UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA
Central Division

In re:	
ROSE RANCH OPERATING PARTNERSHIP, Employer's Tax ID No.46-0354920 Debtor,	Bankr. Case No. 90-30016 Jointly Administered Chapter 12
ROBERT HOUSTON ROSE MARGARET ROSE, Debtors,	MEMORANDUM OF DECISION RE: DISPOSABLE INCOME
AUGUST H. ROSE, a/k/a A.H. ROSE GLADYS C. ROSE Debtors.	

The matter before the Court is Trustee John S. Lovald's Motion to Dismiss for Failure to Complete Plan Payments. This is a core proceeding under 28 U.S.C. § 157(b)(2). This Memorandum of Decision and accompanying Order shall constitute findings and conclusions under F.R.Bankr.P. 7052. As set forth below more fully, the Court concludes that Debtors have not completed all plan payments because they owe $23,093.01 in disposable income.

I.

Debtors filed Chapter 12 petitions on April 10, 1990. On May 14, 1990, the three cases were ordered to be jointly administered. Debtors' plan was confirmed on July 9, 1991. The plan recognized two unsecured claim holders, the Farmers Home Administration [now the Rural Economic and Community Development Agency (RECD)] and the Small Business Administration, and provided that they would receive a "best interest of creditors" payment of

$110,000.00 divided *pro rata* and disposable income. The plan provided that disposable income, as defined by 11 U.S.C. § 1225(b)(1)(A) and (B), received between January 1, 1991 and January 1, 1994 would be applied to the plan.

Debtors filed their final report and account on May 2, 1994. Trustee John S. Lovald filed a Motion to Dismiss for Failure to Complete Plan Payments on May 26, 1994, and claimed all disposable income may not have been paid. RECD filed a joinder on May 26, 1995. Debtors filed a response on August 12, 1994, and claimed they had met the disposable income requirement.

After discovery and settlement attempts, an evidentiary hearing was held December 12, 1994. Appearances included Trustee Lovald, Assistant U. S. Attorney Thomas A. Lloyd for RECD, and James P. Hurley for Debtors. The matter was taken under advisement April 10, 1995 after receipt of briefs and after Attorney Hurley completed his final fee application.

II.

If the trustee or an unsecured creditor files an appropriate objection, a Chapter 12 debtor's plan must include a provision for paying any disposable income during the plan term to unsecured claim holders. 11 U.S.C. § 1225(b)(1). Payment of disposable income to unsecured claim holders is a requirement separate from the best interest of creditors test and serves a distinct purpose. *In re Wood*, 122 B.R. 107, 112 (Bankr. D. Idaho 1990).

Without regard to what creditors would receive in a

> liquidation setting, if a Chapter 12 debtor has the ability because of current income generated during the plan to pay the claims of unsecured creditors without jeopardizing his reorganization effort, the debtor should be required to do so. Otherwise, a debtor with little or no realizable equity in its assets could unjustly deprive creditors of the income enjoyed under a successful plan.

Id. at 112-13. It is designed to promote fairness and provide creditors "with an assurance that what can be done to protect their interests will be done. Disposable income is simply a measure of what can be done to promote fairness." *Rowley v. Yarnall*, 22 F.3d 190, 193 (8th Cir. 1994).

Disposable income is the difference between available income and necessary expenses during the disposable income payment period. 11 U.S.C. § 1225(b)(2). Available income includes all non exemptible funds and is not limited to income as defined by the federal tax code. *In re Martin*, 130 B.R. 951, 964-66 (Bankr. N.D. Iowa 1991). Necessary expenses are those "reasonably necessary . . . for the maintenance or support of the debtor [and his family]" or "the continuation, preservation, and operation of the debtor's business." *Id*. The disposable income payment period begins on the date that the first plan payment is due and ends three years later, or up to five years later if the term of the plan has been extended. 11 U.S.C. § 1225(b)(1)(B).

If a creditor or the trustee successfully argues that a Chapter 12 debtor has not paid all disposable income due under the plan, the debtor may not receive a discharge. 11 U.S.C. § 1228(a). The debtor has the ultimate burden of persuasion to show that all payments under the plan have been made, including payments of disposable income. *In re Kuhlman*, 118 B.R. 731, 738 (Bankr. D.S.D. 1990). Further,

> [w]hen a determination of disposable income is presented to the Court as a contested matter, each case must be examined upon the evidence presented. The Court will determine under the totality of the circumstances whether the debtor's expenses were reasonably necessary for family support and [the] continuation, preservation, and operation of the farm, as required by § 1225(b)(2). Factors the Court may consider include the amount of and reason for any variance in a debtor's actual income and expenses from those projected in the plan, the debtor's past borrowing practices, the availability of credit, and the necessity of any capital improvement.
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> Undocumented numbers or mere estimates of past years' income and expenses will not be accepted. Projections of income and expenses offered to show the funds needed to continue the operation (such as seed and fertilizer for the coming crop year) must be grounded on historical figures.
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> The trustee, as well as the Court and creditors, should be able to rely on the accuracy of the monthly and annual financial reports prepared by Debtors. . . . [A] debtor's failure to turn over disposable income or his efforts to hide assets or otherwise hinder the trustee's verification of financial information may constitute fraud.

Id. at 739.

In most Chapter 12 cases in which discharge is contested due to a debtor's alleged failure to pay disposable income, four questions need to be answered. First, what is the disposable income payment period? Second, what was the value of the debtor's cash, marketable commodities, and accounts receivable, including any earned but not-yet-paid government farm program payments, at the end of the disposable income period. Third, were any expenses incurred or capital purchases made during the disposable income period that were not in the ordinary course of business and which unnecessarily depleted disposable income? Fourth, what amount of income, if any, may be retained by the debtor as "reasonably necessary . . . for the maintenance or support of the debtor [and his family]" or "the continuation, preservation, and operation of the debtor's business," as permitted by § 1225(b)(2)? *In re Broken Bow Ranch, Inc.*, Bankr. No. 87-30137, slip op. (findings and conclusions entered on the record January 8, 1993 and order entered January 13, 1993), *aff'd, Broken Bow Ranch v. United States (In re Broken Bow Ranch, Inc.)*, Civ. No. 93-3016. slip op. (June 9, 1993), *aff'd, Broken Bow Ranch v. Farmers Home Administration (In re Broken Bow Ranch, Inc.)*, 33 F.3d 1005 (8th Cir. 1994); *In re Schmidt*, 145 B.R. 983, 987 (Bankr. D.S.D. 1991). The debtor's disposable income is then the value of cash, marketable commodities, and accounts receivable at the end of the disposable income period, plus any unjustified expenses or capital expenditures, less the funds necessary for the continuation of the business or family support.

III.

Based on applicable law and the evidence presented, the Court concludes that Debtors owe $23,093.01 in disposable income. The Court’s “Broken Bow” calculation is as follows:

CASH, MARKETABLE COMMODITIES, AND ACCOUNTS RECEIVABLE ON JAN. 1, 1994

Cash, operating account	$ 685.16
Cash, savings account	653.96
'93 unsold wheat	176,756.89
'93 calves	93,548.00
'93 gov't payments	2,833.00
'93 Co op dividend	563.23
	$275,040.24

UNJUSTIFIED EXPENSES OR CAPITAL EXPENDITURES

tractor purchase, 1993	$ 9,000.00
	$ 9,000.00

NECESSARY CARRYOVER FUNDS

CCC loan on wheat	$ 89,812.80
final plan payments-	
A.H. Rose	27,166.70
R.H. Rose	10,033.10
'93 federal income tax	
R.H. Rose	5,297.00
unpaid '93 operating expenses	6,418.06
atty fees from estate	45,958.87
first ½ real estate taxes	8,700.00
wheat sale expenses	5,180.14
calf sale expenses	365.00
RECD payment for 4-10-94	5,562.00
ASCS payment for 4-15-94	18,194.51
Northstream payment for 4-15-94	38,259.05
	$260,947.23

($275,040.24 + $9,000.00) - $260,947.23 = $23,093.01 in disposable income

Cash, marketable commodities, and accounts receivable on January 1, 1994. All parties used the actual sales prices to calculate the value of Debtors' 1993 wheat and calf crops. However, the market price for calves and wheat decreased after January 1, 1994. Consequently, the unsecured creditors would receive less disposable income if those sales figures were used. Therefore, the actual value of the marketable calves and wheat *on January 1, 1994* must be used.

Price fluctuations for marketable commodities often will occur between the end of the disposable income period and the date the debtor actually sells them. In some cases, the price will go up and the debtor will benefit. In other cases, the price obtained at a later sale date will be lower and the unsecured creditors would receive less in disposable income. The only fair method is to "snap shot" the value of marketable commodities on the last day of the disposable income period. Then the unsecured creditors are not financing the debtor's market speculation and the debtor is not deprived of any upturn in the market after the disposable income period ends.

To calculate the value of 1993 calves and wheat in this case, the Court used the actual sale prices obtained in January 1994, since they are close to the end of the disposable income period: $3.93 per bushel for wheat[1] and $514.00 per calf.

The parties agree that the values listed for cash, government farm program payments, and the Co op dividend are correct and the Court has used them. Debtors' feed inventory on January 1, 1994 is not included but may be retained by Debtors as a necessary carryover. Since herd bulls must be replaced regularly, the $5,000.00 deposit on bulls paid late in 1993 is allowed as a necessary, ordinary business expense.

Unjustified expenses and capital expenditures. It is undisputed that Debtors needed to purchase a tractor in 1993. The problem arises from their large cash investment. In contrast to the replacement of cull cows and bulls that is done annually, tractors and other major capital expenditures typically are not purchased with cash or over a short installment period. Some term of years is more reasonable. Here, Debtors' payment of $13,500.00

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[1] The Court was unable to adjust the wheat price for protein content because sufficient information was not provided.

in cash for one-half the tractor during the disposable income period and their request for the $13,500.00 balance as a necessary carryover fund are not reasonable nor fair to the unsecured creditors. In essence, Debtors are asking the unsecured creditors to finance the new tractor.

Since no evidence of a reasonable term of years for a capital expenditure of this type was offered, the Court used six years for its "Broken Bow" calculation. For 1993, $4,500.00 is allowed as a reasonable capital expense. The balance of $9,000.00 is included in disposable income. The requested carryover expense of $13,500.00 is not allowed since the second-half payment is not due until October 1994, when Debtors will again have marketable commodities available that can be sold to meet expenses.

Before Debtors make their disposable income payment, the parties may stipulate to another term of years for the tractor purchase. The term of years should be reasonable in light of the available credit at reasonable terms, the value of any trade-in, the life expectancy of the item purchased, and what the usual term of years is for such a purchase. The payment term is *not* a depreciation schedule, as used for tax purposes. If any party contests that six years is not reasonable and if an agreement cannot be reached, a separate evidentiary hearing on that issue may be requested.

The Court further concludes that the purchase of 40 heifers in November 1994 was an acceptable capital expenditure. The heifers replaced cull cows sold earlier in the year. The purchase did not substantially increase Debtors' herd size but kept the number consistent with the size when the plan was confirmed.[2] Debtors' post-trial brief adequately explains what funds were used to reduce Security Bank's claim at the beginning of the plan term.

Necessary carryover funds. Debtors' major sources of income are sales of wheat and calves. Both commodities can be marketed in the fall. Since all 1993 calves and wheat are considered "sold" on the last date of the disposable income term -- January 1, 1994 --, the Court must determine what income Debtors need to carryover until the next fall when marketable commodities will again be available. Both parties agree that carryover funds sufficient to cover the CCC loan on wheat, final plan payments, and 1993 income taxes are necessary. The Court further finds that carryover funds to meet expenses due in the first-half of 1994 are necessary. Included are one-half of the real estate taxes, the RECD payment due April 10, 1994, the ASCS payment due April 15, 1994, and the Northstream payment due April 15, 1994.

Two expenses related to the 1993 marketable commodities also are included. The Court has allowed carryover funds of $5,545.14 to cover trucking the wheat and calves to market. The income could not be realized without that expense. Calf feed expenses of

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[2] The Court would have preferred better evidence on this issue, including the number of culls sold each year of the disposable income term and the number of heifers retained or replacement cows purchased each year of the disposable income term. However, Debtors' numbers generally have been accurate and so their explanation has been accepted.

$3,814.89 is not allowed because the calves are presumed to have been sold on January 1, 1994. As noted earlier, the feed inventory on January 1, 1994 valued at $15,000.00 may be retained to feed the breeding herd.

The other 1993 expenses paid in January 1994 as requested by Debtors have been allowed as necessary carryover funds. Included are a hay trucking payment to Lonnie Roth, rent to Bill Rose, a fuel payment to Midwest Coop, and the balance on the replacement bulls to Kirby Briggs. One-half of the real estate taxes are allowed. The remainder of the taxes can be paid with 1994 income.

Other operating expenses, such as summer tilling, veterinary care, and additional feed must be borne by Debtors with income from government program payments or loans, miscellaneous income, or an operating loan that they may receive during the year.

Finally, the Court will allow carryover funds sufficient to pay Debtors' attorney's fees that are an allowed estate expense. This amount is $45,958.87 as determined by a separate Memorandum of Decision and Order entered today.

An appropriate order will be entered.

Dated this _____ day of July, 1995.

BY THE COURT:

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Irvin N. Hoyt
Chief Bankruptcy Judge

ATTEST:
PATRICIA A. JOHNSON, ACTING CLERK

By ____________________
Deputy Clerk

(SEAL)

UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA
Central Division

In re:	)	
	)	Bankr. Case No. 90-30016
ROSE RANCH OPERATING	)	Jointly Administered
PARTNERSHIP,	)	Chapter 12
Employer's Tax ID No.46-0354920	)	
Debtor,	)	
	)	
ROBERT HOUSTON ROSE	)	ORDER REQUIRING PAYMENT OF
MARGARET ROSE,	)	DISPOSABLE INCOME PRIOR
Debtors,	)	TO ENTRY OF DISCHARGE
	)	
AUGUST H. ROSE, a/k/a A.H. ROSE	)	
GLADYS C. ROSE	)	
Debtors.	)	
	)	

In recognition of and compliance with the Memorandum of Decision Re: Disposable Income entered this day,

IT IS HEREBY ORDERED that Debtors shall pay to Trustee Lovald $23,093.01 in disposable income before a discharge may be entered; and

IT IS FURTHER ORDERED that the amount of disposable income due may be adjusted if the parties in interest agree that a term other than six years for payment of a tractor purchased in 1993 should be used or if a different term is determined by the Court at a separate evidentiary hearing.

So ordered this _____ day of July, 1995.

BY THE COURT:

____
Irvin N. Hoyt
Chief Bankruptcy Judge

ATTEST:

PATRICIA A. JOHNSON, ACTING CLERK

By ________________________
Deputy Clerk

(SEAL)