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DEC 7 2004

UNITED STATES
BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

UNITED STATES BANKRUPTCY COURT
IN AND FOR THE DISTRICT OF ARIZONA

In re KURT L. DEMBAUGH and,
ROBBIE L. DEMBAUGH,

Debtors.

Chapter 13 Proceedings
Case No. 2-04-08750-PHX-CGC

**UNDER ADVISEMENT DECISION
RE: MOTION FOR RELIEF FROM
STAY AND OBJECTION TO
SECOND AMENDED PLAN**

M&I Marshall & Ilsley Bank ("M&I") seeks stay relief to foreclose its lien on Debtor Kurt and Robbie Dembaugh's ("Debtors") home and for an order of this Court denying confirmation of Debtors' Second Amended Chapter 13 Plan. At the last hearing before the Court on October 7, 2004, the Court consolidated the stay relief and confirmation proceedings and instructed the parties to file simultaneous briefs on the legal issues to be decided. That having been done, the matter is now ripe for adjudication.

The underlying facts are not in dispute. M&I holds and first and second lien position on Debtors' home. The first lien is apparently in arrears for approximately \$5,338. Debtors intend to cure this default under the Plan within 26 months. The second position lien was originally for \$40,000 with an interest rate of 10.5%. Debtors were required to make a final balloon payment on December 10, 2002, with respect to this second position lien.¹ According to M&I, the amount now owing and in default is \$42,321.51, which includes principal of \$35,010.57, accrued interest, late fees, miscellaneous fees, and attorneys' fees and costs. While Debtors say they are using the loan balance M&I sets forth in M&I's original motion to lift stay for purposes of their arguments here, that amount is only \$40,770.73 and apparently does not take into account accrued interest from the time the motion to lift stay was filed to the time the post-hearing briefs were filed. According to M&I, that amount now owing is actually

¹Although Debtors claim they were surprised to learn the loan had a balloon payment obligation, they do not challenge the existence of the obligation.

1 \$42,321.51. Putting aside this discrepancy, the Court concludes that the Plan is not
2 confirmable.

3 With respect to M&I's second lien, Debtors' Plan proposes to pay M&I \$400 a month
4 for 36 months with interest at 4.5%. Thereafter, Debtors propose to pay the balance of M&I's
5 claim (estimated to then be around \$31,000) on or before the 36th month through a refinance,
6 or if necessary, the sale of the home.

7 M&I objects because the Plan seeks to modify its claim without satisfying the
8 requirements of 11 U.S.C. section 1325(a)(5), which provides that with respect to "each
9 allowed secured claim . . . the plan provides that the holder of such claim retain the lien
10 securing such claim; and . . . the value, as of the effective date of the plan, of property to be
11 distributed under the plan on account of such claim is not less than the allowed amount of such
12 claim." According to M&I, the Plan proposes to distribute less than the allowed amount of
13 M&I's claim by only paying M&I \$14,400 over the 36 months of the Plan. The remaining
14 amount owed (in essence a balloon payment of over \$30,000) is subject to a speculative
15 refinance or sale of the property at the end of the Plan period. Further, according to M&I,
16 there is no support for Debtors' position that there will in fact be \$36,000 in equity at the end
17 of the Plan. M&I also contends that the \$30,000 balloon payment is unlikely to be paid from
18 any other source than a refinance or a sale because Debtors cannot show they will have a
19 sufficient income at the end of the Plan to make this payment without a refinance or sale.

20 In response, Debtors contend that the home is currently worth \$215,000 with liens
21 totaling approximately \$173,000 in favor of M&I by virtue of its first (\$136,000) and second
22 (\$37,000) lien positions. Therefore, Debtors calculate their equity in the property at \$42,000.
23 Further, after making all Plan payments, the amount owing M&I on its claim will be reduced
24 to about \$31,000. In addition, the value of the property will also have presumably increased
25 and the overall debt to M&I on the underlying mortgages will have decreased by virtue of the
26 continuing monthly payments on the mortgages. Overall, Debtors' equity position will be
27 even greater at the end of the 36 month period, adequately protecting M&I and guaranteeing
28 Debtors the ability to pay off the arrears by either refinancing or selling the home.

1 With respect to the interest rate being reduced from the contracted 10.5% to 4.5%,
2 Debtors contend that the Court can approve a change in rate based on the prevailing market
3 rate and the risk factors involved to determine an appropriate rate under the circumstances.
4 Further, where Debtors are not in fact curing the default, but instead paying the entire claim of
5 M&I, the restrictions of 11 U.S.C. section 1322(c)(2) do not apply.

6 To begin with, Debtors' math seems a little off. Debtors represent that their house is
7 currently worth at least \$215,000. They contend that they owe M&I \$136,000 on M&I's first
8 position lien and \$37,000 on M&I's second position lien for a total debt owing of \$173,000.
9 According to Debtors, their current equity in the home is \$42,000. M&I, however, states its
10 liens against the property total of \$184,386.25, leaving approximately \$30,613.75 in equity.
11 Debtors' current equity interest therefore lies somewhere between \$30,613 and \$42,000 and
12 will presumably increase as Debtors' make their Plan payments and thereby reducing the debt
13 on the second position lien to approximately \$31,000. Regardless of the exact numbers,
14 however, it's a close call to say the least whether Debtors will have sufficient equity to cover
15 the \$31,000 lump sum payment.

16 The balloon payment alone at the end of the Plan does not automatically lead this Court
17 to reject Debtors' Plan. It is instead the lack of any evidence that Debtors will be able to
18 refinance the loan, sell the property or otherwise pay the \$31,000 on their own that leads to its
19 failure. When feasibility is questioned, Debtors must come forward with some evidence to
20 show the Plan is likely to succeed. *See Fantasia v. First National Bank of Boston*, 211 B.R.
21 420 (1st Cir. BAP 1997). In situations where debtors propose a balloon payment, courts have
22 looked to a variety of factors to analyze the Plan's feasibility, such as

- 23 (1) the equity in the property at the time of filing;
- 24 (2) the future earning capacity of the debtor;
- 25 (3) the future disposable income of the debtor;
- 26 (4) whether plan provides for the payment of interest to the secured
27 creditor over the life of the plan;

1 (5) whether the plan provides for payment of recurring charges against
2 the property, including insurance, local property taxes and utility
3 charges; and

4 (6) whether the plan provides for substantial payments to the secured
5 creditor which will significantly reduce the debt and enhance the
6 prospects for refinancing at the end of the plan.

7 *Id.* at 423. Other than pointing to the alleged equity that will exist, Debtors have provided
8 little else to convince this Court that they will in fact be able to refinance or otherwise sell the
9 property for an amount sufficient to pay M&I.

10 Simply stating that they will either refinance the property or sell it sometime within the
11 next three years is not enough. Debtors have provided no evidence that they will be able to
12 refinance the house in 36 months, whether by presenting a lender willing to refinance the
13 property or by showing that they will have sufficient income to qualify for a new loan.
14 Whether the home can be sold for enough to also cover the balloon payment is somewhat
15 speculative. While no one has challenged Debtors' representation that the house is worth at
16 minimum \$215,000 today, no evidence of value has been provided.

17 Further, Debtors' schedules indicate that Debtors' future earning capacity is far from
18 solidified. At the time Debtors filed their Schedule I, Mr. Dembaugh had been self-employed
19 as a woodworker for one month, listing his income at \$1,500 a month. Whether this self-
20 employment will continue, will be successful, or will increase is, at this early stage, anyone's
21 guess. Schedule I seems to further indicate that this \$1,500 is without any federal or state
22 deductions, which would further reduce his net monthly income. Ms. Dembaugh in turn nets
23 \$2,732 a month. Their total monthly expenses are listed as \$3,636, without including their
24 Plan payments. To be gentle, they are living on the margin. Will this income be sufficient to
25 allow a refinance? The Court is left to guess. Certainly, Debtors will not have the funds to
26 pay the \$31,000 themselves if a refinance or sale does not happen.

27 The Plan also fails to provide any sort of game plan to refinance or sell the property,
28 other than stating that it will happen "on or before the 36 month." When will Debtors begin

1 trying to refinance or sell the property? In addition, while property values have as a general
2 matter increased over the years, there are no guarantees. There are similarly no guarantees
3 that interest rates will remain low, a more favorable factor to allowing Debtors' to refinance.
4 The overall Plan payments on this debt are also fairly minimal, accounting for only a 34%
5 reduction of the debt owed (\$14,400 of the \$42,000 owed will be paid).

6 For these reasons, the Court finds the Plan unfeasible, and confirmation on these terms
7 is denied. The Court further orders that the automatic stay shall remain in effect for the next
8 sixty (60) days to allow Debtors additional time to file an amended plan. Debtors shall remain
9 current to M&I on all postpetition payments during this time. If an amended plan is filed, the
10 Court shall hold a plan confirmation hearing on **March 1, 2005, at 11:00 a.m.**, at the United
11 States Bankruptcy Court, 201 N. Central Ave., Phoenix, Arizona.

12 So ordered.

13 DATED: Dec. 7, 2004

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15 
16 CHARLES G. CASE II
UNITED STATES BANKRUPTCY JUDGE

17 COPY of the foregoing mailed or sent
18 via facsimile this 7th day of
19 December, 2004, to:

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10
11  A handwritten signature in cursive script, appearing to read "G. Maney", is written over a horizontal line. The signature is positioned to the right of the line number 11.

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