

# Chapter 12 Basics

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# Today's Presentation

[www.woodsaitken.com/resources/bankruptcy/](http://www.woodsaitken.com/resources/bankruptcy/)



# Overview

- Chapter 12 Eligibility and Process
- Who Does Chapter 12 Help
- Operating in Chapter 12
- Preparing to Filing
- Chapter 12 Plan
- Keys to Plan Completion



# Chapter 12 Eligibility and Process

- The term “farming operation” includes farming, tillage of the soil, dairy farming, ranching, production or raising of crops, poultry, or livestock, and production of poultry or livestock products in an unmanufactured state

[11 U.S.C. 101(21)]



# Chapter 12 Eligibility and Process

- Engaged in a farming operation
- Aggregate debt not to exceed \$4,153,150 (§101(18)(A))
- Majority of debt from farming operation
- Majority of gross income from farming operation in preceding tax year or 2nd and 3rd preceding tax year



# Chapter 12 Eligibility and Process

- Filing of Petition
- 341 Exam
- Plan filing (120 days)
- Confirmation of Plan (no objections - 30 days)
- Plan duration (typically 3 years, can be up to 5 years)
- Discharge process (60 days)
- Final Report (90 days)



# Will Chapter 12 Help?

- Overview of operation: different bankruptcy issues arise with different operations
  - Annual and/or perennial crops, ranch, agistment/custom, contract, hogs, dairy
- Liquidation & cash flow analyses: project a 12
  - How much will have to be paid?
  - On what likely terms?
  - Does it look feasible?



# Will Chapter 12 Help?

- Liquidation analysis
  - FMV: then subtract secured claims, exemptions, costs of sale (10%), estimate tax consequences of sale
    - How much to unsecureds under this test?
- Cash flow analyses
  - Land debt: 15-30 years
  - Livestock: 5-12
  - M&E: 3-7
  - Till rate
  - State tax liens: statutory - 14%
  - Trustee fees
  - Real estate taxes



# Will Chapter 12 Help?

- Tax analysis - 1232
  - Has there been a sell down? Is a sell-down needed?
  - Are there loss carry forwards? (Maybe avoid 12)
  - Will more sell-downs likely occur?
- Executory contracts
  - Dependence on leased ground is risky
  - What (and how) are lessor relationships?
  - Are they leases or security devices?



# Will Chapter 12 Help?

- Cost of 12
  - Review attorney fees
  - Review 506 fees
  - Review trustee fees
- Weigh the possible outcomes, the risks, the costs
- Review alternatives



# Operating in Chapter 12

- How to operate in a 12? Where does money come from?
  - Off farm income
  - Services income - custom farming, yardage, etc
- Open account purchases: available? feasible?
- Use of cash collateral
- New secured financing



# Operating in Chapter 12

- Use of cash collateral
  - §§ 363 and 1205: creditor's consent or court order, i.e. adequate protection
  - Adequate protection in 12
    - Protect against decline in value of collateral (not necessarily extent of equity cushion)
    - Cash payment, replacement/additional lien; equity cushion
  - Compensation for Debtor: "The debtors are not slaves to the creditor." (Beck) Compensation available to debtors from collateral proceeds for labor, expenses, use of M&E



# Operating in Chapter 12

- Incurring secured debt: § 364
  - § 552 - Season for 12s: before annual crops are planted
    - Pledge prospective crop, assign crop insurance & USDA program payments
  - Alfalfa/perennial crops - prepetition lien continues (to some extent)
    - Difficult to pledge for new financing
  - Livestock: prepetition lien continues (to extent)
    - Operating funds typically more difficult to obtain
  - Subordination of original creditor to new lender
  - Family financing - available?



# Preparing to File

- Determine immediate needs
  - Time frames: Has ag lender sent notice of availability of farm mediation
  - Foreclosure, replevin, repossession
  - Reacquiring repossessed property is immediately expensive: file before taken
  - Cash collateral
  - Secured borrowing
- Avoid surprises: “You will be questioned under oath on the Schedules and SFA.”
- Have tax returns been filed?



# Some Initial Matters

- Summary of Operations for Trustee
- Proof of insurance
- Prior year return
- Motion to Employ Attorney
- Motion to Participate in Farm Service Agency Programs
- Assumption of executory contracts for land
- CPA statement on liquidation consequences



# Chapter 12 Plan

- Address all Secured Creditors and all classes of creditors (similar to a Chapter 11 Plan)
- Provide all information from Local Rule 3015
- Communicate with secured creditors
- Make sure plan is feasible
- No voting process



# LR 3015-1 Highlights

- 1. A statement disclosing any change of the debtor's assets or liabilities from the date of filing of the petition through the date of the filing of the plan.
- 2. A cash-flow projection for the year immediately following confirmation of the proposed plan, including and identifying the debtor's farm and non-farm income sources.
- 3. Assumptions and sources upon which the cash-flow projection is based, with historical or other data justifying such assumptions.



# LR 3015 Highlights

- 4. Farm income and expense information in a form comparable to Internal Revenue Code Schedule F forms filed by the debtor for the previous four years plus a statement of the debtor's non-farm income for the tax year preceding the filing of the motion.
- 5. Projected administrative expenses, including attorney fees.
- 6. A plan summary indicating the dates, amounts, and payees of all amounts to be paid under the plan as provided by the Chapter 12 trustee.
- 7. If the plan proposes the sale of assets, a statement from a qualified tax accountant or attorney, setting forth the probable tax consequences thereof.
- 8. The basis of any valuation of property, including names of appraisers and dates of appraisal, if any.



# LR 3015 Highlights

- 9. A statement with detailed information, specifying the need for the plan payments to be made over a period longer than three years.
- 10. If the debtor proposes to retain secured property, a statement itemizing such property, the value of the property, and the basis of the valuation estimate.
- 11. A liquidation analysis sufficient to show compliance with 11 U.S.C. § 1225(a)(4), including a statement from a qualified tax accountant or attorney as to tax liabilities from liquidation, if any.
- 12. A projected disposable income statement for the term of the plan.



# CHAPTER 12 PLAN

§ 1222 - Power to repay secured creditors beyond life of the plan. Amortization factors may include

- type of collateral,
- length of useful life,
- original term of loan,
- nature of current commercial market,
- balloons, interest rate windows, drop deads, etc.



# CHAPTER 12 PLAN

## § 1225 - Secured claims

- Consent of creditor
- Present value with retention of liens: *Till* Rate (presumptive 2% above national prime)
  - Land debt: 15-30 years
  - Livestock: 5-12
  - M&E: 3-7
  - State tax liens: statutory - 14%
- Surrender
- Cure default and retain contract terms



# CHAPTER 12 PLAN

## § 1225 - Unsecured claims

- Liquidation test
  - FMV less secured claims, exemptions, costs of sale, tax consequences of sale
- Ability to pay
  - Pay full value
  - Submit quarterly reports to trustee to determine disposable income
  - Project and pay 3-5 years of disposable income (No quarterly reports)
  - Disposable income excludes amounts needed to farm



# Chapter 12 Plan

§ 1232 - Allows Chapter 12 debtor to strip certain claims of their priority:

- Any unsecured claim of a governmental unit
- Arising before 12 is filed or after, and before discharge under § 1228
- Arises out of sale, transfer, exchange or other disposition
- Of any property used in the debtors farming operation

Potentially powerful tool for sell-down reorganizations



# Chapter 12 Plan

## § 1232

- Does not apply to secured claim
- Compute amount subject to 1232 using marginal method
  - Two returns: actual and pro forma (exclude qualifying sales) with difference being general unsecured amount
- Timing of post-petition sales relative to discharge
  - May need to consider extending plan to 4 or 5 years
- 1232 provides notice procedure for use



# Chapter 12 Plan

- Review of sample plan



# Keys to Plan Completion

- Full Disclosure
- Communication



# Role of Chapter 12 Trustee

- Conduct 341 Exam
- Advocate for unsecured creditors
- Review of Plan
- Monitoring and making Plan Payments
  - Unsecured
  - Modified debt
- Review of Fee Applications
- Review for discharge/plan compliance
- Monitor and report bankruptcy fraud
- Monitor case progression



Questions?