

UNITED STATES BANKRUPTCY COURT

DISTRICT OF SOUTH DAKOTA

ROOM 211

FEDERAL BUILDING AND U.S. POST OFFICE

225 SOUTH PIERRE STREET

PIERRE, SOUTH DAKOTA 57501

IRVIN N HOYT

CHIEF BANKRUPTCY JUDGE

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June 19, 1997

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Subject: **Smith v. United States**
(In re Wilbur J. and Betty J. Smith),
Adversary No. 94-3010;
Chapter 12; Bankr. No. 87-30162

Dear Counsel:

The matter before the Court is Plaintiff's complaint seeking a declaratory judgment, damages, and attorney's fees. This is a core proceeding under 28 U.S.C. § 157(b)(2). This letter decision and declaratory judgment shall constitute this Court's findings and conclusions under F.R.Bankr.P. 7052. As set forth below, the Court declares that any lien that the Farm Service Agency (FSA) has on the Smiths' real property arising from the Smiths' Chapter 12 plan must be satisfied when the Smiths complete their Chapter 12 plan payments to the FSA. The Court further concludes that the present adversary proceeding is not the appropriate forum for this Court to determine the post-confirmation status of FSA's claim and the extent of its lien on Katcon's and the Smiths' real property pursuant to Katcon's confirmed Chapter 11 plan.

SUMMARY OF FACTS. The material facts are set forth in this Court's MEMORANDUM OF DECISION RE: MOTIONS FOR SUMMARY JUDGMENT entered July 24, 1995, and the Court's subsequent letter decision entered December 22, 1995 regarding Wilbur and Betty Smiths' MOTION TO AMEND DECISION. Curiously, although cross-motions for summary judgment were filed before this Court, the Smiths successfully argued before the District Court that issues of material fact existed regarding their commitment of their real property to the modified § 1111(b) treatment of FSA's claim in the Katcon Chapter 11 plan. Subsequent to the remand, this Court by letter dated January 29, 1997 cautioned counsel that jurisdictional problems were likely present because the parties were asking the Court to interpret Katcon's

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Chapter 11 plan through an adversary proceeding filed in the Smiths' Chapter 12 case. The parties decided to proceed with the adversary and, in lieu of a formal trial, the parties agreed to submit certain documents and depositions regarding Debtors' participation in the Katcon plan, which included the January 25, 1997 deposition of Richard J. Smith, a former related Chapter 12 debtor and a former shareholder and officer of Katcon; an affidavit by Gary Jackson, the Agriculture Credit Manager for FSA who administered the loan files of Katcon and the Smiths; an affidavit by Debtor Wilbur Smith; copies of the plans and related documents in the Smiths' Chapter 12 case and Katcon's Chapter 11 case; and some documents regarding FSA's recent foreclosure on Katcon.¹ The parties also filed a Stipulation of Facts that mirrored this Court's findings in the summary judgment memorandum.

The gist of this additional evidence, in the light cast by the Smiths, is that Wilbur and Betty Smith did not sign any documents in Katcon's Chapter 11 case or otherwise consent to their real property being included in FSA's modified § 1111(b) election in the Katcon plan. They and their son, Richard Smith, acknowledge that Wilbur Smith was the President of Katcon but state it was only a figurehead position. Richard Smith and Wilbur Smith further stated that Wilbur and Betty Smith did not own any shares of Katcon and that Richard Smith was the decision-maker for Katcon until 1991.² FSA argues that the Smiths' consent was not needed for FSA to exercise a § 1111(b) election in Katcon.

DISCUSSION. As this Court stated in a letter to counsel on January 29, 1997, under *Harmon v. United States*, 101 F.3d 574 (8th Cir. 1996), it is clear that a lien may be stripped down in a Chapter 12 case and that the lien is extinguished when the Chapter 12 debtor pays a secured claim in full. Thus, any lien that FSA has on the Smiths' real property arising from their Chapter 12 plan will be extinguished when the Smiths complete the plan payments on FSA's secured claim in the Chapter 12 case. That, however, does not fully answer the question presented in the Smiths' complaint. The Smiths also want this Court to declare that the Smiths' real property was not included as collateral in the

¹ Neither party clearly addressed why parole evidence should be received to interpret the plans.

² Even if the Court were to interpret Katcon's plan at this time, the affidavit of Wilbur Smith and the deposition testimony of Richard Smith would carry little weight because they are self-serving, despite Richard Smith's statements to the contrary, and have limited support in the record.

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modified § 1111(b) election that FSA made in Katcon's Chapter 11 case. That apparently is also the question of fact that the District Court remanded for this Court to decide.

This Court, however, does not have jurisdiction to interpret Katcon's Chapter 11 plan through this adversary filed under the Smiths' Chapter 12 case. As previously stated in the January 27, 1997 letter:

Had the *Harmon* decision been entered before this Chapter 12 related adversary was filed, the Court would have declined jurisdiction because *Harmon* decides conclusively all the Chapter 12 questions. The remaining issues are essentially only Chapter 11 post-confirmation matters in *Katcon* over which this Court may or may not have jurisdiction, especially if the issues go beyond interpreting this Court's prior orders in *Katcon*, and depending on the post-confirmation jurisdiction recognized in *Katcon*'s plan. See *In re Dakota Industries, Inc.*, Bankr. No. 87-40209, slip op. (Bankr. D.S.D. November 8, 1996). If this adversary is continued, the parties also will need to discuss whether *Katcon* and its principals must be brought into it since their interests may be affected. *Katcon*'s and Debtors' interests may be divergent and so they will need separate counsel. See *In re Black Hills Greyhound Racing Assoc.*, 154 B.R. 285, 292-93 (Bankr. D.S.D. 1993); and *In re Marolf Dakota Farms Cheese, Inc.*, Bankr. No. 89-50045, slip op. at 3-7 (Bankr. D.S.D. October 17, 1990).

While the Smiths' Chapter 12 case and *Katcon*'s Chapter 11 case were related -- a fact that the Smiths' Chapter 12 plan acknowledges -- and while the debt to FSA is the same in both cases, this Court and the parties cannot ignore the fact that there were two separate bankruptcy cases potentially involving the Smiths' real property as collateral for the FSA debt and that each plan may have created separate liens and obligations regarding that collateral. An adversary under the Smiths' Chapter 12 case is not the appropriate place to decide what liens, if any, may remain on the Smiths' real property pursuant to *Katcon*'s Chapter 11 plan and FSA's modified § 1111(b) election therein. If a party wants *Katcon*'s Chapter 11 plan interpreted to determine whether the FSA's modified § 1111(b) election covered both *Katcon*'s and the Smiths' real property, they will have to commence an appropriate action -- before this Court or

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another.³

This Court is reluctant to look past this jurisdictional problem for three reasons. First and foremost, FSA already has foreclosed on Katcon in District Court. Therefore, it appears that the District Court is [or was] the better forum for FSA to litigate the amount of their claim and the extent of the collateral that secures that claim pursuant to Katcon's confirmed plan. The status of the foreclosure action in District Court was not clearly presented to this Court until after the summary judgment motions were addressed.

Second, if a separate action is filed to interpret Katcon's plan, Katcon or its successor and principals can be included as necessary parties. This is especially important where Terence Smith may be personally liable for any deficiency on the Katcon debt, as stated in the District Court's Judgment of Foreclosure entered March 6, 1997, and where the amount of the deficiency may be reduced if the Smiths' real property is still collateral for that debt.⁴

Third, some preliminary questions must be answered before Katcon's confirmed plan can be interpreted and its binding effect established.⁵ These preliminary questions have not been addressed by the parties in the present action. Was Katcon's plan ever substantially consummated? See 11 U.S.C. §§ 1127(b) and 1141(a) and 1127(b); *Metropolitan Life Insurance Co. v. Olsen* (*In re Olsen*), 861 F.2d 188, 190 (8th Cir. 1988); and *United States v. Novak*, 86 B.R. 625 (D.S.D. 1988). Also, if Katcon did not continue in business post-confirmation, what is the status of Katcon's discharge? 11 U.S.C. § 1141(d). Finally, what is the impact, if

³ A bankruptcy court generally has jurisdiction to interpret its prior orders. 11 U.S.C. §§ 1141 and 1142 and 28 U.S.C. §§ 157 and 1334; see *Norwest Equipment Finance, Inc. v. Nath* (*In re D & P Partnership*), 91 F.3d 1072, 1074 (8th Cir. 1996); and *United States v. Unger*, 949 F.2d 231, 234 (8th Cir. 1991).

⁴ Wilbur and Betty Smith, Willard Smith, and Richard Smith received Chapter 12 discharges so they will have no personal liability on the FSA debt. 11 U.S.C. § 1228(a).

⁵ These preliminary questions were not addressed by the parties here but may already have been answered in part or sum during the Katcon foreclosure action -- another reason that this Court should not interpret the Chapter 11 plan at this time.

I hereby certify that a copy of this document was mailed, hand delivered, or faxed this date to those creditors and other parties in interest identified on the attached service list.
Charles L. Nail, Jr., Clerk
U.S. Bankruptcy Court
District of South Dakota

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By: Mr. Kay River
Date: 06-19-97

any, of *United States v. Unger*, 949 F.2d 231, 234 (8th Cir. 1991):

[W]here a trustee, custodian, or other person charged with the assets of the estate of a debtor deals with those assets in complete contravention of a confirmed plan, such assets remain effectively unadministered; they are in *custodia legis* of the bankruptcy court and property of the estate.

Id. at 234 (relying on the Act case of *United States v. Ivers*, 512 F.2d 121, 124 (8th Cir. 1975)). Only after these preliminary questions are answered can this or another court answer whether the Smiths' real property is covered by the modified § 1111(b) election in Katcon, whether the Smiths' consent for the election was necessary, and, if so, whether they in fact did consent. See also *American Bank and Trust Co. v. United States (In re Barton Industries, Inc.)*, 159 B.R. 954, 959-62 (Bankr. W.D. Okla. 1993); *Buckhead American Corp. v. Mulberry Chesterton Inn (In re Mulberry Chesterton Inn)*, 142 B.R. 566, (Bankr. S.D. Ga. 1992); *In re Depew*, 115 B.R. 965 (Bankr. N.D. Ind. 1989); *United States v. Standard State Bank*, 91 B.R. 874 (W.D. Mo. 1988), *aff'd on other grounds*, 905 F.2d 185 (8th Cir. 1990); compare *Derrick v. Richard L. Grafe Commodities, Inc. (In re Derrick)*, 190 B.R. 346 (Bankr. W.D. Wis. 1995).

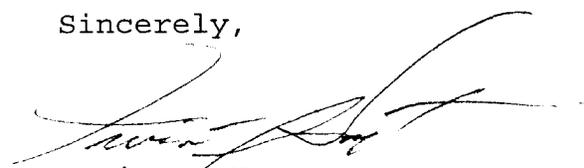
A declaratory judgment will be entered stating any liens that FSA has on the Smiths' real property arising from the Smiths' confirmed Chapter 12 plan must be extinguished when the plan payments on FSA's claim are completed. The judgment will also state that the status of any liens that FSA has on the Smiths' real property arising from Katcon's confirmed Chapter 11 plan will have to be decided in a separate proceeding. No costs or damages will be awarded to either party. FSA's reluctance to release the Smiths' liens is not a product of bad faith but arises from the parties' disagreement regarding Katcon's Chapter 11 plan, the § 1111(b), and its effect on the Smiths' real property.

NOTICE OF ENTRY
Under F.R.Bankr.P. 9022(a)
Entered

JUN 19 1997

Charles L. Nail, Jr., Clerk
U.S. Bankruptcy Court
District of South Dakota

Sincerely,



Irvin N. Hoyt
Chief Bankruptcy Judge

INH:sh

CC: adversary file(docket original; copies to parties in interest)

Case: 94-03010 Form id: 122 Ntc Date: 06/19/97 Off: 3 Page : 1
Total notices mailed: 5

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