

# *Top 10 Things You Need to Know About Ag Bankruptcy*

*By: Stephen L. Gershner*

## **1. Types of relief available**

**Chapter 7** — Straight bankruptcy. Individuals and entities are eligible to be debtors. Debtor files a petition, listing assets and debts. Upon filing the petition, an estate is created. A Trustee is appointed as representative of the estate. The Trustee is charged with liquidating non-exempt assets and distributing proceeds to creditors. Discharge of indebtedness is granted to individuals on most debts unless an objection to discharge or dischargeability is sustained. Corporations do not get Chapter 7 discharge.

**Chapter 11** — Reorganization. Originally designed for entities, however, individuals are also eligible for Chapter 11 relief. As with Chapter 7, an estate is created upon filing a petition. Upon filing a Chapter 11 petition, the debtor becomes the debtor-in-possession and exercises most of the rights and duties as a Trustee. The debtor-in-possession operates the debtor's business and files a plan of reorganization and disclosure statement, which is voted on by creditors. Individuals get discharged upon confirmation of the plan. Confirmation of the plan creates a new contract between debtor and creditor.

**Chapter 12** — Reorganization for family farmers (and fishermen). Chapter 12 was created by Congress in 1985. Individuals and entities are eligible. Family farmers must have no more than \$4,153,150 in total indebtedness, at least 50 percent of debt must be derived from farming and 50 percent of gross income must be derived from farming. Partnerships and corporations are eligible to be debtors if a single farmer owns more than half of the equity in the entity. A Chapter

12 Trustee is appointed upon filing and is a party in interest. The debtor operates the business and proposes a plan for payment of creditors.

**Chapter 13** – Reorganization for individuals with regular sources of income. Chapter 13 is not designed for farmers, but its provisions have similarities. Chapter 13 relief is only available for debtors having non-contingent liquidated unsecured debts of less than \$384,725 and non-contingent, liquidated secured debt of less than \$1,184,200. The regular income requirements and debt limitations of Chapter 13 are not generally suited for Ag reorganizations.

**2. Ag reorganization can be expensive and difficult.**

Commodity prices, fuel, weather, disease, and input costs can vary significantly from year to year. Distressed farmers may have difficulty obtaining production loans and those that do often encounter significantly higher borrowing costs. Row crop operations frequently operate through multiple entities, which complicates and adds to the expense of reorganization attempts.

Chapter 12 was implemented by congress as a reorganization proceeding for family farmers and fisherman but is seldom used. Family farmers often have multiple entitles with cross collateralization and cross default provisions. These types of operations may require multiple filings to protect assets necessary for an effective reorganization. To qualify for Chapter 12, the debtor must be a family farmer. A family farmer is defined as having aggregate debt that does not exceed \$4,153,150. This debt limitation eliminates many distressed farming operations from Chapter 12 relief.

Chapter 11 was intended for reorganization of business entities, but individuals are eligible to be debtors in Chapter 11 cases. The 1984 Amendments to the bankruptcy code added §707(b), which authorized the court to dismiss cases filed by individuals under Chapter 7 or convert the case to Chapter 13, if the debts were primarily consumer debts and if the debtor had disposable

income. In 2005, the bankruptcy code was amended to address concerns of the consumer credit lobby. The 2005 amendments contain provisions which make confirmation of Chapter 11 plans of individual debtors very difficult. Individuals as principals or guarantors are debtors in the great majority of farming operations.

### **3. Chapter 12 Overview.**

Very few Chapter 12 cases have been filed. In large part, this is due to the debt limitations. Debt limitations affect eligibility and indirectly affect feasibility. In many instances, distressed farming operations of that size will have debt in excess of the maximum permitted for a Chapter 12 debtor. Attached is a Farm Bureau article reporting a small number of Chapter 12 filings per state and nationwide since 2009.

#### **a. Eligibility**

11 USC 109(f) Must be family farmer or fisherman.

11 USC 101(18) (A) “family farmer”

The individual or husband and wife must be engaged in a farming operation whose aggregate must not exceed \$4,153,150.

Senate Bill S.897, introduced March 27, 2019 and referred to the Judiciary Committee, seeks to amend §101(18) to increase the debt limitation on Chapter 12 eligibility to \$10,000,000.

At least 50%, of the aggregate non-contingent liquidated debts (exclusive of debt for the debtor's principal residence) must be related to the farming operation owned by the individual and spouse on the date of filing.

More than 50% of the gross income of the individual and spouse for the preceding tax year or, for family farmers only, for each of the 2nd and 3rd prior tax years must have come from the farming operation, or

11 USC 101(18) (B)

A corporation or partnership in which more than 50% of the outstanding stock or equity in the corporation or partnership must be owned by one family or by one family and its relatives. The family or the family and its relatives must conduct the farming operation.

More than 80% of the value of the corporate or partnership assets must be related to the farming or fishing operation.

The total indebtedness of the corporation or partnership must not exceed \$4,153,150 and not less than 50% for a farming operation of the corporation's or partnership's total debts, which are fixed in amount (exclusive of debt for one home occupied by a shareholder or partner as principal residence), must be related to the farming operation.

If the corporation issues stock, the stock cannot be publicly traded.

11 USC 109 (f) Only a family farmer with a regular annual income may be a debtor under Chapter 12.

11 USC 101(19) a family farmer with regular annual income means a family farmer whose income is sufficiently stable and regular to enable the family farmer to make payment under a Chapter 12 plan.

11 USC 1203 gives the debtor-in-possession all the rights of a Trustee except for right of compensation and requires that the debtor-in-possession perform all duties of a Chapter 11 Trustee except for duty to investigate the debtor and report on the investigation.

The primary power of the Chapter 12 debtor-in-possession is operating the debtor's business.

b. Sec. 1222 – Plan Requirements

(a) The plan shall:

- (1) provide for submission of all of such portion of future earnings or income of debtor the supervision or control of the Trustee.
- (2) provide for full payment of sec. 507 priority claims, unless holder agrees otherwise.
- (3) if plan classifies claims or interests treat each holder of claims within a class the same way.
- (4) may pay sec. 507(a)(1)(B) priority (domestic) claims less than in full only if all disposable income for 5 years will be applied to make plan payments
- (5) treat tax claims arising from pre or post-petition disposition of assets used in farming as unsecured claims.
- (6) may not provide for payments over more than three years unless the court approves up to five (maximum).

(b) Subject to subsections (a) and (c) of this section, the plan may –

- (1) designate a class or classes of unsecured claims, of this title, but may not discriminate unfairly against any class so designated; however, such plan may treat claims for a consumer debt of the debtor if an individual is liable on such consumer debt with the debtor differently than other unsecured claims;
- (2) modify the rights of holders of secured claims, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims;
- (3) provide for the curing or waiving of any default;
- (4) provide for payments on any unsecured claim to be made concurrently with payments on any secured claim or any other unsecured claim;
- (5) provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due;
- (6) subject to section 365 of this title, provide for the assumption, rejection, or assignment of any executory contract or unexpired lease of the debtor not previously rejected under such section;

- (7) provide for the payment of all or part of a claim against the debtor from property of the estate or property of the debtor;
  - (8) provide for the sale of all or any part of the property of the estate or the distribution of all or any part of the property of the estate among those having an interest in such property;
  - (9) provide for payment of allowed secured claims consistent with section 1225(a)(5) of this title, over a period exceeding the period permitted under section 1222(c) ;
  - (10) provide for the vesting of property of the estate, on confirmation of the plan or at a later time, in the debtor or in any other entity;
  - (11) provide for the payment of interest accruing after the date of the filing of the petition on unsecured claims that are nondischargeable under section 1228(a) , except that such interest may be paid only to the extent that the debtor has disposable income available to pay such interest after making provision for full payment of all allowed claims; and,
  - (12) include any other appropriate provision not inconsistent with this title.
- (c) Except as provided in subsections (b)(5) and (b)(9), the plan may not provide for payments over a period that is longer than three years unless the court for cause approves a longer period, but the court may not approve a period that is longer than five years.
  - (d) Notwithstanding subsection (b)(2) of this section and sections 506(b) and 1225(a)(5) of this title, if it is proposed in a plan to cure a default, the amount necessary to cure the default, shall be determined in accordance with the underlying agreement and applicable nonbankruptcy law.

c. Sec. 1225 - Confirmation of plan.

- (a) Except as provided in subsection (b), the court shall confirm a plan if-
  - 1. the plan complies with Ch. 12 and other applicable title 11 provisions;
  - 2. all required fees have been paid;
  - 3. the plan is filed in good faith and not by means forbidden by law;
  - 4. the value of property distributed to unsecured creditors is not less the amount would be paid if debtor were liquidated under chapter 7;

5. With respect to each allowed secured claim provided for by the plan.
  - A. the holder has accepted the plan;
  - B. The holder of such claim retains its lien and is paid the value of the allowed secured claim; or
  - C. the debtor may surrender the property.
6. the debtor will be able to make app plan payments and comply with the plan;
7. the debtor has paid all domestic support obligations that became due after the petition was filed.

(b)

- (1) If the Trustee or an unsecured creditor objects to confirmation, the court may not approve the plan unless, as of the effective unless;
  - (A) the value of the property to be distributed under the plan on account of such claim is not less than the amount of such claim;
  - (B) the plan provides that all of the debtor's projected disposable income to be received in the three-year period, or such longer period as the court may approve under section 1222(c), beginning on the date that the first payment is due under the plan will be applied to make payments under the plan; or
  - (C) the value of the property to be distributed under the plan in the 3-year period, or such longer period as the court may approve under section 1222(c), beginning on the date that the first distribution is due under the plan is not less than the debtor's projected disposable income for such period.
- (2) For purposes of this subsection, "disposable income" means income which is received by the debtor and which is not reasonably necessary to be expended—
  - (A) for the maintenance or support of the debtor or a dependent of the debtor or for a domestic support obligation that first becomes payable after the date of the filing of the petition; or for the payment of expenditures necessary for the continuation, preservation, and operation of the debtor's business.

- (B) Maintenance and support of the debtor or a dependent of the debtor and domestic support obligations. Continuation, preservation and operation of the debtor's business.

The bankruptcy estate of individuals in Chapter 12 is not a separate taxable entity. In 2017, section 1232 was enacted and states:

In Chapter 12, unsecured claim of governmental unit against the debtor or the estate that arises before or after the filing of bankruptcy petition but before the debtor's discharge under section 1228, as a result of the sale, transfer, exchange or other disposition of any property used in the debtor's farming operation –

- (1) Shall be treated as an unsecured claim arising before the date on which the petition is filed.
- (2) Shall not be entitled to priority under section 507;
- (3) Shall be provided for under a plan; and
- (4) Shall be discharged in accordance with Section 1228.

#### **4. Chapter 11 issues.**

Chapter 11 is a reorganization proceeding designed for businesses. However, individuals are eligible to be debtors in Chapter 11 cases. Chapter 11 has provisions similar to those of Chapter 12, but the requirements to confirm a Chapter 11 plan are much more difficult. In a Chapter 11 plan, claims are classified and there is a hierarchy of creditor rights. Secured creditors are at the top of the hierarchy, followed by priority claim holders, then unsecured creditors. Equity holders or individual debtors are referred to as the class of interest and are at the bottom of the hierarchy.

To confirm a Chapter 11 plan, creditors vote by class. A class accepts the plan if more than two-thirds in amount and more than 50% in number of claims that vote accept the plan. See Sec. 1126(c).

A class of interests accepts a plan upon the vote of at least two-thirds of allowed amount of interest accepting the plan. See Sec. 1126(d).



To confirm a plan under Sec. 1129(a), all classes which vote must either accept the plan or the plan must provide that the rejecting class receive as much as it would receive if paid in a case under Chapter 7.

In Chapter 11, secured creditors are entitled to the value of their collateral. Remaining property of the bankruptcy estate is paid first to expense of administration and thereafter to unsecured creditors. Section 507 establishes priorities for various types of unsecured claims. The debtor in individual cases or equity holder in corporate cases are lower in priority than all classes of claims.

A concept known as the absolute priority rule arose from case law in the early 1900's. The absolute priority rule was codified in the 1978 code with section 1129(b) which allows the bankruptcy court to confirm a plan over a rejecting class if the plan is fair and equitable with respect to each class which has not accepted the plan. The absolute priority rule requires that for a plan to be fair and equitable a class that is junior to a rejecting class receive nothing under the plan if a senior rejecting class is not paid in full.

Section 541(a)(6) excludes from property of the estate, earnings from services performed by an individual after commencement of the case. Section 1306 of the bankruptcy code includes a debtor's post-petition earnings as property of the bankruptcy estate in Chapter 13 cases. However, the debt limitation for eligibility to be a Chapter 13 debtor is \$394,725 in unsecured and \$1,184,200 in secured debt. Section 707(b) of the bankruptcy code provides for dismissal of Chapter 7 cases of debtors hold primarily consumer debt the debtor converts to Chapter 11 or 13. Prior to the 2005 amendments a debtor with consumer debts in exceeding Chapter 13 eligibility could liquidate in a Chapter 11 case and their post-petition earnings would not be property of the estate or subject to creditor claims. The 2005 amendments added section 1115, which makes an

individual debtor's post-petition earnings property of the Chapter 11 estate to make individual Chapter 11 cases more like Chapter 13. However, while Chapter 13 does not have an absolute priority rule the 2005 amendments did not address the absolute priority rule in Chapter 11 cases.

One of the means of overcoming the absolute priority rule in Chapter 11 has been the *new value* exception, in which the debtor made a substantial contribution to the reorganized debtor to retain ownership of the debtor to retain his equity or ownership interest, The 2005 amendments making an individual Chapter 11 debtor's post-petition earnings property of the estate, makes it extremely difficult for a debtor to contribute new value in exchange to retain his interest in the reorganized debtor.

Following the 2005 amendments there was a great deal of writing about whether the absolute priority rule still applied in individual Chapter 11 cases. All of the circuit courts which have addressed the issue hold that the absolute priority rule continues to apply in individual Chapter 11 cases. See *Maharaj v. Stubbs & Purdue*, 681 F. 2d 588 (4<sup>th</sup> Cir. 2012); *In re Lively*, 717 F, 3d 406 (5<sup>th</sup> Cir. 2013); *Ice House America LLC. v. Cardin* 751 F.3d 734 (6<sup>th</sup> Cir. 2014); *Zachary v. California Bank & Trust*, 811 F,3d 1191(9<sup>th</sup> Cir. 2016); *Dill Oil Co. LLC v. Stephens (In re Stephens)* 704 F. 3d 1279 (10<sup>th</sup> Cir. 2013).

In the 8<sup>th</sup> Circuit, there is no binding precedent on the status of the absolute priority rule in individual Chapter 11 cases. *In re Tegeder*, 390 B.R. 477 (Bankr. D. Neb. 2007) and *In re O'Neal* 490 B.R. 276 (Bankr. W.D. Ark. 2013) hold that the absolute priority rule no longer applies in individual Chapter 11 cases. But, *In re Woodward*, 537 B.R. 894 (B.A.P. 8th Cir. 2015) holds that the absolute priority rule still applies.

The absolute priority rule makes Chapter 11 is much less attractive as a vehicle for farm reorganization.

The bankruptcy estate in a Chapter 11 case is a separate taxable entity.

## **5. Multiple Entities.**

Section 327 of the bankruptcy code authorized employment of attorneys and other professionals who do not hold an interest adverse to the debtor or the estate.

Farming operations frequently are conducted through multiple affiliated entities which may bring about a need for multiple filings. The existence of multiple entities may result in a need for multiple bankruptcy filings, which could result in the need for separate counsel.

Bankruptcy Rule 1015 authorizes joint administration of multiple cases by or against (1) spouses, (2) a partnership and one or more of its general partners or (3) a debtor and an affiliate.

Joint administration is procedural only, each debtor has its own property and creditors.

Substantive consolidation may be appropriate upon consideration of (1) the necessity of consolidation due to the interrelation of the debtors, (2) the benefits of consolidation outweigh the harm to creditors; and (3) the prejudice that may result from not consolidating the debtors. *In re Giller*, 962, F.2d 796 (8<sup>th</sup> Cir, 1992).

Substantive consolidation is rooted in case law and the court's equitable powers under Section 105 of the Bankruptcy Code. *In re Reider*, 31 F.3d 1102, 1105 (11th Cir. 1994).

Joint administration generally occurs in larger corporate cases and substantive consolidation is rare.

## **6. Debtor's Conduct**

Prepetition conduct and transactions of the debtor can seriously affect the ability of the debtor to reorganize or get a discharge.

Prepetition transfers may be voidable as preferences pursuant to section 547 or fraudulent transfers pursuant to section 548.

Section 727 allows prepetition transfers within one year of filing bankruptcy petition with intent to hinder, delay or defraud a creditor to result in discharge being denied.

Section 1104 applies in Chapter 11 cases and states cause for appointment of a trustee includes fraud, dishonesty, incompetence, and gross mismanagement the affairs of the debtor by current management.

Section 1204 provides for removal of the debtor as debtor-in-possession for cause including fraud, dishonesty, incompetence, and gross mismanagement the affairs of the debtor by current management.

## **7. Financing Chapter 11 and Chapter 12 Cases.**

Operating a farm requires a great deal of cash. Even more is required to operate in a Chapter 11 or Chapter 12 case. Substantial fees are likely to be incurred with attorneys, accounts, appraiser, realtors etc. Attorneys and accounts generally require a substantial retainer.

Funding farming operations normally accomplished through a combination of existing financing on land and equipment and annual operating loans. A non-liquidating Chapter 11 or Chapter 12 case is unlikely to go very far without an operating lender. Operating loans are generally going to require some equity in real or personal property.

Common sources of financing are:

Banks

Farm lenders such as FSA 90/10 guaranty

Purchases on account from suppliers

Use of cash collateral

## 8. The Automatic Stay

The automatic stay of section 362 arising upon the filing of a bankruptcy petition. The automatic stay is very broad and generally stays the commencement and continuation of actions against the debtor or its property.

Co-debtor stay only applies to co-debtors on consumer debts in Chapter 12 and 13. See 11 USC 1201(a) and 1301(a).

Relief from co-debtor stay will be granted to creditor to the extent the non-debtor received the consideration for the creditor's claim; the debtors plan proposes not to pay the claim, or the creditor will be irreparably harmed if the stay is not lifted. 11 U.S.C. 1201(c), 1301(c).

Farming enterprises frequently involve multiple entities. Individuals, general partnership, limited liability company or corporation.

Non-debtors generally not protected by the automatic stay:

To extend the stay to non-debtor must show harm to debtor. Affecting value or debtor's property is not sufficient to extend the stay to a non-debtor. *National Bank of Arkansas v. Panther Mountain Land Development*, 686 F 3d 916 (8<sup>th</sup> Cir. 2012).

In rare circumstances, the stay may be extended to protect non-debtors through use of courts equitable powers under section 105 of the bankruptcy code. Use of equitable powers to extend the stay to protect non-debtor requires adversary proceeding and is analogous to seeking injunctive relief. *Id.*

However, a possessory interest in real property is protected by the automatic stay. See *In re 48th Street Steakhouse, Inc.* 835 F.2d 427, 430 (2d Cir. 1987). Restaurant leased to tenant who subleased property. Tenant/sublessor defaults. Subtenant filed Chapter 11. Sub-lease property of estate. Automatic stay barred termination of defaulted lease.

## 9. Adequate protection.

The bankruptcy code authorizes adequate protection for interests of entities in property in certain circumstances. Adequate protection in cases other than Chapter 12 is pursuant to section 361. Adequate protection in chapter 12 is pursuant to section 1205.

Adequate protection is designed to protect the interest of secured creditor or co-owner from loss. *U.S. v. Whiting Pools, Inc.* 462 U.S. 198, (1983); *U.S. Savings Association v. Timbers of Inwood Forest Assoc. Ltd.* 484 U.S. 65 (1988).

### a. §361 Adequate protection

When adequate protection is required under section 362, 363, or 364 of this title of an interest of an entity in property, such adequate protection may be provided by —

(1) requiring the trustee to make a cash payment or periodic cash payments to such entity, to the extent that the stay under section 362 of this title, use, sale, or lease under section 363 of this title, or any grant of a lien under section 364 of this title results in a decrease in the value of such entity's interest in such property;

(2) providing to such entity an additional or replacement lien to the extent that such stay, use, sale, lease, or grant results in a decrease in the value of such entity's interest in such property; or

(3) granting such other relief, other than entitling such entity to compensation allowable under section 503(b)(1) of this title as an administrative expense, as will result in the realization by such entity of the indubitable equivalent of such entity's interest in such property.

Adequate protection in Chapter 12 cases is through Section 1205.

Section 1205 contains all of the provisions of section 361 but also states that adequate protection can be provided by “paying to such entity for the use of farmland the reasonable rent customary in the community where the property is located, based upon the rental value, net income, and earning capacity of the property.”

Lack of adequate protection is grounds for relief from the automatic stay of section 362.

The sale, use or lease of property of the estate pursuant to section 363 will be denied if a objecting secured party or co-owner lacks adequate protection.

A section 364(d) post-petition loan secured by a senior lien on encumbered property may be approved if the primed lien holder is granted adequate protection.

Adequate protection is most commonly granted for protection from loss arising from interest accruals, depreciation, depletion, and market forces. Common means of providing adequate protection include, equity cushion (amount varies depending on facts but generally expect 20% or greater). periodic payments, replacement lien on other property of estate, lien on property not belonging to estate, non-debtor guaranty.

#### **10. Executory Contracts and Leases**

Executory contracts and leases governed by section 365 of the bankruptcy code. Land and equipment leases are common in farm operations. A trustee in a Chapter 7 case and a debtor-in-possession in a Chapter 11 and Chapter 12 may accept or reject an executory contract or lease.

To accept an executory contract or lease, the trustee or debtor-in-possession must provide adequate assurance that defaults will be promptly cured and adequate assurance of future performance. Sec. 365(b)(2).

Cure of default does not include defaults relating to the debtor financial condition, bankruptcy filing, appointment of a trustee or receiver or penalties arising from the default.

A Chapter 7 trustee must assume or reject within 60 days unless the bankruptcy court extends the time to assume or reject for an additional 60 days. Sec. 365 (d)(2).

In Chapter 11 and 12, the executory contract or lease can be assumed or rejected at any time before confirmation of a plan. Sec. 365 (d)(2).

Until the executory contract or lease is assumed or rejected, the trustee or debtor in possession must perform all of the debtor's obligations other than those in section 365(b)(2).

If an executory contract or lease is rejected the non-debtor lessor or lessee has an unsecured claim for damages arising from the rejection. Section 365(g)

A trustee or debtor in possession may assign an executory contract or lease after assumption, if the assignee provides adequate assurance of future performance, notwithstanding provisions of the executory contract or lease which restrict or prohibit assignment. Provisions which modify or terminate a lease as a result of an assignment under section 365 are not enforceable. Section 365(f).

Section 365(h) deals with real estate leases in which the debtor is a lessor. A debtor's rejection of a lease of real property does not deprive the lessee of possession, it merely relieves the debtor of the lessor's obligations and grants the lessee rights of set off against amounts due to the lessor.

Section 365(i) has similar provisions for real estate installment contracts in which the debtor is the seller and the non-debtor lessee is in possession.



# What is Chapter 12 Family Farmer Bankruptcy?



[Market Intel](#) / April 11, 2019

In recent months much attention has been given to the rise in Chapter 12 family farmer bankruptcies in portions of the U.S., e.g., [Farm Bankruptcies in 2018 - The Truth is Out There](#). On the legislative front, the [Family Farmer Relief Act of 2019](#) was introduced to help more family farmers reorganize and restructure their debt following several years of low commodity prices and [poor economic conditions](#) in agriculture.

Today's article provides a high-level overview of the Chapter 12 family farmer bankruptcy provisions. Farmers seriously considering Chapter 12 bankruptcy should work with their creditors and an attorney to establish and confirm a Chapter 12 plan.

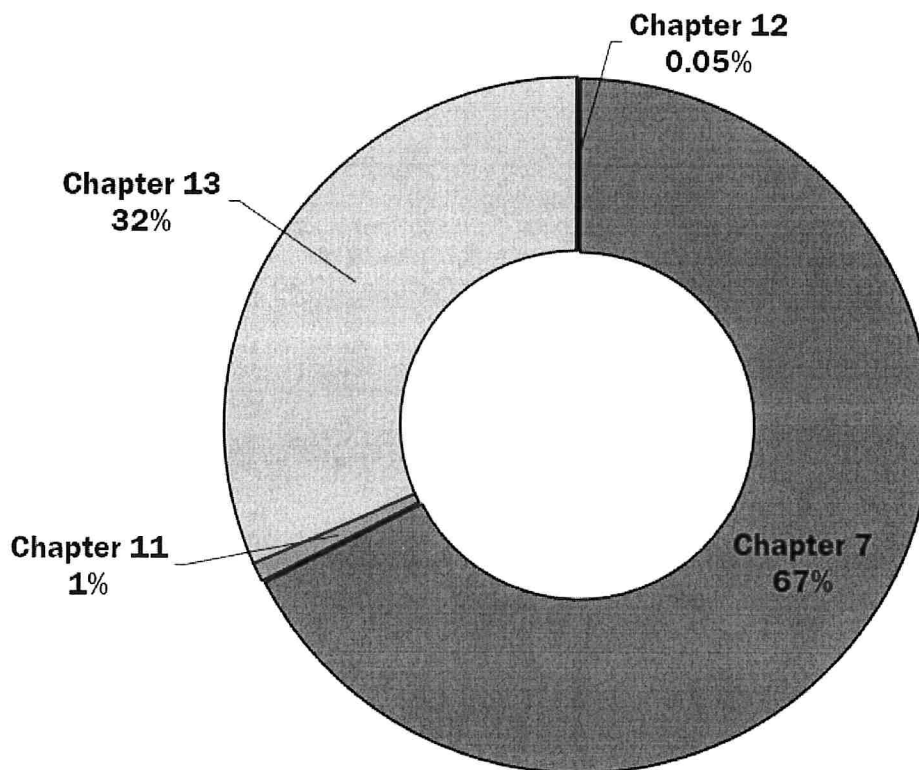
## What is Chapter 12 Bankruptcy?

[Chapter 12 bankruptcy](#) was created in 1986 in response to the poor economic conditions that plagued agriculture, including low commodity prices, low farm income, record farm debt and tight agricultural credit markets. Modeled after Chapter 13 bankruptcy, Chapter 12 provides reorganizational advantages and financial relief specifically for family farmers in debt. Those advantages include a seasonal repayment schedule over a three- to five-year period and lower costs

relative to other chapters. Filing under Chapter 12 provides a quick and predictable process for farmers to reorganize debt to avoid asset liquidation or foreclosure.

In 2018 there were 498 Chapter 12 bankruptcy filings, compared to nearly 766,000 Chapter 13 and Chapter 7 filings -- which are predominately consumer in nature. Over the last decade there have been more than 10 million total filings in Chapter 7 and Chapter 13, compared to 5,039 Chapter 12 filings. During this time, Chapter 12 bankruptcy filings have represented less than five-hundredths of a percent of total consumer and business bankruptcy filings, Figure 1.

**Figure 1. Share of Bankruptcy Filings by Chapter  
2009 to 2018**



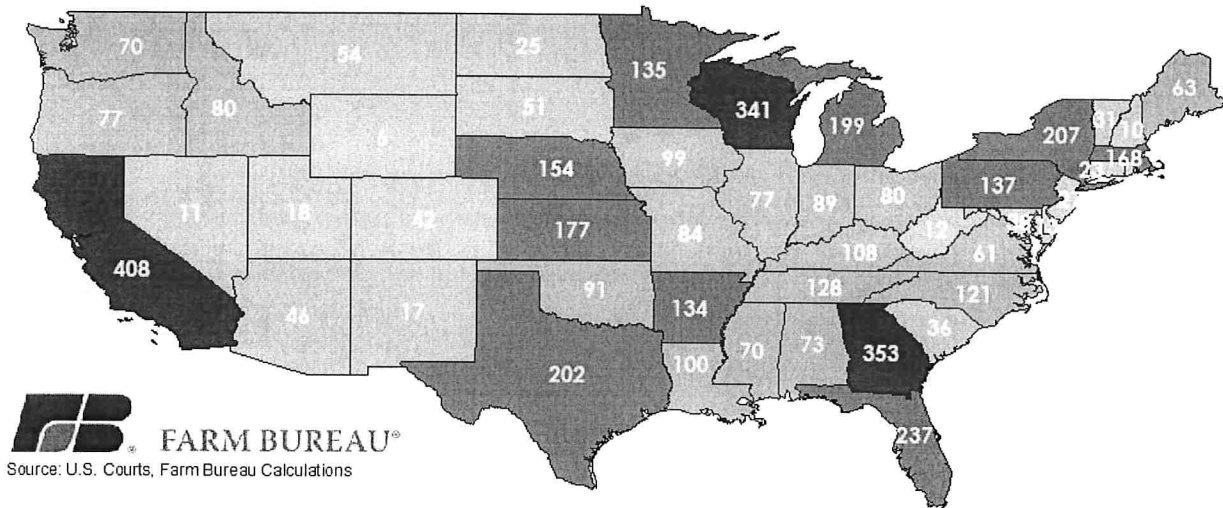
Source: US Courts, Farm Bureau Calculations

Expand Image

At 408, California has had the highest number of Chapter 12 filings over the last decade. Following California was Georgia at 353 filings and Wisconsin at 341 filings. Overall, Chapter 12 bankruptcies were the highest in the Midwest at 1,511

filings, followed by the Southeast at 1,484 filings. Figure 2 highlights Chapter 12 bankruptcy filings over the last decade.

**Figure 2. Number of Chapter 12 Bankruptcy Filings in Last Decade 2009 to 2018**



[Expand Image](#)

## Benefits of Chapter 12

There are several benefits associated with Chapter 12 bankruptcy filings.

First, debtors can cramdown debt on almost all secured debt (this is the only chapter that allows for cramdowns). A cramdown is when the debtor pays the present market value of a property rather than the whole debt during the bankruptcy filing process. For example, if a debtor owes \$20,000 on a loan after the accumulation of missed payments and interest and the underlying asset for the loan is worth \$15,000, the debtor can reduce - or cramdown - that debt to the base value of \$15,000.

Second, the farmer can propose a repayment plan to make installments to creditors over three to five years if the plan meets the requirements set forth in chapter 12. The creditor does not need to approve the plan, nor do they have the opportunity to vote against it. Additionally, there is no requirement for equal monthly payments, allowing for seasonal or balloon payments that align with the harvesting and marketing of agricultural commodities produced on the farm.

Third, the debtor may use, sell or lease property of the estate in the normal course of business without court approval. Additionally, if a farmer sells farm assets, the tax claims from those sales can be treated as unsecured claims and they may not

have to be paid in full or at all.

Finally, if the farmer is unable to complete the repayment plan due to medical illness or natural disasters, he may be eligible for a hardship discharge - effectively freeing him of remaining obligations.

Effectively, Chapter 12 provides farmers with more repayment flexibility than would be the case under Chapter 7 or Chapter 11 bankruptcy. The ability to make seasonal payments accommodates the reality of a farmer's fluctuating income and is not offered under any other chapter of bankruptcy. In addition, the fact that farmers can sell farmland and farm equipment free and clear of liens gives them more options to pay down their debts.

## Eligibility for Chapter 12

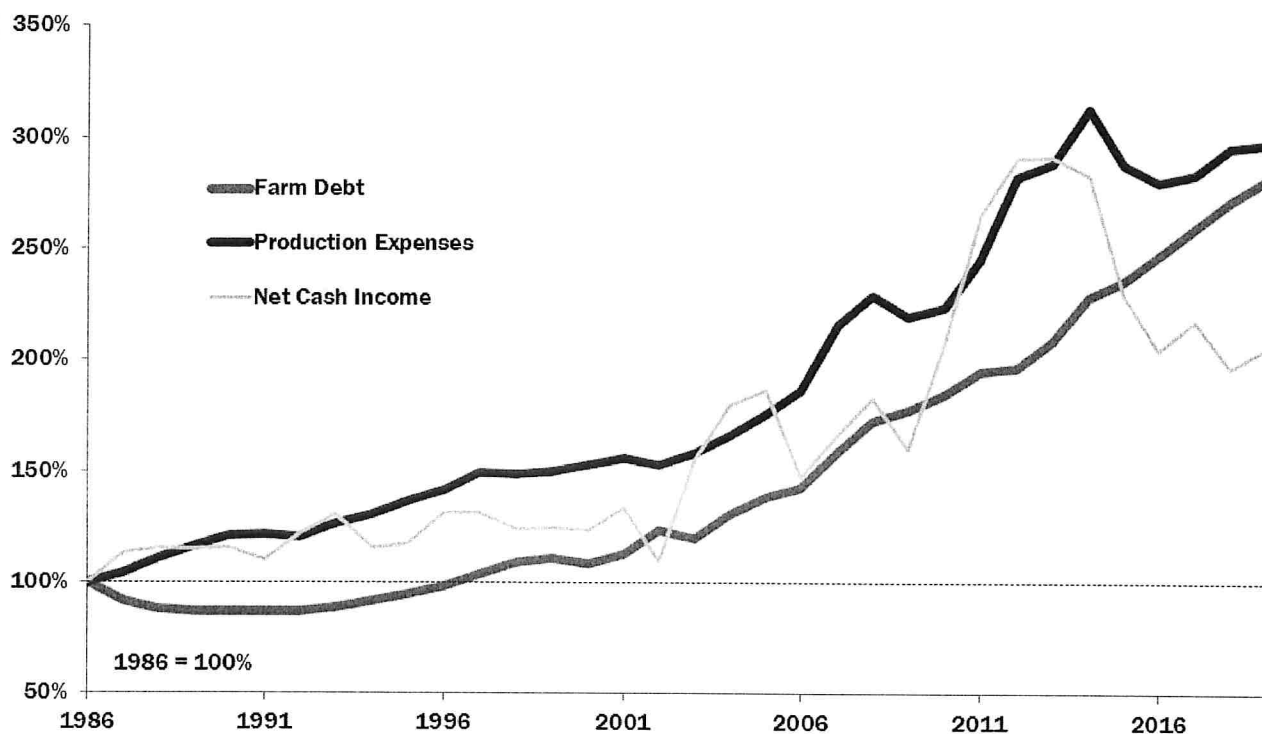
In discussions with farm lenders, Chapter 12 bankruptcy is generally considered the last resort for farmer debtors. First, lenders may seek to work with their farmer customers to find cost efficiencies, improve marketing and enhance the use of risk management tools. If Chapter 12 is used, farmers must meet the following criteria:

- The individual(s) must be engaged in a farming operation or commercial fishing operation.
- More than 50 percent of the gross income, i.e., income before taxes and other deductions, of the individual(s) for the preceding tax year must have come from the farming or commercial fishing operation. For family farmers, additional gross income criteria on prior tax years may also be evaluated relative to the gross income from farming.
- Total debts of the farm operation must not exceed \$4,153,150 for a farming operation.
- For family fisherman, the total debt must not exceed \$1,924,550 in inflation-adjusted dollars.
- At least 50 percent of the total debts that are fixed in amount, exclusive of debt for the debtor's home, must be related to the farming operation. For a commercial fishing operation, it's 80 percent.

## Is More Help on The Way?

Prior to 2005, the Chapter 12 liability cap was \$1.5 million, it was raised to \$3.2 million in 2005, and after adjusting for inflation now stands at \$4.2 million. Meanwhile, relative to 1986, and in nominal dollars, production expenses in agriculture have increased by 198 percent and farm debt has increased by 182 percent, while net cash income has experienced only half of that growth, Figure 3. As a result, the liability cap under Chapter 12 does not align with the modern credit and risk environment associated with family farming.

**Figure 3. Index of Farm Production Expenses, Total Farm Debt and Net Cash Income from Farming, 1986 to 2019**



Source: USDA ERS, Farm Bureau Calculations

Expand Image

To more properly align Chapter 12 laws with the modern credit needs of agriculture, the liability cap should be lifted. The Family Farmer Relief Act of 2019 will do just that by raising it to \$10 million in pre-inflation dollars. Recognizing that agriculture today is much different than in 1986 when Chapter 12 provisions were first introduced, the American Farm Bureau Federation supports lifting the liability cap.

## Take action here! Ask Congress to support changes to Chapter 12 Bankruptcy.

 \* \* \* \* city and state not required \* \*

**Find Legislators →**

- Send me emails about this campaign
- Send me text messages about this campaign

Share with Others

 [Twitter](#)  [Facebook](#)

© 2019. All rights reserved. Subject to [Privacy Policy](#).

### Contact:

John Newton, Ph.D.  
Chief Economist  
(202) 406-3729

[jnewton@fb.org](mailto:jnewton@fb.org)

Harrison Collins  
Public Affairs Assistant  
(202) 406-3624  
[harrisonc@fb.org](mailto:harrisonc@fb.org)

## Subscribe

Get Market Intel delivered to your inbox