$ 700,000
2.	Second Mortgage	900,000
3.	Third Mortgage	210,000
		$ 1,810,000

Assume further that the debtor proposes to keep his farm and pay its fair market value ($1,200,000) over ten years. Then, assume that each lienor is a separate class of creditors under the plan, that the first lienor accepts the plan, and that the junior two classes vote against the plan. Can the court confirm the plan and allow the farmer to retain it by paying its fair market value?

Properly posed, the question is whether section 1129(b)(2)(B)[168] will operate to preclude a farmer retaining, redeeming, or purchasing his farm under an ongoing or a liquidating plan of reorganization in the event that undersecured lienors value their collateral, are declared unsecured creditors, and (as unsecured creditors) vote against the plan. A facial reading of the Code indicates that, if an unsecured class of creditors does not vote for the farmer-debtor's plan (which may include the undersecured portion of the second and third mortgages encumbering the debtor's farm under the above hypothetical example), one may argue that he may not be able to "cram down" the plan on any dissenting classes and keep his farm. The Code appears to state that all nonconsent-

166. 11 U.S.C. § 1129(b)(2)(A) (Supp. IV 1980).

167. This hypothetical example is extracted from Anderson, *supra* note 115, which advanced a proposition similar to the one in the text accompanying this footnote.

168. 11 U.S.C. § 1129(b)(2)(B) (Supp. IV 1980).

ing unsecured classes should be fully satisfied (i.e., receive or retain property equal to their claims) before the debtor may receive any benefits.[169] A facial reading of the Code appears to mandate that the holders of junior claims or interests (e.g., the farmer-debtor) to any dissenting class "will not receive or retain on account of such junior claim or interest any property."[170] This is a modification of the Rule of Absolute Priority developed under prior reorganization law, which required that each superior class receive completely compensatory treatment before the next descending class may receive any benefits under a reorganization plan.[171]

Since the second mortgage debt exceeds the value of the farm by $400,000, and since there is no equity or value in the farm for the third mortgage debt, the farmer-debtor will have one secured claim for $700,000; one partially unsecured claim totalling $900,000 (of which $400,000 is the undersecured portion of the second mortgage claim and of which $500,000 is the fully secured portion of the second mortgage claim);[172] and one completely undersecured claim in the amount of $200,000. Thus, unless the second mortgage holder elects under section 1111(b) to have all of his debt treated as fully secured, the unsecured claims will be $610,000.[173] Therefore, if the farmer-debtor proposes to buy back his farm in the amount of $1,200,000 (which is its appraised fair market value) over a period of time and with an appropriate discount or interest rate, the question is whether such a plan can be confirmed if the unsecured creditors created by the undersecured mortgages vote against such a plan, and block the farmer-debtor from repurchasing his farm under an ongoing or a liquidating plan of reorganization.

There is an absence of commentary arguing that this may be an appropriate result under the new Code.[174] However, the traditional right of the farmer to repurchase his farm at fair market

169. *See id.*
170. *Id.*
171. The main precepts of the Rule of Absolute Priority are contained in various Supreme Court decisions. Reconstruction Finance Corp. v. Denver & R.G.W.R., 328 U.S. 495 (1946); Group of Inst. Investors v. Milwaukee R., 318 U.S. 523 (1943); Consolidated Rock Prods. Co. v. DuBois, 312 U.S. 510 (1941); Case v. Los Angeles Lumber Prods. Co., 308 U.S. 106 (1939); for an expanded discussion see Blum, *supra* note 15; and for a discussion of how the Rule of Absolute Priority has been modified under the new Code, *see* Klee, *supra* note 125.
172. *Accord* Klee, *supra* note 125, at 150-56.
173. *Id.*
174. *Cf.* the authorities cited *supra* note 171.

value appears to be one which is presumably necessary for a reorganization of his finances.[175] Furthermore, one might argue that this plan is simply one of liquidation and that the farmer should not be denied his exclusive right to repurchase his own farm land for its fair market value.

Conversely, creditors will argue that, to the extent the debtor is given the exclusive right of redemption or purchase, they are being denied the right to potential full recovery and that the farmer-debtor is obtaining the possibility of a windfall in the event of significant appreciation in the value of the farm after confirmation. Naturally, the farmer-debtor can reply that any appreciation in value will be more probably caused by his work efforts, rather than the economic climate. Furthermore, unless the mortgage holders involved are prepared to farm the property and produce crops, the nation's economy may suffer unless the farmer-debtor retains his farm and continues to produce commodities.

CONCLUSION

These writers cannot clearly state the rule(s) that may result under the new Code. However, it is our view that the full policy of debtor relief in terms of farmer rehabilitation must favor the farmer's retention of his property (by paying its fair market value) and continuation of crop production on the land. The decisions regarding this issue will be made, in all probability, on a case-by-case basis under the new Bankruptcy Code.

It is hoped that this article will have given the reader some insight into the problems of farmers and the means provided through reorganization proceedings to aid in their financial amelioration. It has not been intended to give every possible means by which farmers may be assisted in reorganization proceedings. Only extensive experience and in-depth study will make the reader fully aware of all the nuances of the debtor relief provisions of the new Bankruptcy Code, especially as they relate to farmers. What has been given, rather, is a review of the usual and basic rehabilitative schemes envisioned by the Bankruptcy Code. With a basic understanding of reorganizations available to farmers under the new Code, counselors may be better able to advise their clients as to what may be expected when they attempt to reorganize.

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175. *See* authorities cited *supra* notes 38-96 and accompanying text.